

The Decline of Correspondent Banking in Pacific Island Countries

Technical Paper 3: Literature Review of extent and impact of CBR decline on Pacific Island Forum countries

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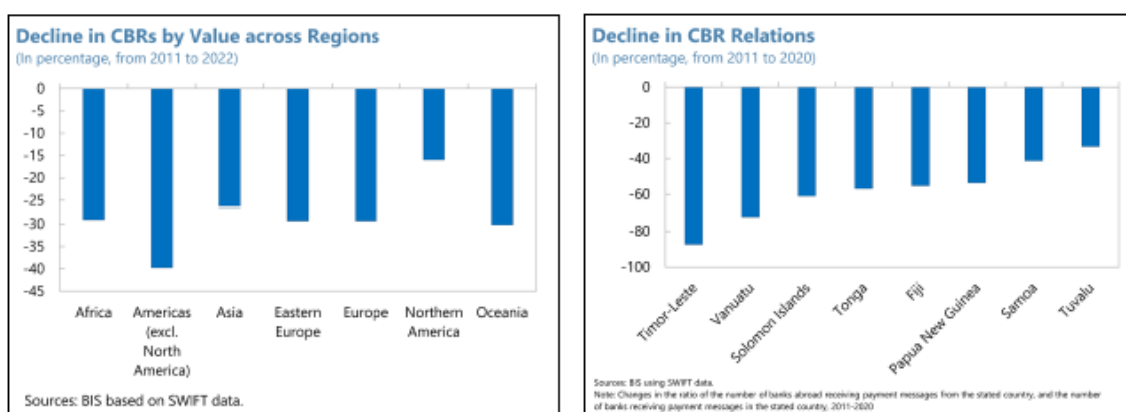
1 Overview

The purpose of Technical Paper 3 is to present the information available from previous studies on the extent and impact of de-banking on Pacific Island Forum members. Section 1 summarises the information that is available regarding changes in CBRs by region and corridors, the observed impact on the banking sector, remittances and trade finance, and the extent of PI countries' compliance as reported by FATF. Section 0 provides a summary of the position of individual PI Forum countries in regard to CBRs, drawn from published sources and the results of the survey described in TP5. Section 3 sets out the detailed information and sources publicly available for each country.

1.1 Changes in CBRs and payment corridors

A March 2023 IMF Article IV study reported on the loss of CBRs by region and by countries within the Oceania region. This study found that while the percentage reduction in CBRs over the period 2011 to 2020 was greatest in the Caribbean, the situation for some individual Pacific Island countries is severe given the few CBRs left - just one in the case of Tuvalu – see Figure 1 (IMF Mar 2023).

Figure 1: Decline in CBRs



Source: IMF March 2023

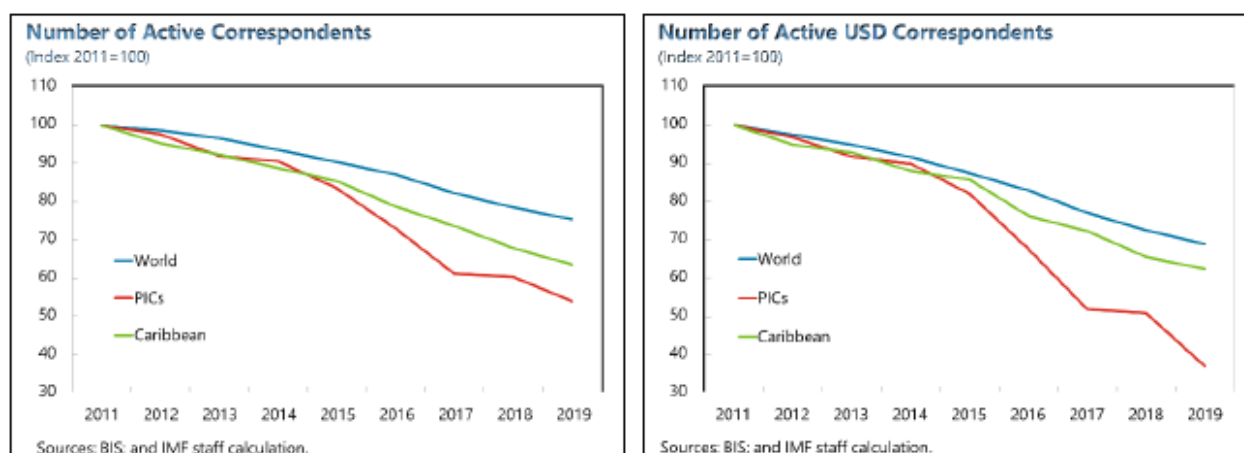
Indeed, in its 2021 analysis of correspondent banking, the Reserve Bank of New Zealand noted that the inclusion of Australia and New Zealand in the Oceania region tends to mask the disproportionate effect of de-banking on small Pacific Island nations (Reserve Bank of New Zealand 2021).

The impact of continued de-banking on Pacific Islands countries in particular has been a source of considerable concern due to the large reduction in numbers of CBRs in the region coupled with the lower absolute number of CBRs held by banks to start with.

Moreover, banks are sometimes given little warning or information on the reason for the withdrawal of a CBR (WB 2018).

A 2021 Article IV study by the IMF found that the loss of CBRs in Pacific Island countries was worse than for the Caribbean in recent years and had been accelerating – see Figure 2 (IMF Sep 2021).

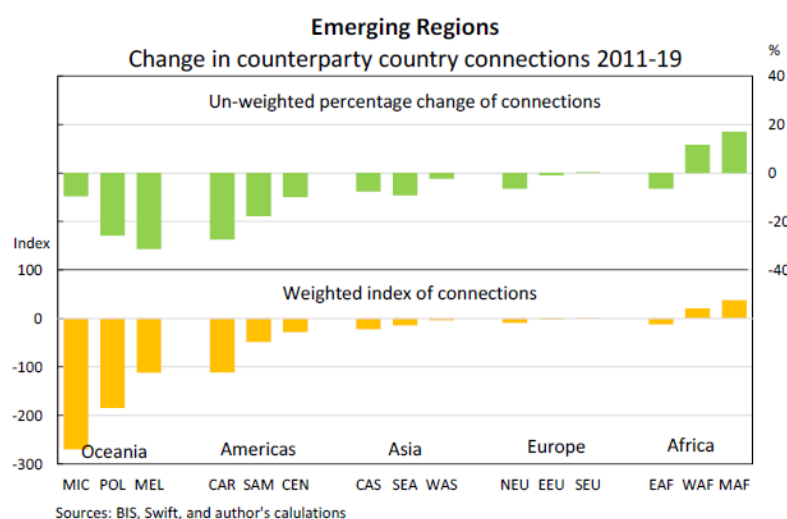
Figure 2: Indices of Active Correspondents



Source IMF March 2021

An unpublished paper by Chris Becker sought to identify countries' vulnerability to the further loss of CBRs by taking account of the absolute number of CBRs in each country. His paper began by identifying within-region disparities in banking connectivity by adjusting for trend declines in CBRs (Becker 2023b).

Figure 3: Change in counterparty countries

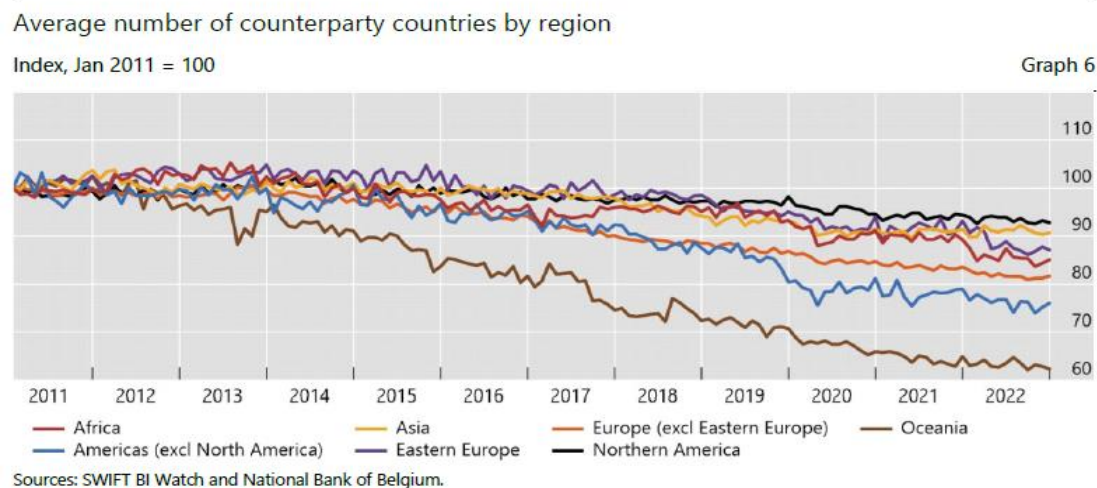


Source: Becker 2023b

In Figure 3, the top (green) section of the figure shows the percentage change in CBRs for three countries within each region relative to a numeraire that represents the most connected country in the region. In the case of Oceania, the numeraire is Australia. The intention of this adjustment is to standardise for the world-wide trend reduction in CBRs. The bottom section of the figure (in yellow) then weights the relative change in counterparty connections by each country's degree of connectivity (measured relative to the connectivity of the numeraire country). On this basis, recent de-banking can be seen to have had a disproportionate effect on three sub-regions within Oceania, namely Micronesia, Polynesia and Melanesia.

Moreover, the loss of CBRs tends to be accompanied by a loss of cross-border payment corridors. Analysis of Swift data by CPMI revealed steady declines in the number of counterparty countries over the period 2011 to 2020, with Oceania experiencing the greatest losses (CPMI 2021).

Figure 4: Average number of counterparty countries by region



Source: CPMI 2023

Rice et al. agree that corridors tend to disappear as banks cut respondents, albeit at a slower rate. Their analysis suggested country corridors reduce at about half the rate at which CBRs cease (Rice et al 2020). They found that a complete loss of access to a corridor is rare but the length of payment chains can increase as transfers are routed via third countries. Longer payment chains in turn raise the possibility that the costs of cross border intermediation increase with the loss of CBRs.

1.2 Impact on banking sector, remittances and trade finance

Banks

Table 1 shows the composition of the financial sector for those selected Pacific Island countries covered by the 2022 World Bank study.

Table 1: Composition of financial sector for selected Pacific Island countries

Country	Commercial banks	Insurance companies	Insurance brokers	Money transfer/fx dealers	Other financial institutions	Total
PICs with central banks						
Fiji	6	9	4	11	19 ⁷	49
Papua New Guinea	4	5	4	10	50 ⁸	73
Samoa	4	6	4	13	4	31
Solomon Islands	4	4	6	13	13 ⁹	40
Timor-Leste	5	3	-	12	3 ¹⁰	23+
Tonga	4	-	-	11	-	15
Vanuatu	4	34	-	-	10 ¹¹	48
PICs without central banks						
Federated States of Micronesia	2	-	-	-	-	2
Palau	5	-	-	-	3 ¹²	8+

Source: Asian Development Bank

Source: World Bank June 2022, using ADB data

In many of the Pacific Island countries foreign-owned banks have a substantial presence. In the past this has been a strength, with foreign banks contributing technology, staff and capital to domestic financial systems (IMF Mar 2023). However, it has also exposed the Pacific Island countries to the risk of loss of financial capacity if de-banking leads to the withdrawal of a foreign-owned bank from operating within the country (World Bank 2022). ANZ is now the only one of Australia and New Zealand's "big four" banks that maintains a presence in the Pacific Island countries,¹ and the resultant loss of competition and increase in concentration in banking is seen as an unintended and undesirable consequence of derisking (Coyne 2022). The increase in concentration in the banking sector is seen as likely to increase costs and add to market and systemic risks (IMF Mar 2023)

Particular examples where concerns have been raised about the concentration of US dollar cross-border payments include the Marshall Islands, whose only domestic bank faced the possibility of termination of its sole CBR in 2014— avoided only by the intervention of US agencies (IMF Sep 2018). Another example is Tuvalu, which has only one CBR (IMF Mar 2023).

There is concern also that the withdrawal of CBRs will force banks and their customers to use informal and/or unregulated payment channels that could facilitate money laundering (IMF Mar

¹ Westpac sold its Cook Islands, Samoa and Tonga operations to Bank of South Pacific (BSP) on 14 July 2015 for A\$91m (Westpac 2015).

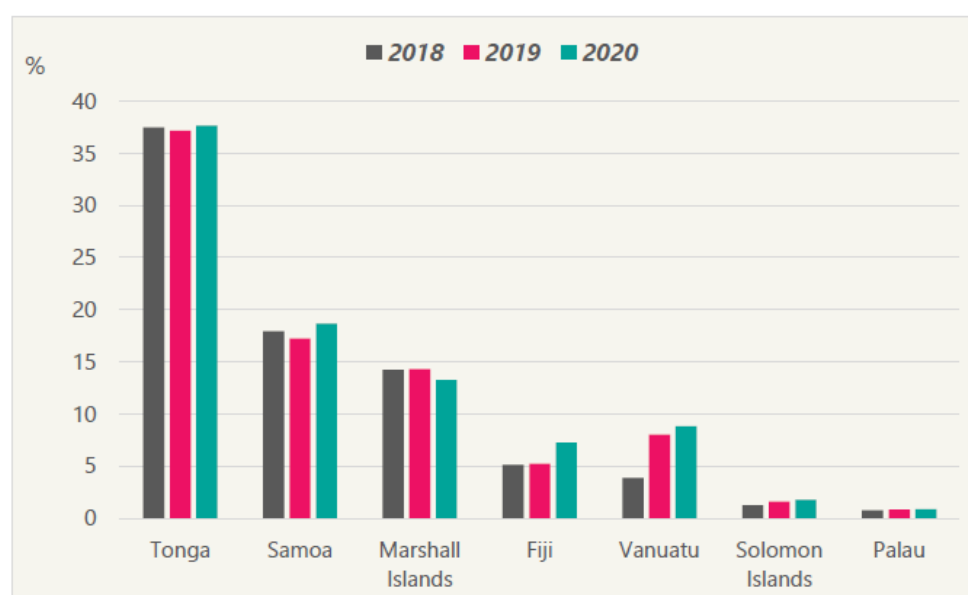
2023, RBNZ 2021). In high-risk countries, such as Syria and Somalia, money transmitters (MTOs) and non-profits have been forced to use nonbanking channels which are inherently more risky. Examples extend to representatives of non-profits carrying suitcases of cash, creating dangers for couriers and agents, and a lack of transparency on the use of the funds (GOA 2021).

In the Pacific the consequences have been much less extreme. There has been some proliferation of smaller MTOs, and concern that some of the new entrants undertake insufficient due diligence and hence create new vulnerabilities to money laundering (Coyne 2022). In addition, ongoing loss of CBRs increases the fragility of financial system and raises the risk that a Pacific Island country could end up in the catastrophic position of losing their last CBR (RBNZ 2021).

MTOs and Remittances

A function of CBRs which is particularly important for many Pacific Island countries is enabling the transfer of remittances. Remittances are a key source of foreign exchange and support the livelihoods of thousands of households (PIRI 2022, Boulton and Winton 2018). Figure 5 shows remittances as a share of GDP for a selection of Pacific counties (RBNZ 2021).

Figure 5: Remittances as a share of GDP



Source: RBNZ 2021

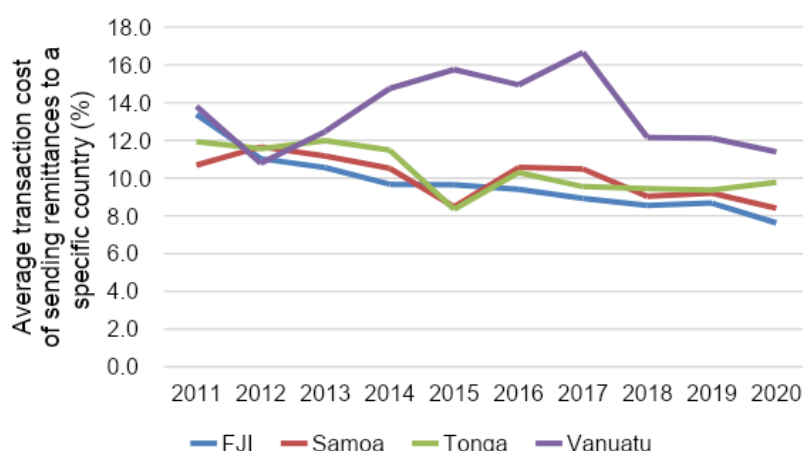
The role of remittances is quite variable across Pacific Island countries, with PNG being a net exporter of remittances, (RBNZ 2021, PIRI 2022). The impact of COVID-19 has accentuated the importance of remittances even further, so that by 2021 Tonga and Samoa remittances accounted for some 39% and 25% of GDP respectively (Capal 2022).

However, MTOs are vulnerable to closure of CBR services because ideally they require a bank account to complete their cross-border transfers (unless they also resort to cash couriers). MTOs typically aggregate many small payments, usually less than \$500, for cross-border payments, primarily for migrant populations. Concerns that MTOs handle higher risk transactions while not maintaining sufficient anti-money laundering and combating of terrorist and proliferation financing measures, have given rise to risk concerns by banks. These concerns are elevated by the fact that MTOs are not subject to comprehensive financial regulation and supervision (Boulton and Winton

2018, GAO 2021). Despite this, AUSTRAC has assessed the ML/TF risk to be low for remittance providers handling remittances from Australia to the Pacific Islands (AUSTRAC 2017).

Various commentators have noted that, despite the closure of CBRs, remittances to the Pacific Island countries have continued to grow in value and volume, and that where MTOs had bank accounts closed they were able to find a replacement (Boulton and Winton 2018, IMF Sep 2018). Likewise, the cost of remittances has been falling over recent years in most Pacific Island countries. The margin between the cost for bank versus MTO transfers has reduced from some 7 to 8% to 2 to 3%. (Capal 2022, PIRI 2022). Figure 6 shows a declining trend of average cost for Fiji, Samoa and Tonga, with the more variable pattern for Vanuatu being influenced by its FATF grey-listing in 2016 and de-listing in 2018.

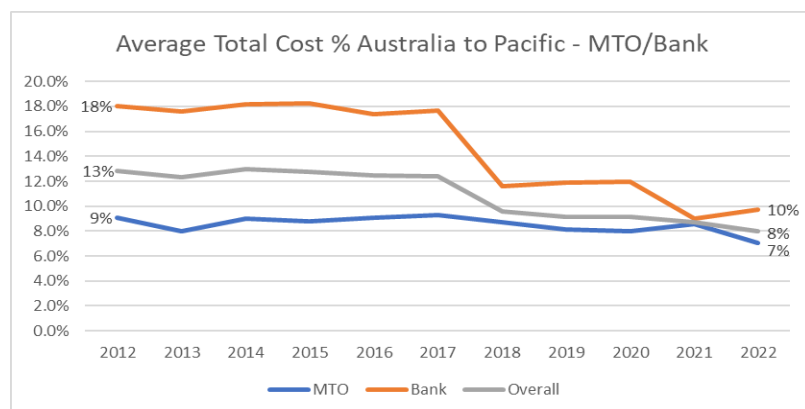
Figure 6: Remittance costs – average all channels



Source: PIRI 2022

Figure 7 shows the declining cost of bank transfer fees relative to the more steady level of MTO fees.

Figure 7: Remittance costs – average all channels



Source: Capal 2022

Some authors have concluded from this that the effect of the loss of CBRs on remittances is uncertain or not material (IMF 2018). However, others have noted that the cost of sending cross-border remittances is much higher in Pacific Island countries than elsewhere (Boulton and Winton 2018, Rice et al 2020). Analysis of 194 countries by Rice et al found that all instances of rising remittance costs were associated with lost CBRs, and that remittance costs fell by less when CBRs

were in retreat (Rice et al 2020). Analysis undertaken in TP6: Empirical Analysis shows that the cost of remittances is indeed considerably higher in the countries for which data is available, when compared to South East Asia and South Asia.

1.3 Effect on trade

The impact of loss of CBRs on trade and FDI flows is even more difficult to assess. IMF country reports note the importance of CBRs for Pacific Island export industries, and there are anecdotal examples of CBR issues creating difficulties for particular export industries – for example the export of logs in Samoa and Vanuatu’s difficulties after losing one of its USD CBRs (IMF Sep 2021).

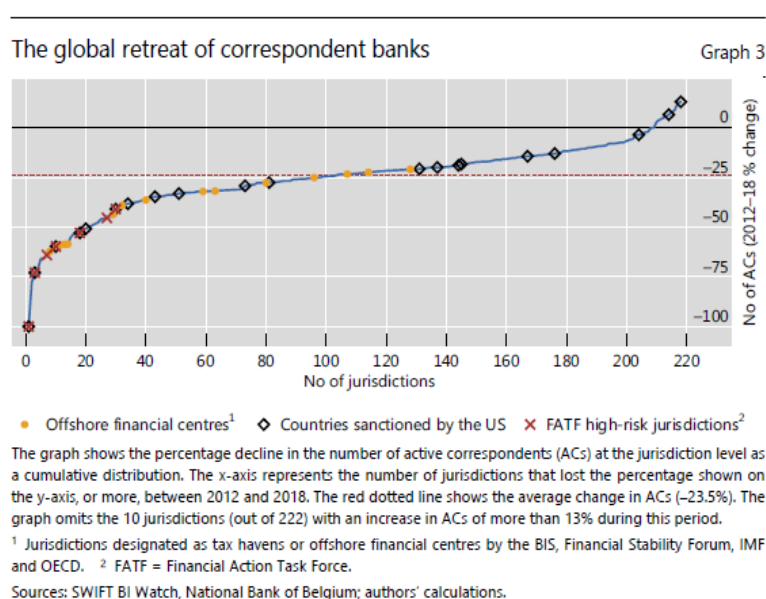
In practice the relationship between trade and CBRs is likely to run in both directions. Analysis by Rice et al found that trade “supports” CBRs and that facilitating trade was a key purpose of correspondent banking. Similarly, stronger growth was found to stem the loss of CBRs and that shrinking economies lost more CBRs (Rice et al 2020).

The study by Becker found some evidence that the decline in CBRs acts to depress international transactions. His analysis found that as the pace of decline in CBRs accelerates, the pace of international transactions slows (Becker 2023b).

1.4 Extent of Compliance

One of the major drivers of global de-risking is the increasing burden of compliance with AML/CFT regulations, coupled with the reputational risk involved when banks incur large fines for money laundering and terrorism financing offenses (RBNZ 2021). Analysis by Rice et al found that “high risk” countries have lost large shares of active correspondents (where high risk is defined as being designated as deficient in multiple areas (i.e. AML/CFT compliance, sanctioned countries or tax havens/offshore centres (Rice et al 2020)). Their conclusion was that jurisdictions with deficient AML/CFT regimes lost far more CBRs than other jurisdictions, as shown in Figure 8.

Figure 8: High risk jurisdictions versus loss of CBRs



Source: Rice et al 2020

A 2021 IMF Article IV Report for Vanuatu noted that:

All of the PICs facing CBR issues previously have been found by the Asia Pacific Group on Money Laundering (APG) to have important deficiencies in their AML/CFT regimes (IMF Sep 2021).

The 2022 report for PIRI countries found that Pacific Island countries continue to face challenges in regard to compliance with AML/CFT regimes. Table 4 below sets out selected FATF assessment ratings for compliance with FATF Technical Compliance recommendations taken from that report. The table shows that Fiji and Vanuatu were compliant or largely compliant, Samoa and Solomon Islands had some areas of partial compliance, and PNG, Timor-Leste and Tonga had several areas of non-compliance (although note that the dates of assessment vary and are earlier for the latter three countries).

Table 2: FATF technical compliance ratings for PIRI Countries

		Recommendation													
Country	Report year	1	2	10	14	16	20	22	26	27	28	29	30	31	33
Fiji	2019	LC	LC	LC	C	LC	LC	LC	LC	LC	LC	C	C	LC	C
Samoa	2018	PC	LC	LC	C	PC	LC	PC	PC	PC	PC	LC	C	LC	LC
Solomon Islands	2019	PC	PC	NC	PC	NC	C	NC	PC	LC	PC	LC	C	LC	PC
Vanuatu	2018	C	C	LC	C	C	LC	LC	LC	C	LC	LC	C	C	LC

Notes: LC= largely compliant, C= compliant, PC= partially compliant. Source: Country Mutual Evaluation Reports

		Recommendation													
Country	Report year	1 ¹	2	5 ²	14	16	20	22	26	27	28	29	30	31	33
Papua New Guinea	2011	PC	PC	NC	PC	PC	PC	NC	NC	NC	NC	NC	PC	PC	NC
Timor-Leste	2012	PC	PC	PC	PC	PC	PC	PC	LC	LC	NC	NC	PC	LC	PC
Tonga	2010	PC	LC	NC	PC	PC	PC	NC	NC	PC	NC	PC	PC	LC	LC

Notes: LC= largely compliant, C= compliant, PC= partially compliant. Source: Country Mutual Evaluation Reports

Detailed analysis of AML/CFT statistics showed (PIRI 2022):

- Low level and insufficient reporting compared to the level of risks
- Few money laundering investigations and successful prosecutions
- Forfeiture outcomes remain modest

Follow up Mutual Evaluation Reports have shown marked improvements in recent years however (PIRI 2022). This is important, because poor ratings expose countries to a higher risk of being listed on international grey-lists for non-compliance, increasing the perception of AML/CFT risks and hence raises the risk of future de-banking (PIRI 2022).

A related issue that is particularly important for the smaller Pacific Island countries is the capacity of the financial sector and its regulators. The small size of their economies and limited pool of financial sector expertise has constrained their access to financial intelligence and ability to build the systems

required for robust AML/CFT systems. There can also be broader weaknesses in governance which has been exacerbated by the exodus of foreign-owned banks (Coyne 2022, RBNZ Feb 2022).

Another key driver, that has been of particular importance for Pacific Island countries, concerns the profitability of banking operations relative to other markets. Many studies have identified the small size of Pacific Island economies, and the resultant lack of economies of scale, as putting pressure on the commercial viability of CBR activities for banks (Becker 2023b). This is coupled with the relatively high cost of due diligence of monitoring MTOs, with the result that many banks have rationalised their businesses and chosen to withdraw CBRs from the region (GAO 2021).

Indeed, a 2017 FSB survey of banks found that around a third of banks said that they had exited relationships that were no longer profitable or cost-effective because of the required due diligence or other economic reasons (FSB 2017).

Weakening of business opportunities is also cited as a factor in making Pacific Island countries less attractive to investors than other regions. GDP growth per capita has been low, and the areas of potential FDI funding (such as tourism, retail and manufacturing) have issues including political uncertainty (IMF 2023). High reliance on remittances also weighs against profitability considerations for banks, since there is relatively little opportunity to provide other services, such as the provision of trade finance or operating accounts (GAO 2021, Lankford 2022).

2 Summary of CBR position for individual Pacific Islands Forum members

Table 5 shows the change in number of correspondent banking relationships, cross border transaction values and local banks between 2011 and 2022, for the countries for whom CPMI publish data. The table shows that all countries have suffered significant reductions in the number of CBRs, ranging from a decrease of 40% for Kiribati to a decrease of 70% for the Cook Islands.

Table 3: Changes in CBRs, transaction values and local banks 2011 – 2022

	CBR (counterparties abroad) (% Change 2011 to 2022)	Cumulative transaction value (% Change 2011 to 2022)	Local banks (% Change 2011 to 2022)	Number of local banks in 2023
Cook Islands	-70.6 %	-86.8 %	0.0 %	4
Fiji	-65.7%	61.2%	16.7%	6
French Polynesia	-47.7%	-10.6%	0.0%	5
Kiribati	-40.7%	13297.7%	0.0%	2
New Caledonia	-59.9%	-15.9%	0.0%	5
PNG	-55.5%	-26.0%	20%	4
Samoa	-51.6%	278.3%	0.0%	4
Solomon Islands	-57.3%	641.3%	25.0%	4
Tonga	-49.0%	-33.4%	25.0%	4
Tuvalu	-50.0%	91.0%	0.0%	2
Vanuatu	-65.1%	13.7%	33.3%	6

Source: CPMI 2023 and own investigation

The CPMI data does not, however, provide information on the total number of correspondent banks providing services to each country. While large decreases are a source of concern, most worrisome is the situation of the countries that are left with few remaining CBRs.

The need for better information on the extent of CBR closures, and the extent of issues perceived by individual countries is a constant refrain amongst the recommendations discussed in TP2. The main report recommends that a framework or “dashboard” be developed which classifies the status of de-banking in individual countries according to agreed criteria. Such a framework could be developed by an international agency, such as the World Bank or the IMF. In the meantime, it is possible to

glean some indication of the vulnerability of individual countries from public sources, such as IMF Article IV reports, other published materials and the responses to the survey (reported in TP5). Table 4 provides an illustrative dashboard using publicly available information.

Table 4: Illustrative dashboard for PI Forum Countries

	Status	Source	Date of info	Notes
Cook Islands	No information			
Fiji	No issue	IMF Article IV	Dec 2021	Fiji is not facing pressure on CBRs
French Polynesia	No information			
Kiribati	No issue	IMF Article IV Mission	Feb 2023	No issues raised
Nauru	Some issues	IMF Article IV	Feb 2022	Limited ability to undertake international transactions in non-AUD currencies. Significant exchange rate induced revenue losses
New Caledonia	No information			
Niue	No information			
PNG	No issue	IMF Article IV Survey	Sep 2022 2023	
Samoa	Some Issues	IMF Article IV	Mar 2021	The two domestic banks had their USD CBRs terminated in 2021
Solomon Islands	Some Issues	IMF Article IV	Jan 2022	CBRs under pressure for past several years. AML/CFT framework needs strengthening
Tonga	Some Issues	IMF Article IV Survey	Aug 2020 2023	Loss of CBRs seen as important downside risk by IMF
Tuvalu	Some Issues	IMF Article IV Survey	Jul 2023 2023	Only 3 CBRs left
Vanuatu	Some Issues	IMF Article IV	Mar 2023	Predominance of foreign banks provides resilience, but at risk of de-risking

3 Evidence from previous studies for individual Pacific Islands Forum members

3.1 Cook Islands

The Cook Islands is a self-governing island country comprising 15 islands. It is an independent country in free association with New Zealand. Most Cook Islanders also have New Zealand citizenship. The population has declined to around 8,000 (CIA 2023a). The Cook Islands is prone to extreme weather events, tropical cyclones in particular.

The country uses the New Zealand dollar as its currency. Tourism is the main driver of the economy, although there are also some agriculture, mining and fishing activities as well as offshore banking services. Cook Islands is also dependent on foreign aid from New Zealand and the ADB. It is not a member of the IMF, although it receives technical assistance from the IMF. Tourism from New Zealand has recovered at a more rapid pace than in many other countries in the region and the ADB anticipates that the Cook Islands will grow significantly faster than its Pacific Island peers in 2023 and 2024 (ADB April 2022).

While remittance inflows from New Zealand used to be important, there is now a net remittance outflow due to the combination of outflows to support school and university students studying abroad and an extensive migrant labour force working in tourism sending remittances home (ADB Dec 2022).

Table 5 below (and the equivalent table for subsequent countries) shows the percentage change in a range of measures related to correspondent banking in the period 2011 to 2020. An entry of zero (0.0) in the relevant column means that there has been no change, a positive number means that there has been an increase, a negative number a decrease. For example, -34.3% means that cumulative transaction volume in 2020 was 34.3% lower than it was in 2011. CPMI define CBRs as the number of counterparties abroad.

Table 5 shows that in the Cook Islands, between 2011 and 2022 the number of CBRs fell by 70% and transaction values fell by 87%. The number of local banks remained unchanged.

Table 5: Changes in correspondent banking relationships 2011 – 2022 – Cook Islands

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	8.9 %	-86.8 %	-70.6 %	0.0 % 4 banks in 2023	-70.6 %

Source: CPMI 2023

3.2 Fiji

In terms of population, Fiji is one of the larger Pacific Island countries, with some 890,000 people. It is geographically dispersed, with over 332 islands of which a third are inhabited. Fiji is highly prone to natural disasters and climate change risks, particularly cyclones. Tourism is the largest economic sector, employing around 119,000 Fijians and contributing

more than 30% of GDP (Investment Fiji 2023). It is followed by agriculture (sugar being the biggest primary agricultural export). Remittances contribute a relatively small share of GDP, averaging just below 5% over the 2010 to 2019 period (PIRI 2022).

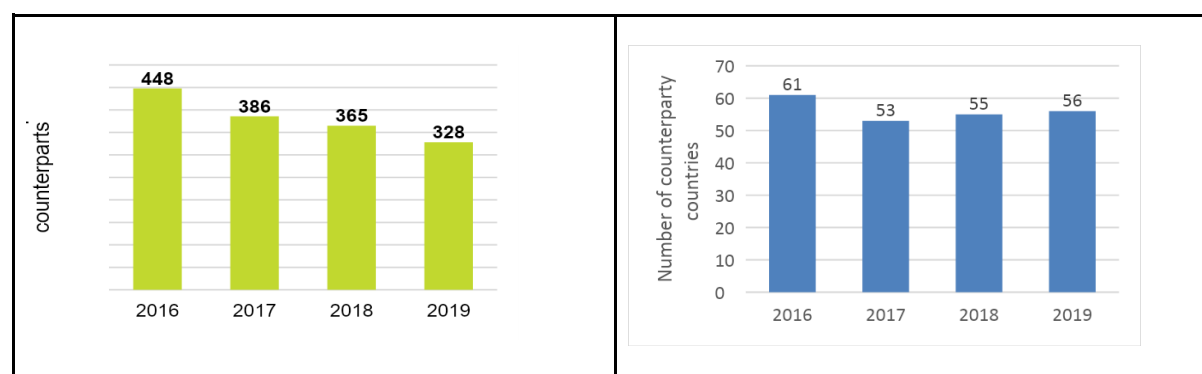
Table 6: Changes in correspondent banking relationships 2011 – 2022 – Fiji

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	42.5 %	61.2 %	-65.7 %	16.7 % 6 banks in 2023	-70.6 %

Source: CPMI 2023

Table 6 shows that over the period 2011 to 2022, Fiji lost 66% of its CBRs according to Swift data, while transaction values increased. The number of local banks increased slightly (CPMI 2023).

Figure 9: Number of CBRs and number of counterparty countries – Fiji



Source: PIRI 2022

Figure 9 shows that while the number of unique counterparties has fallen steadily over the period 2016 to 2019, the number of counterparty countries increased in 2018 and 2019. This suggests that Fiji's connections to the international finance sector remain fairly robust (PIRI 2022).

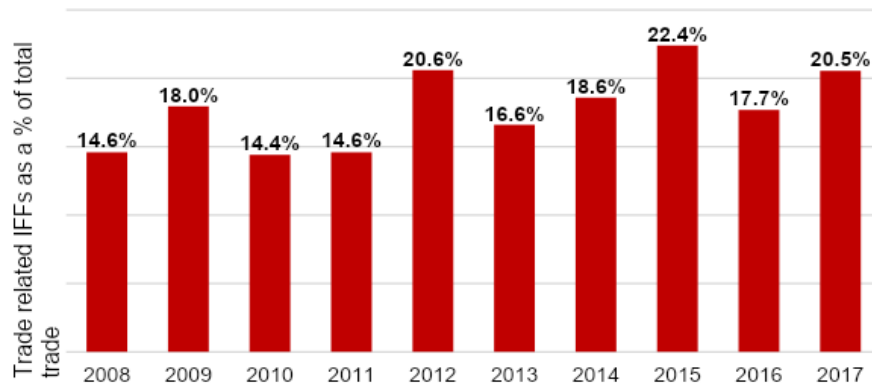
It should be noted, however, that data provided for the PIRI project reflected steady increases from 2010 to 2020. As noted in the PIRI report, this may be due to differences in definitions or calculation methodology (PIRI 2022).

Fiji's financial system is relatively well developed. Of the six commercial banks, five are foreign owned (World Bank June 2022). The banks have good track records on AML/CFT compliance, there are strong licensing requirements, and prudential regulations comply with AML/CFT requirements (IMF Dec 2021). On the other hand, Fiji has been listed as a non-cooperative tax jurisdiction by the EU, a matter which is not directly related to AML/CFT compliance, but is often factored in by global banks into country risk-ratings for AML/CFT purposes (PIRI 2022). Trade related illicit financial flows²

² The trade related IFFs reported by the PIRI study are compiled by Global Financial Integrity (GFI) and is based on trade mis-invoicing. The data collected by GFI is subject to both over-estimation and under-estimation errors and should be regarded as indicative.

as a percentage of trade are somewhat variable, but show an increasing trend, as shown in Figure 10 (PIRI 2022).

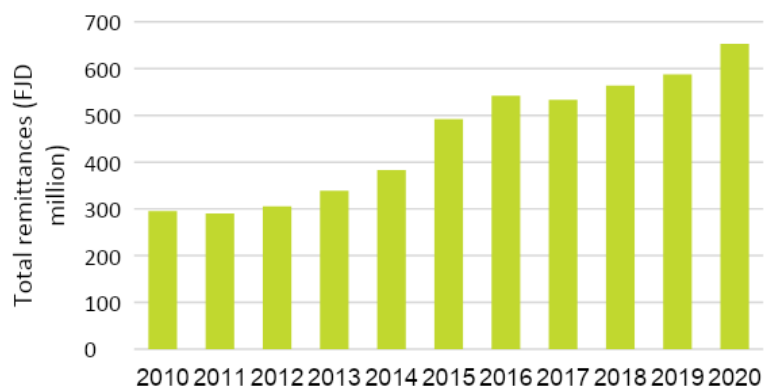
Figure 10: Trade related illicit financial flows— Fiji



Source: PIRI 2022

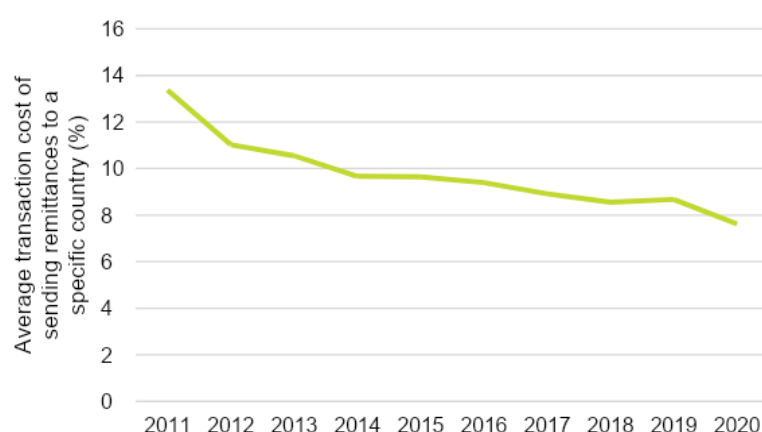
The value of total remittances exhibits a steady increase over the period 2010 to 2020 (Figure 11), while the average transaction cost of sending remittances has been falling (Figure 12) (PIRI 2022).

Figure 11: Value of total remittances— Fiji



Source: PIRI 2022

Figure 12: Average cost of sending remittances— Fiji



Source PIRI 2022

3.3 French Polynesia

French Polynesia is a territory of France comprising some 40 islands. Its population is around 304,000, of whom 62% live within cities. French Polynesia's GDP per capita is one of the highest in the region, at US\$19,914 in 2021 (World Data No date (a)).

Tourism is a major driver of the economy, although black cultured pearls, principally from the Tuamotu and Gambier islands groups, account for some two-thirds of export earnings (Britannica no date). Manufactured products include copra, coconut oil, other oils, beer, printed cloth, and sandals.

Table 7 shows that the number of CBRs fell by 48% between 2011 and 2022, with transaction values falling by just over 10%. The number of local banks remained unchanged.

Table 7: Changes in correspondent banking relationships 2011 – 2022 – French Polynesia

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2023	46.9 %	-10.6 %	-47.7 %	0.0 % 5 banks in 2023	-47.7 %

Source: CPMI 2023

3.4 Kiribati

Kiribati is one of the most remote countries in the world. Its population of around 112,000 people are spread over 21 islands in a geographic area of 3.5 million square kilometres. The country is vulnerable to climate change, and has a narrow economic base which is dominated by fishing (IMF Jan 2019).

The IMF has identified the need to strengthen institutional capacity, including the production of financial and national accounting data, the effective supervision and regulation of financial institutions, and further capacity building of the recently established anti-corruption unit (IMF Feb 2023).

Table 8: Changes in correspondent banking relationships 2011 – 2022 – Kiribati

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	67.7 %	13297.7 %	-40.7 %	0.0 % 1 bank in 2023	-40.7 %

Source: CPMI 2023, IMF xxx 2023

Table 8 shows that the number of CBRs fell by just over 40% between 2011 and 2022, despite a huge increase in transaction values. The number of local banks remained unchanged.

3.5 Nauru

Nauru is a remote island with a total land area of just 8 square miles but vast territorial waters. It has a population of around 12,000 (IMF Feb 2022). Transport costs are extremely high, which contributes to high fixed costs and a high cost of living. Fishing and shipping are its main economic sectors; almost all consumer goods are imported. Nauru is exposed to both natural disasters and climate change.

Nauru uses Australian dollars as its legal tender, and it has no central bank and no commercial banks. In 2015 Nauru entered into an agency arrangement with Bendigo Bank, an Australian bank, and its accounts and transactions are managed by the overseas parent bank.

As a consequence, Nauru does not have direct CBRs to enable it to conduct cross-border transactions in non-Australian currencies, as all transactions go through the bank agency. Foreign exchange transactions are difficult to conduct and expensive in other major currencies (including USD, euros, British pounds and now Fiji dollars) (IMF Feb 2022).

The Bendigo Bank Agency operates under the Australian AML/CFT regulatory regime and is supervised by AUSTRAC. Nonetheless CBR pressures remain, particularly in relation to USD transactions. These are likely to stem from a combination of legacy reputational issues (from Nauru's former attempt to set up a financial centre), broader CBR challenges in the Pacific Islands, remaining AML/CFT concerns and profitability concerns. Efforts to comply with the AML/CFT framework are ongoing (IMF Feb 2022). Nauru was removed from the EU's list of uncooperative tax havens 20 years ago.

The lack of connectivity to the international payments system heavily constrains inbound investment and economic development, and even makes the receipt of aid complicated and expensive (IMF Feb 2022).

3.6 New Caledonia

New Caledonia is an overseas territory of France. It has a population of some 300,000 people, most of whom live on the main island, in and around the capital Noumea (CIA 2023b). The country is subject to cyclones.

New Caledonia has a large tourism sector, which was hit hard by Covid-19. It also has a strong industrial base centred on mining and refining nickel, holding about 25% of global reserves. Three

refineries account for 90,000 tonnes of refined nickel per annum. Other trade with New Zealand includes food and beverage (dairy, meat and fruit) as well as wood products and machinery (NZFAT Oct 2022).

Table 9: Changes in correspondent banking relationships 2011 – 2022 – New Caledonia

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	0.1 %	-15.9 %	-59.9 %	0.0 % 5 banks in 2023	-59.9 %

Source: CPMI 2023

Table 9 shows the decline in transaction values was greatly outstripped by a decline in CBRs of nearly 60%. The number of local banks remained unchanged.

3.7 Niue

Niue is one of the world's largest coral islands. In mid 2022 its population was approximately 2,000. Niue self-governs in free association with New Zealand: thus Niue is responsible for internal affairs, but it has invited New Zealand to take responsibility for external affairs and defence (CIA 2023c). Niue also uses the New Zealand dollar as its currency and relies on the New Zealand banking system. Technical assistance is provided to the country by the United Nations Joint Sustainable Development Goals (SDG) Fund (ADB Dec 2022). Its exports in 2021 were \$5.7 million, of which 64% was passenger and cargo ships. 57% of exports were to Indonesia, and 7% to Thailand.

3.8 Papua New Guinea (PNG)

Papua New Guinea is rich in natural resources, which make up some 84% of exports (primarily LPG and LNG, gold and copper). Agricultural forestry and marine products make up the remaining exports. Of the 8.8 million population most live in rural areas, without access to power or infrastructure and over 80% rely on subsistence farming for livelihoods (PIRI 2022, IMF Sep 2022).

Over the six years to 2020, public debt built up due to low commodity prices, a severe drought in 2015-16 and a major earthquake in 2018. Since then, public finances have been further strained by the COVID pandemic coupled with poor public health resources (IMF Sep 2022).

The finance sector is relatively under-developed compared to the size of PNG's economy, and a substantial proportion of the population has no or limited access to banking services. There are four commercial banks operating in PNG: two domestically owned and two foreign owned. There are also smaller deposit-taking and lending institutions, with microfinance lenders playing an important role in lending to those without bank accounts (World Bank June 2022).

Table 10 shows the number of CBRs declined by 55% over the 11 years to 2022, with no change in the number of local banks.

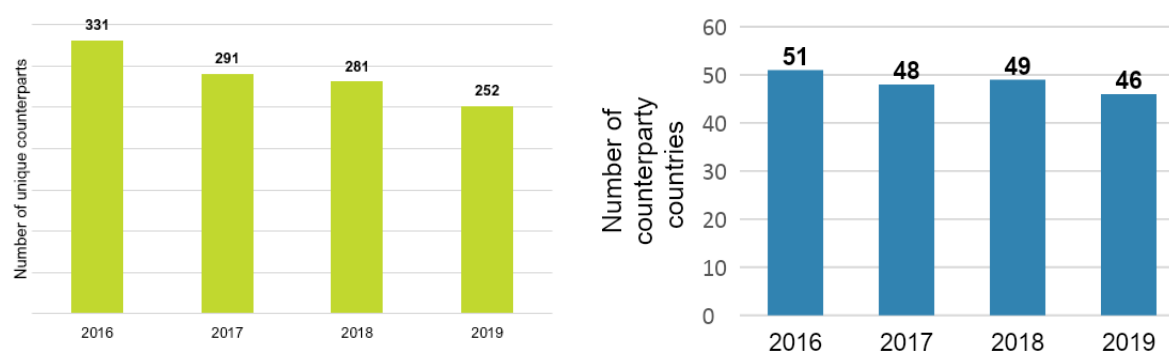
Table 10: Changes in correspondent banking relationships 2011 – 2022 – PNG

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	126.2 %	-26.0 %	-55.5 %	20.0 % 4 banks in 2023	-62.9 %

Source: CPMI 2023

Figure 13 shows a declining trend in number of unique counterparties over the period 2016 to 2019. Over the same period there was some reduction in the number of counterparty countries, but the downward trend was much less pronounced (PIRI 2022).

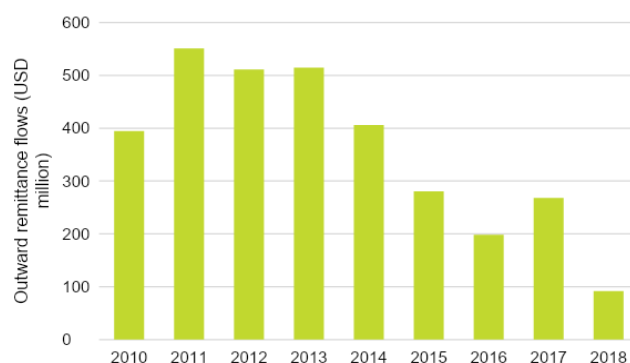
Figure 13: Number of CBRs and number of counterparty countries-- PNG



Source: PIRI 2022

The closure of CBRs has affected MTOs in particular, with institutions losing CBRs, having difficulty securing them, and/or institutions having to close or impose strict conditions on service providers in order to maintain their CBRs (PIRI 2022).

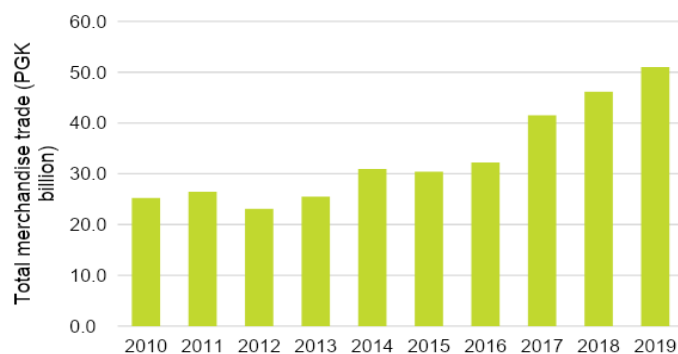
Figure 14: Value of total remittances– PNG



Source: PIRI 2022

PNG differs from other Pacific Island Forum members in that it is a net remittance sending country. Figure 14 shows a downward trend in outward remittances since 2011. The main destinations are Indonesia and Australia, sent by migrant workers. These fund transfers are conducted mainly through commercial banks (PIRI 2022).

Figure 15: Total value of imported and exported goods – PNG

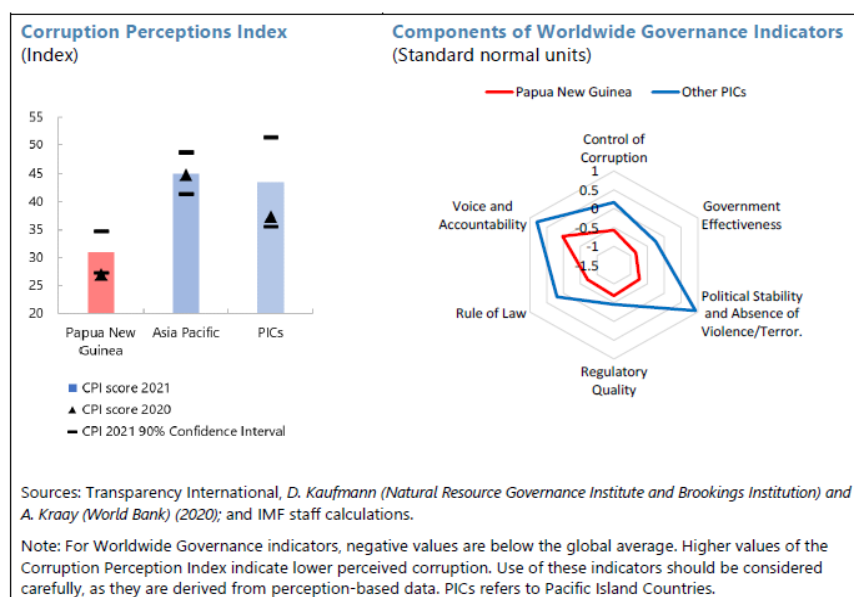


Source PIRI 2022

As shown in Figure 15, the total value of trade flows has dipped in the period 2012 to 2016, before largely recovering by 2019. Data on Illicit Financial Flows (IFFs) is largely lacking, although for the years it is available the IFFs can be up to 17% of total trade (PIRI 2022).

PNG was placed on the FATF greylist in 2014, as a jurisdiction with strategic AML/CFT deficiencies. Following significant improvements, it was removed from the greylist in 2016. PNG's performance on Corruption Perceptions improved in 2021. However significant governance challenges remain, with PNG being given negative scores in almost all components of Worldwide Governance Indicators. Work on improvements to the AML/CFT legal framework continues (IMF Sep 2022).

Figure 16: Corruption Perception Index and Worldwide Governance Indicators– PNG



Source: IMF Sep 2022

3.9 Samoa

Samoa has a population of around 197,100. Samoa's economy is based heavily on agriculture, tourism and fishing and some 82% of the population live in rural areas. Samoa is remote and also highly vulnerable to natural disasters, being amongst the top five countries suffering from climate-related losses, when measured as a % of GDP, over the twenty-year period to 2018 (PIRI 2022). As a consequence, Samoa is heavily dependent on official aid (IMF Mar 2023a).

Samoa has a large diaspora, so its inward remittances are sizeable, comprising some 18.7% of GDP in 2021 (IMF Mar 2023a, PIRI 2022). Dependence on tourism, agricultural exports and foreign aid makes Samoa vulnerable to reductions in CBRs.

As at the end of 2021, Samoa's financial system comprised 30 licensed financial institutions, including four commercial banks – two of whom are foreign owned. Non-bank financial institutions include MTOs, some very small, micro-finance providers, credit unions and a small insurance sector (World Bank Jun 2022).

In common with other Pacific Island countries, Samoa has experienced pressure on CBRs (IMF Mar 2023a). As shown in Table 11, Samoa lost 52% of its unique counterparties between 2011 and 2022 despite a significant increase in the value of cross border transactions. The number of local banks remained unchanged (CPMI 2023).

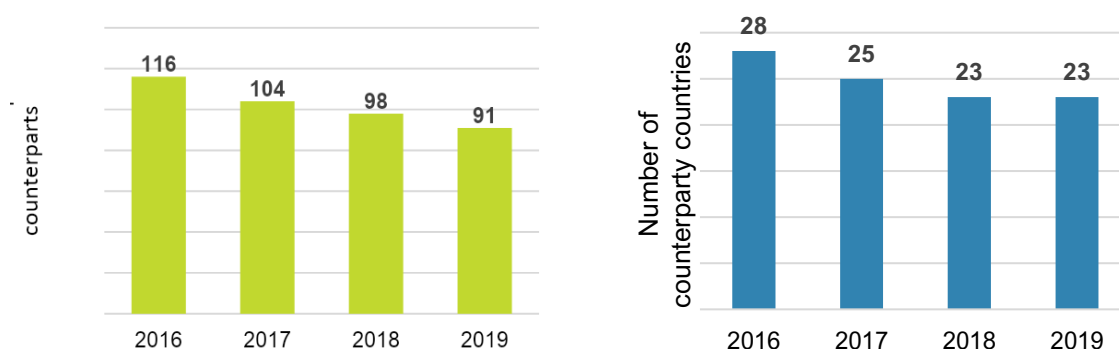
Table 11: Changes in correspondent banking relationships 2011 – 2022 – Samoa

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	39.1 %	278.3 %	-51.6 %	0.0 % 4 banks in 2023	-51.6 %

Source: CPMI 2023

Figure 17 shows a steadily declining trend in number of unique counterparties over the period 2016 to 2019. The decline in number of counterparty countries is less pronounced and looks to have stabilised in 2019 (PIRI 2022).

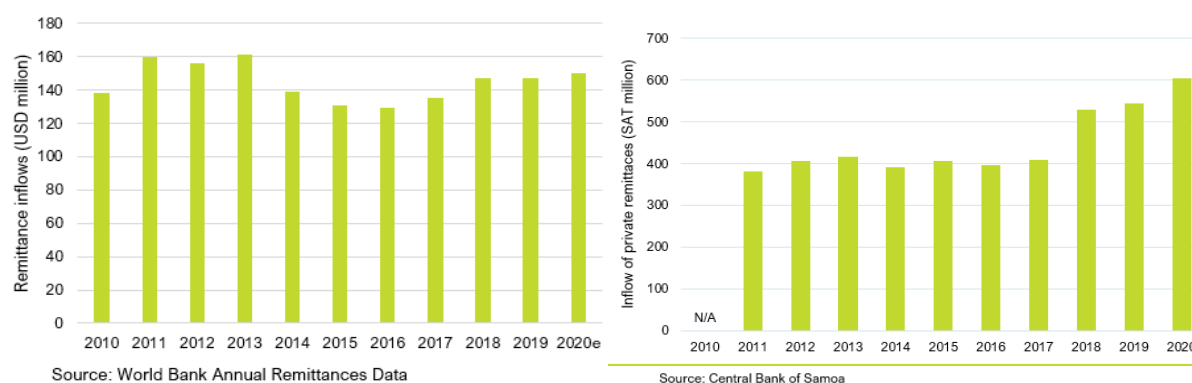
Figure 17: Number of CBRs and number of counterparty countries – Samoa



Source: PIRI 2022

Two of Samoa's banks had their USD CBRs terminated by their Australian counterparties in 2021 (their Aus dollar accounts remain active). The banks secured alternative USD arrangements, although these are more expensive and the banks continue to pursue new CBRs (IMF Mar 2023a). Larger MTOs have maintained access to bank accounts, but many smaller ones have struggled. Between 2010 and 2018, the number of money traders operating in Samoa halved (PIRI 2022)

Figure 18: Value of total remittances – Samoa

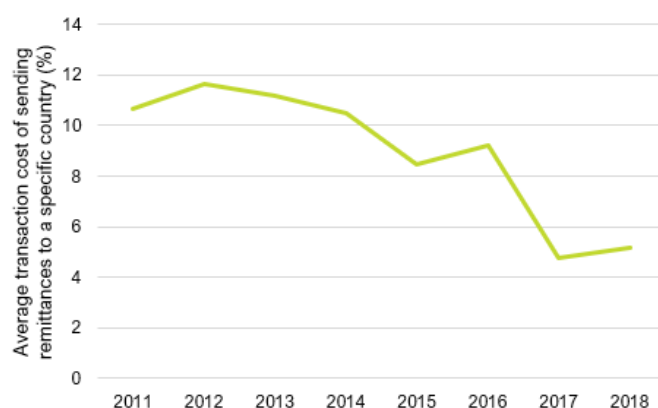


Source: PIRI 2022

World Bank data on the value of total remittances shows no discernible trend over the period 2010 to 2020 (see Figure 20), although data from the Central Bank of Samoa suggests an increasing trend. (PIRI 2022).

The average transaction cost of sending remittances were previously quite high (IMF Mar 2023a), but appears to have fallen in recent years as per Figure 21 (PIRI 2022).

Figure 19: Average cost of sending remittances – Samoa

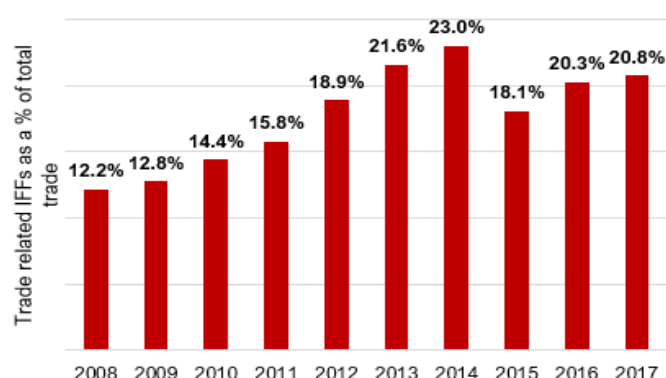


Source PIRI 2022

Key drivers of de-banking in Samoa include low profitability, risks from weaknesses in AML/CFT supervision, and reputational risks arising from Samoa's offshore centre (IMF Mar 2023a, PIRI 2022). However, Samoa has not been identified as a country with strategic AML/CFT deficiencies (PIRI 2022) and the authorities are currently conducting an updated AML/CFT risk assessment and elaborating a national AML/CFT strategy (IMF Mar 2023a).

Figure 20 shows that trade-related Illicit Financial Flows increased as a proportion of trade until reaching 23% in 2014, before falling in 2015 and then starting to rise again (PIRI 2022).

Figure 20: Trade related IFFs – Samoa



Source: Global Financial Integrity

Source PIRI 2022

3.10 Solomon Islands

Solomon Islands is a small, low-income Pacific Island country. Its population of some 670,000 is dispersed over 922 islands, of which 347 are inhabited. Three quarters of the population live in rural areas, and agriculture and forestry are the most important sectors of the economy (PIRI 2022, IMF Jan 2022).

The country is regarded as fragile, due to long standing socio-economic tensions, vulnerability to natural disasters and climate change, gaps in infrastructure and vulnerabilities in governance and corruption. Although Solomon Islands has made significant strides, it continues to face development challenges (IMF Jan 2022).

Solomon Island's financial sector is dominated by four commercial banks and a provident fund. Bank and institutional lending is at relatively low levels, and there is also a low level of financial inclusion (World Bank Jun 2022).

The sole domestic bank lost its USD CBR and could not secure an alternative. As a temporary measure, cross-border transactions were conducted via the Central Bank of Solomon Islands, on a limited scale until a new USD CBR was secured. The hiatus did, however, affect the country's main export business, logging (PIRI 2022).

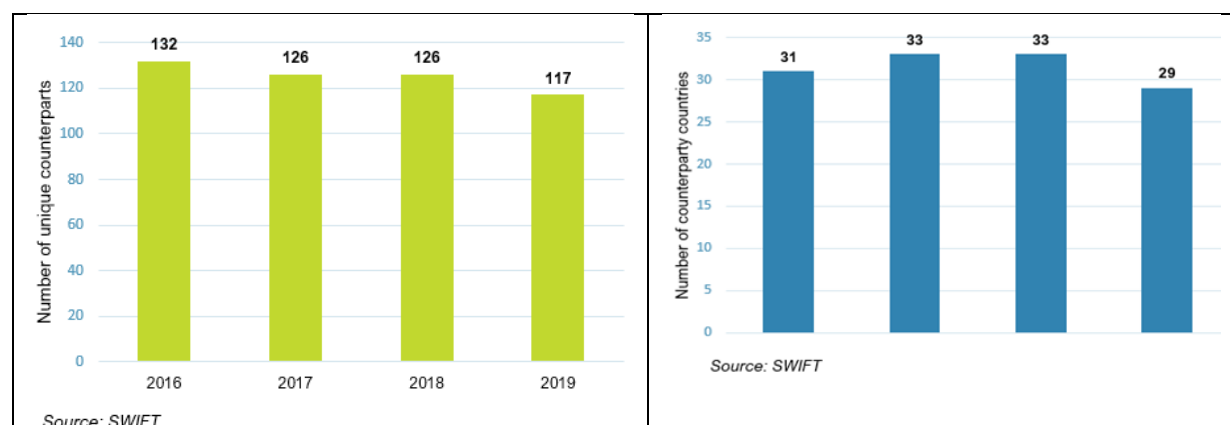
Table 12: Changes in correspondent banking relationships 2011 – 2022 – Solomon Islands

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	30.2%	641.3 %	-57.3 %	25.0 % 4 banks in 2023	-65.8 %

Source: CPMI 2023

Table 1 shows that the number of unique counterparties has more than halved over the period 2011 to 2022 while the number of local banks remained unchanged (CPMI 2023). Figure 21 shows a steady fall in CBRs from 2016 to 2019, with the number of counterparty countries showing a rising then falling pattern.

Figure 21: Number of CBRs and number of counterparty countries – Solomon Islands

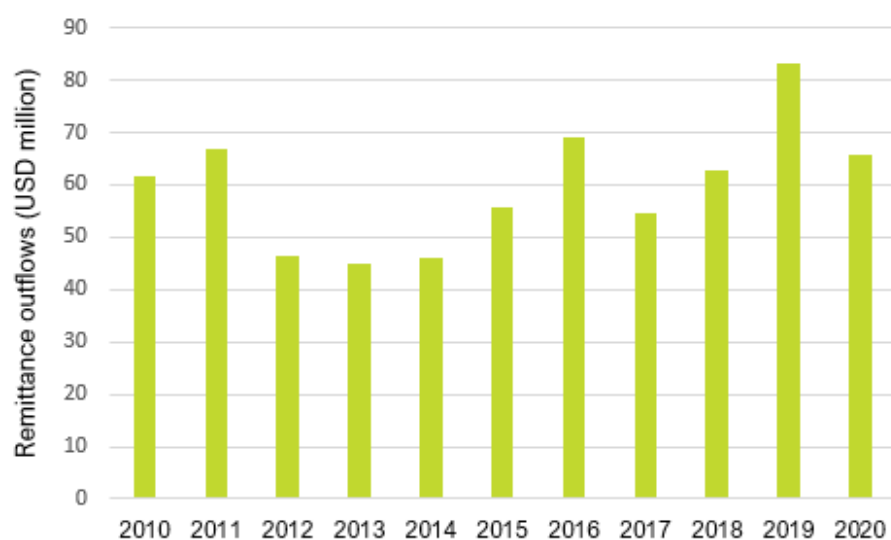


Source: PIRI 2022

Unlike many Pacific Island countries, remittances are not an important part of the Solomon Islands economy, as it does not have a large diaspora. The decline in CBR's has perhaps had less of an impact in Solomon Islands than in other Pacific Island nations, although some MTOs have closed (PIRI 2022).

Figure 22 shows a somewhat variable pattern of outward remittances over time. Data on the cost of remittances was not available (PIRI 2022).

Figure 22: Remittance outflows of remittances – Solomon Islands

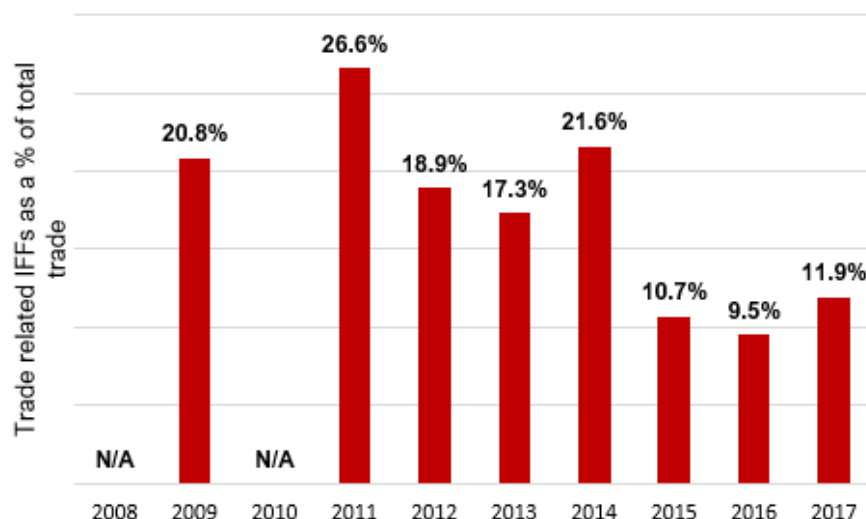


Source: World Bank Annual Remittances Data

Source: PIRI 2022

The pressure on CBRs in the Solomon Islands is attributed to several factors, namely weaknesses in AML/CFT supervision of the financial sector, the high cost of due diligence for transactions and profitability concerns (IMF Jan 2022).

Figure 23: Trade related Illicit Financial Flows – Solomon Islands



Source: Global Financial Integrity

Source: PIRI 2022

Figure 23 shows that illicit financial flows as a % of trade more than halved between 2011 and 2017. This decline coincided with strong growth in transaction values of CBRs and it is possible that trade flows were increasingly transacted through more regular channels (PIRI 2022).

3.11 Tonga

Tonga's population of some 104,500 is spread across 36 islands, and over three quarters live in rural areas (PIRI 2022). Tonga is particularly vulnerable to natural disasters. It was battered by two major tropical cyclones in 2018 and 2020, and then a powerful volcanic eruption created a tsunami and ashfalls which caused extensive damage. The undersea fibre optic cable to Tonga was severed by the tsunami, disrupting communications and remittance flows (IMF Aug 2022).

Tonga's main economic sectors are tourism and agriculture. Its growth potential is assessed as being relatively low, due to its exposure to natural disasters, geographical remoteness and limited production capacity (IMF Aug 2022).

Tonga is heavily reliant on inflows of remittances for foreign exchange. The vast majority of remittances (some 86% in Dec 2020) are transferred via Foreign Exchange Dealers, with the remainder transferred by banks (PIRI 2022). There are four commercial banks operating in Tonga, two domestically owned and two foreign owned (World Bank June 2022).

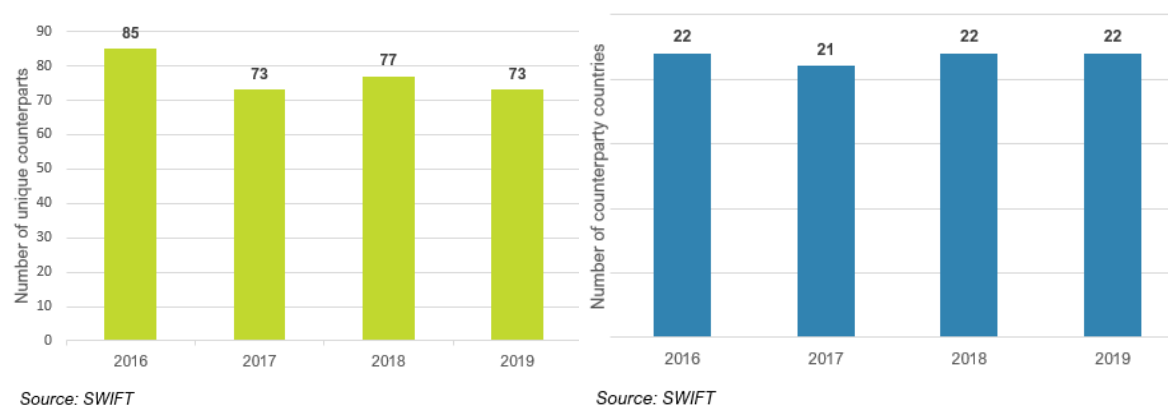
Table 13: Changes in correspondent banking relationships 2011 – 2022 – Tonga

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	27.8 %	-33.4 %	-49.0 %	25.0 % 4 banks in 2023	-59.2 %

Source: CPMI 2023

Table 13 shows over the 21 years to 2022, CBRs declined by 49% while the number of local banks increased by 25%. From Figure 24 it appears that much of the reduction had occurred by 2017 and that the number of counterparty countries has remained relatively stable (PIRI 2022).

Figure 24: Number of CBRs and number of counterparty countries – Tonga

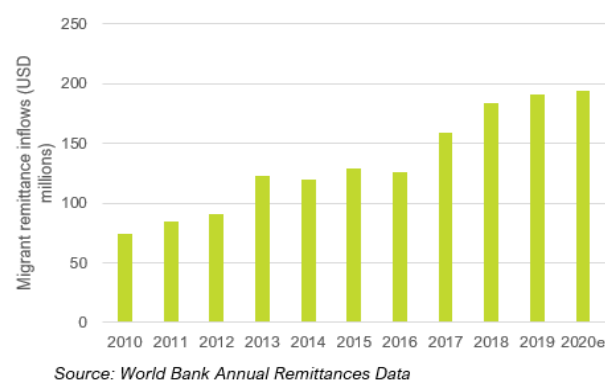


Source: PIRI 2022

De-banking has been a major issue for Tonga, and has resulted in the closure of the bank accounts of many MTOs. While the MTOs have typically found replacements, it has at times resulted in increased remittance costs (PIRI 2022).

Figure 25 shows that remittance inflows have been increasing steadily since 2010, reflecting significant increases in the number.

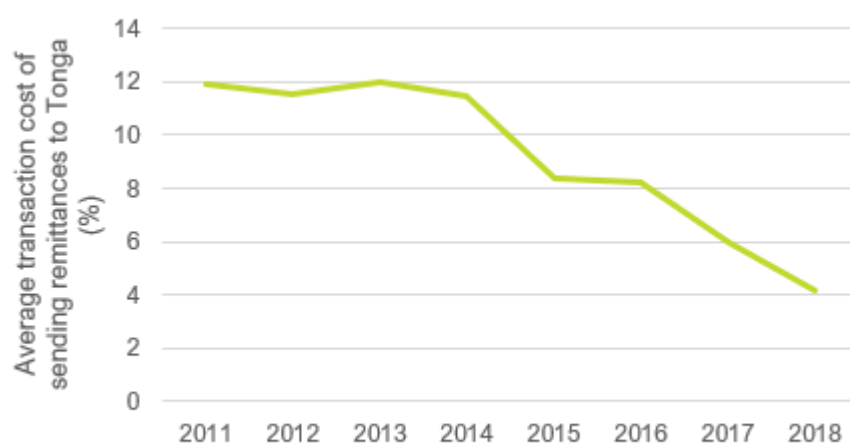
Figure 25: Remittance inflows of remittances – Tonga



Source: PIRI 2022

The cost of remittances has reduced significantly since 2013, as shown in Figure 26. The World Bank speculated that the factors contributing to this decline could include the introduction of more cost-effective products, such as the Ave Pa'Anga Pau voucher for use in the New Zealand corridor, the arrival of innovative providers such as Clickex and the general flexibility remittance providers. However other data sources, such as Send Money Pacific, found the average cost of sending remittances to Tonga to be well above the global average (PIRI 2022).

Figure 26: Remittance inflows of remittances – Tonga



Source: World Bank Development Indicators

Information on illicit trade flows in Tonga is not available beyond 2014.

3.12 Tuvalu

Tuvalu is small and geographically remote. With a population of just 11,000 people Tuvalu lacks economies of scale and institutional capacity. Tuvalu also has a narrow production base and is highly dependent on imports. Coupled with its exposure to natural disasters and climate change, Tuvalu's economy is regarded as exceptionally fragile (IMF Aug 2021).

Table 14: Changes in correspondent banking relationships 2011 – 2022 – Tuvalu

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	30.2 %	91.0 %	-50.0 %	0.0 % 2 banks in 2023	-50.0 %

Source: CPMI 2023

Tuvalu uses Australian dollars as its legal tender and has no central bank. The Asia Pacific Group on Anti-Money Laundering and the Fiji Intelligence Unit support its AML/CFT efforts, and the authorities are planning to establish a domestic Financial Intelligence Unit (IMF Aug 2021).

Table 14 indicates that Tuvalu lost half of its CBRs between 2011 and 2022, while the number of local banks increased by a quarter. The IMF report that in April 2020 lost its CBR with Australian banks, which left it with an existing CBR with the Bank of Hawaii and a newly established CBR with

the Bred bank in Fiji (IMF Aug 2021). In July 2023, the IMF reported that Tuvalu had only three CBRs remaining (IMF Jul 2023).

3.13 Vanuatu

Vanuatu comprises 83 islands with a total population of some 300,000. Vanuatu graduated from the United Nations list of least developed countries in 2020, but its development needs remain high, with GDP per capita below most of the other Pacific Island countries (IMF Sep 2021, PIRI 2022).

Vanuatu is also extremely vulnerable to climate change and natural disasters, and suffers from frequent tropical cyclones, earthquakes and volcanic eruptions.

Critical infrastructure projects are hampered by a lack of domestic capacity and weak governance has contributed to ballooning deficits. (IMF Mar 2023).

Agriculture and tourism are the main economic sectors, with agricultural products accounting for some 75% of Vanuatu's total exports. Vanuatu has zero income tax and is on the EU list of non-cooperative tax jurisdictions. Weaknesses in Vanuatu's Economic Citizen Program (ECP) have added to governance and corruption concerns (IMF Mar 2023).

Vanuatu has two domestic banks and three foreign banks in its onshore banking system and nine foreign banks in its offshore centre. The high predominance of foreign owned banks is seen as providing some much-needed resilience to the banking system (IMF Mar 2023). Remittance inflows are amongst the lowest of all Pacific Island countries, and form a relatively small proportion of GDP. The majority of remittance transfers are undertaken by MOTs (PIRI 2022).

Table 15 shows that Vanuatu lost 65% of its unique counterparties between 2011 and 2022, while the number of local banks increased by one third (CPMI 2023).

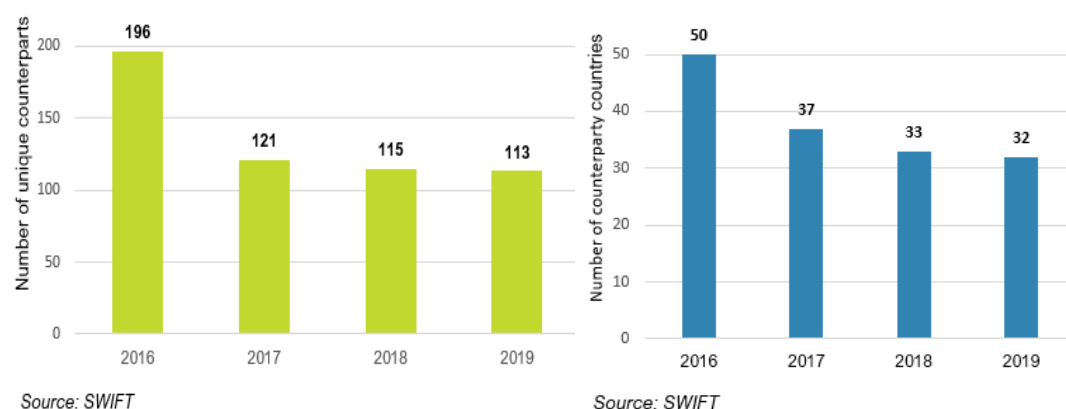
Table 15: Changes in correspondent banking relationships 2011 – 2022 – Vanuatu

	Cumulative transaction volume	Cumulative transaction value	CBR (counterparties abroad)	Local banks	Ratio CBR/Local banks
% Change 2011 to 2022	38.0 %	13.7 %	-65.1 %	33.3 % 5 banks in 2023	-73.8 %

Source: CPMI 2023, IMF xxx 2023

Figure 27 shows that most of this reduction in CBRs occurred in 2017, which is shortly after Vanuatu was greylisted by FATF (PIRI 2022).

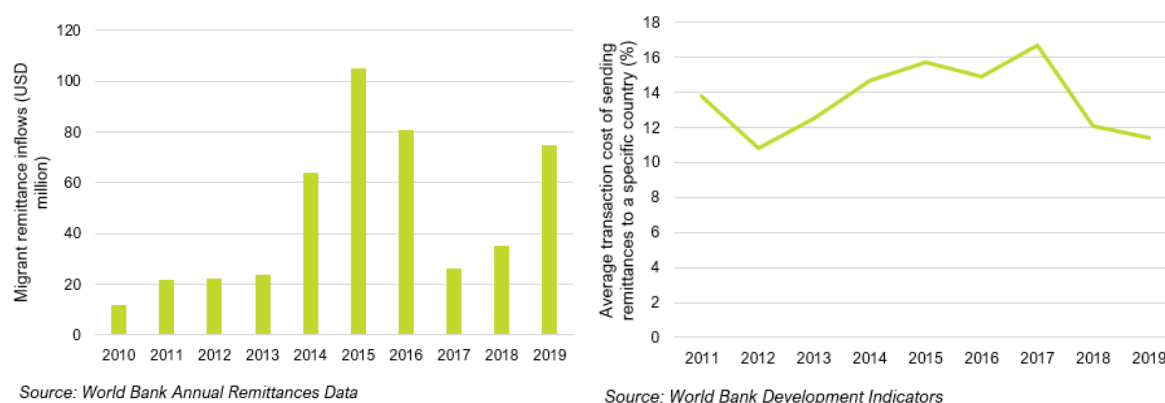
Figure 27: Number of CBRs and number of counterparty countries – Vanuatu



Source: PIRI 2022

In 2021, the National Bank of Vanuatu lost its USD CBR with the National Australia Bank. The IMF reported that this decision was likely influenced by the concerns being raised regarding Vanuatu's Economic Citizenship Program (ECP) (IMF Sep 2021, IMF Mar 2023).

Figure 28: Remittance inflows and cost of remittances – Vanuatu



Source: PIRI 2022

The value of remittances into Vanuatu increased substantially in 2014 and 2015, and has been variable since then, as can be seen in Figure 28. Unlike other Pacific Island countries, the cost of remittances increased between 2012 and 2017 and has remained relatively high throughout the period.

Information on trade-related illicit financial flows (IFFs) is unavailable beyond 2011 (PIRI 2022).