

Economic Bulletin



A Quarterly Publication of the Central Bank of Timor-Leste

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I. Development of the Balance of Payments

According to the IMF's balance of payments manual, by definition, the balance of payments is a statistical statement that systematically summarizes, for a specific time period, the economic transactions of an economy with the rest of the world. Transactions, for the most part between residents and nonresidents, consist of those involving goods, services, and income; those involving financial claims on, and liabilities to, the rest of the world; and those (such as gifts) classified as transfers, which involve offsetting entries to balance—in an accounting sense—one-sided transactions.

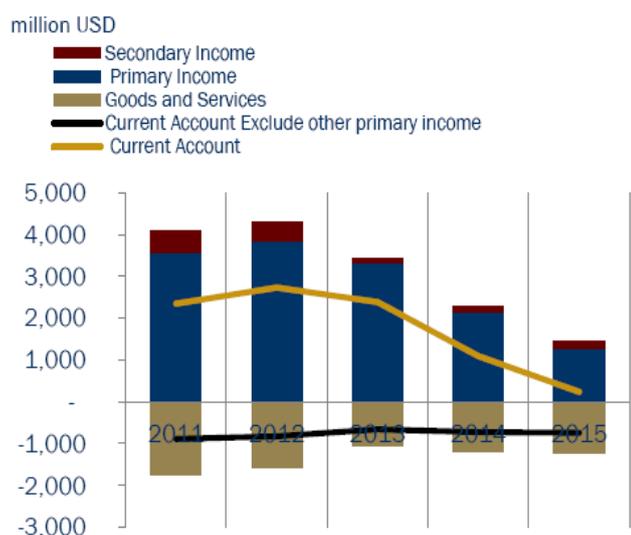
Hence, in the balance of payments there are accounting system recording applied, which is based on the

double entry principle with every item booked as a credit and a debit. Therefore, the overall result will be in balance and the equation for the balance of payments should be zero.

A term that in general is often argued is a deficit or surplus in the balance of payments. The registration of a current account deficit essentially means that a country spends more than it produces in a given period. The difference between absorption at home and domestic production constitutes the accumulation of debt or the sale of domestic assets to non-residents.

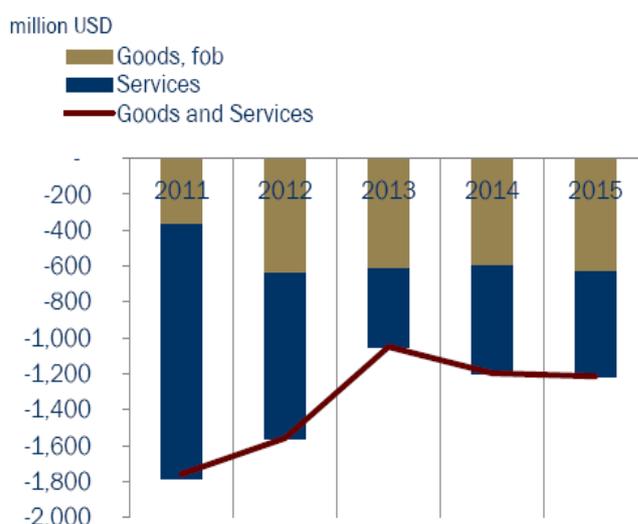
In fact, the current account of Timor-Leste's balance of payments statistics has demonstrated a remarkable sign of surplus while declining. The current account reached its highest level in 2012 of USD 2.7

Chart 1
TL BOP Current Account



Source: BCTL

Chart 2
TL BOP Goods and Services



Source: BCTL

billion, while continues declining up to just USD 240 million in 2015, recording a 91.3% decline over the period. We have to recognized that, this current account surplus mainly was due to the incoming revenue received from the oil and gas, currently treated as primary income in the Timor-Leste's balance of payment statistics.

It is inevitable that the decline in world oil prices has had a negative effect on oil revenues, and as evidence the deterioration in the current account surplus in Timor-Leste's balance of payments statistics.

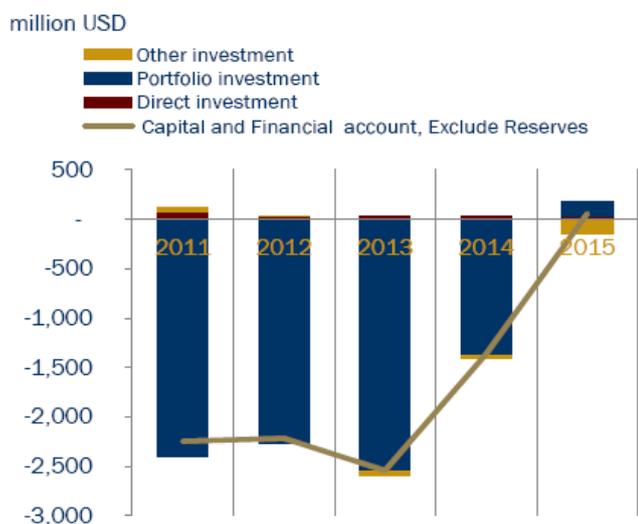
The current account become deficit, when it excluded the primary income, as the country's import of goods and services are significantly high. In average during 5 year from 2011, the deficit of goods and services reached USD 1.4 billion per year, resulting an averages current account's deficit of US770 million during that period, representing 58% of non-oil GDP during that 5 years. This essentially means that Timor-Leste is spend more than it produces during that period. By contrast, Timor-Leste will produce more than spend when we include the oil and gas revenue.

For the balance in Timor-Leste's balance of payments statistics, we should included all transactions, means the current account is surplus or positive while the capital and financial account is negative. However we are interested, in this analysis, to see what should be our capital and financial account when we exclude the oil and gas revenue.

A negative current account balance requires a positive capital and financial account and this says that the holding of domestic assets by foreigners must increase. The simple rule states: when the residents of a country (individuals, businesses, and government) sell more assets to foreigners than they buy from foreigners, the capital and financial account will be positive.

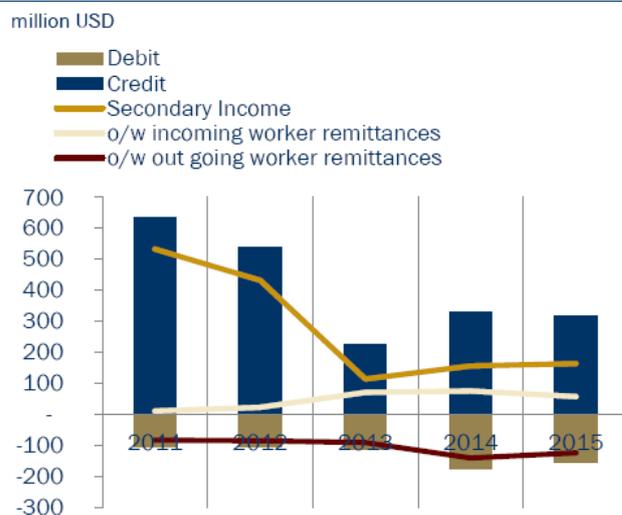
By looking to the average (5 years) deficit of Timor-Leste's current account balance of USD 770 million (current account excluded primary income), means that Timor-Leste should have in its capital and financial account a positive balance, in average during that 5 years, of USD 860 million. For the balance, in accounting purposes if necessity, it required an additional amount of foreign investment in the country of USD 2.5 billion. In the other word, Timor-Leste is required the additional holding of domestic assets by foreigners by that amount, which to be use to buy the goods and services imported. By contrast, to reduce it, additional production of goods and services in the country is required, at least to substitute and reduce both the import of goods and services. Another policy that could be designed is reducing public spending to reduce the demand in the economy. It is well note that this policy will conflict with other macroeconomic objectives, as with lower aggregate demand (AD), growth is likely to fall hence will causing higher unemployment. However, a policy may need to be consider to improve the country current account deficit.

Chart 3
TL BOP Capital and Financial Account



Source: BCTL

Chart 4
TL BOP Secondary Income



Source: BCTL

Let's see the development of the secondary income, the current transfer. In fact, there is more incoming transfer than outgoing and that contributed to the surplus of current transfer account, while declining. Large incoming transfers were the result of the grants received from the donors' country to Timor-Leste, and it was actually declining. From these transfer there is incoming and outgoing worker remittances. The increasing of Timorese workers' abroad has resulting in the increase in the incoming worker remittances, estimated be representing 4% of non-oil GDP in 2015. There is also numbers of foreigners' workers in the country, as shown in the high value of outgoing remittances, in fact it is higher than incoming remittances.

II. Recent Monetary and Credit Development

II. a. Money Supply

Broad money growth has slowing down in the quarter, while the loan growth is declining. The broad money has decelerated again after having experienced recovering in two consecutive quarter. The domestic economic activities were the main driver of the decrease in the growth rate of broad money, reflecting the slowdown in the growth rate of deposits, both of the enterprises and individuals'. After recorded an acceleration of the growth rate in the last quarter, M2 has slowed down again, has reduced from 27% to 15% in September quarter. The decrease, in some extend, was followed by reduction in the other depository corpora-

tions' net foreign assets (NFA), and the decline in the credit development from the banking system to private sector.

As the intermediary between those that who has excess of the fund and those who lack of fund, banks have been performed their role by receiving and channeling the fund from and to the private sector in the economy, while for some reason they have to also diversify their assets by deposit or investing the funds abroad.

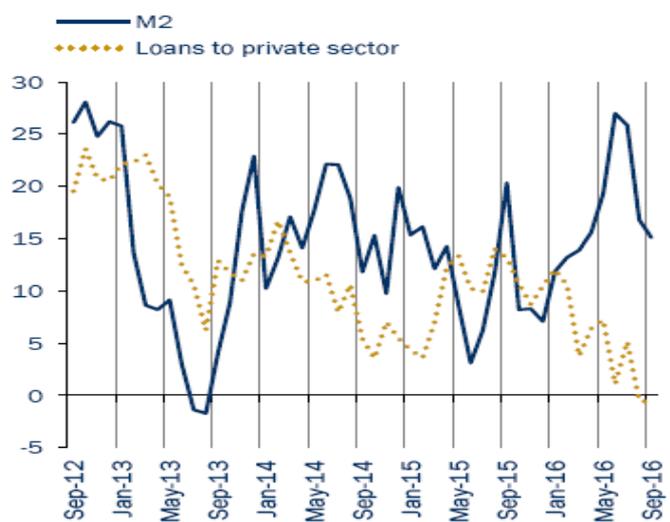
In fact, the growth rate of the deposits of both corporations and individuals were slowing down. The annual growth rate of deposits of corporations decreased to 21% compared to 28.4% growth rate observed in the previous quarter. Further, the individuals' deposits grew by 12% after having recorded an increased of 26.4% in the last quarter.

Transferable deposits, the demand deposits, continues as the main driver to the growth rate of the broad money, M2, in the quarter, has grown by 22%, followed by an increase of 37.6% observed in the last June quarter, has contributed by 12.3% to the deceleration in growth rate of M2 in the quarter of September.

The time and savings deposits, or the term used in monetary statistics as other deposits, in conjunction, revealed a slow down growth of 5.2% reversing the increase growth of 14% in the last June quarter. Together they contributed by 2.2% to the slowdown of the M2 in the quarter. The currency in circulation

Chart 5
TL Broad money growth

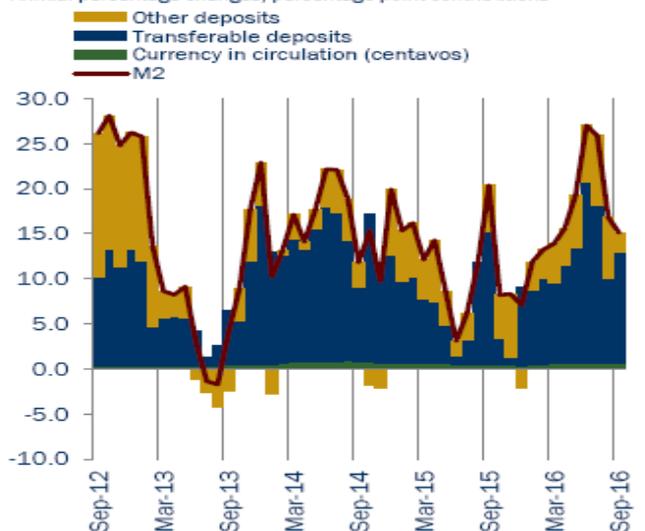
Year on year percentage changes



Source: BCTL

Chart 6
TL M2 and its components

Annual percentage changes; percentage point contributions



Source: BCTL

(centavos), while slowing but continues grow, rising by 26.6%, followed an increase of 28.5% in the last quarter, contributed by 0.6% to the M2 growth.

The annual growth rate of commercial banks' credit to private sector continued with the tendency of declining, has reduced by 0.6% in the quarter, after recorded a growth rate of 1.1% in the last quarter of June 2016. Loan growth continue deteriorate during this period of 2016. This total amount of credit in September quarter 2016 represented 35% of M2, decreased from 37% recorded in the last quarter and 41% compared to the same quarter last year. The reduction mostly was due to the decline in the growth rate of the credit, while the deposit growth just slow down. The conditions to push banks to continue tighten their terms and condition of the credit for approving loans still high. As the result, elevating the foreign assets.

II. b. Net Foreign Assets

The annual growth rate of net foreign assets (NFA) for the financial system or the depository corporations has accelerated, rose by 37%, followed a 35% increased observed in the June quarter of 2016. In fact, this progress was driven mainly by increase in the other depository corporations' NFAs, with some contribution from the central banks' NFS. The Central bank's NFAs recovered again by 2% after recorded a negative growth of 9.8% in the last June quarter, contributed by 0.6% to

the increased in the growth rate oh total NFA. The growth rate of other depository corporations' NFAs was slowed down, but still with large expansion, grew by 50.4% in September quarter, contributed by 36% to the total growth of the NFA.

The main driver of the changes in the central banks' NFAs was the increase in the growth rate of its claims on non-residents, both in transferable and other deposit, rose by 119% and 14% respectively. In part, its liabilities decreased by 0.5%, followed a decline of 0.8% observed in the last quarter.

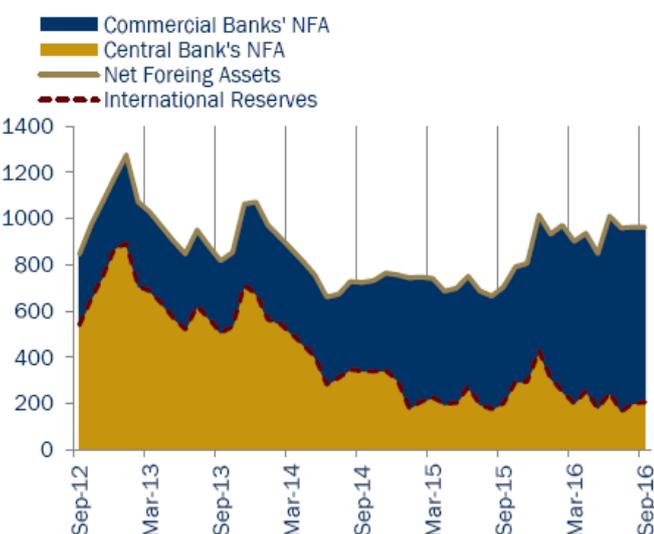
In fact, NFA of other depository corporations has expanded during the last three years, oversize the central banks' NFAs. The increased was mainly due to the development in its transferable and other deposits, rose by 42% and 50.6% respectively. The growth rate of other deposits was slowing down from 68.7% increase observed in the last June quarter. Cash holding has reduced by 25.7% after recorded a growth rate of 14% in June quarter, contributed negatively of 2% to the slow down in the growth rate of the other depository corporations' NFA. Its liabilities has contributed to slowing down of the NFA, with a negative growth of 7.6%, which contributed -1.1% to the growth rate of the NFA.

II. c. Net Domestic Assets

The domestic assets composed by claims on central

Chart 7
TL Net Foreign Assets

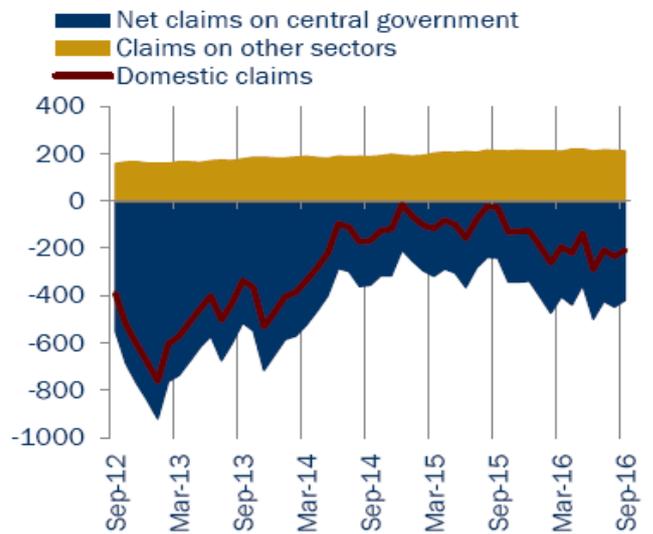
in million USD



Source: BCTL

Chart 8
TL Domestic Claims

In million USD



Source: BCTL

government (net) and claims on private sector. Net claims on central government contain credit and liabilities to central government from the financial system.

The annual growth of Domestic Claims has a remarkable increase in the September quarter of 2016, rose by more than 600% followed an increase of 84% observed in the last June quarter. The liabilities of the depository corporation, both the central bank and commercial banks, to the central government are components with the large contribution to the movement of the domestic claims.

In fact the commercial banks liabilities to the central government start to lead the growth rate of domestic claim, representing 56.7% of the total liability of depository corporations in the quarter, with the annual growth of 96%, or contributed about 48.6% to the growth rate of total liabilities. On the other hand, the liabilities of central bank increased by 52.5%, contributed 26% to the growth rate of total liabilities of the depository corporations.

While, the claims on private sector, has a negative annual growth in the quarter, declined by 0.6% after recorded a slow down growth of 1.1% in June quarter. This sector therefore contributed by 4.4% to the growth rate of total domestic claim in the quarter.

From the total claims on private sector, loans represent about 98%, of which commercial banks occupied 87.5% in the quarter and the rest was from other mi-

crofinance institutions. In fact, these total loans has declined by 0.5% while commercial banks loans to the private sector recorded a reduction of 4.1%, down from 14.5% increase observed in the last quarter of June 2016.

A beneficial part of subdued decrease in the credit to private sector from the commercial banks is accounted by sharp decline in the non-performing loans, which has an annual reduction of 37%, followed a fall of 33% in the last June quarter. Provision for loan losses has also declined, reduces by 28.7% in the quarter under review, representing 22% of the total gross credit to the private sector.

The individual sector continues become the main sector that has the higher share of credit from the commercial banks, representing 43.2% of the total credit in the quarter, decreased from 48% recorded in the last quarter, as the lending to this sector was declining, has reduced by 8%, which contributed by 3.6% to the decline in the total credit growth.

Two sector that receive more credit in the quarter and has positive growth to brake the sharp decline in the total credit were the trade and finance and tourism and services sector. Trade and finance sector, recorded a growth rate of 79.5%, and contributed by 6.6% to the total credit growth, representing the third larger share of total credit in the quarter, placed at 15.5%.

The tourism and services sector were recorded as the

Table 1
TL Loans to Private Sector

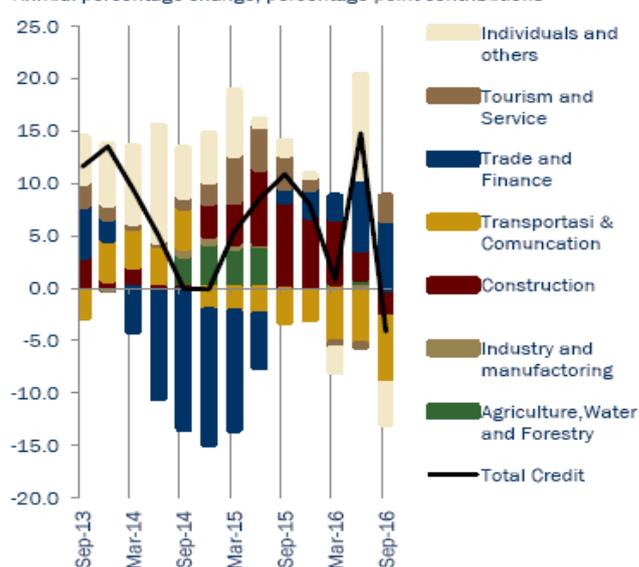
in thousand USD

Sector	2015	2016		Change from Sept 2015	% point to contribution	Sept Share (%)
	Set	Jun	Sept			
Agriculture, Water and Forestry	6,516	10,378	5,472	-16.0	-0.5	3.0
Industry and manufacturing	2,677	2,433	2,607	-2.6	0.0	1.4
Construction	52,181	53,218	47,799	-8.4	-2.3	25.9
Transport & Comuncation	14,239	6,089	2,020	-85.8	-6.3	1.1
Trade and Finance	16,000	25,738	28,725	79.5	6.6	15.5
Tourism and Service	14,262	14,768	18,326	28.5	2.1	9.9
Individuals	86,817	104,079	79,785	-8.1	-3.6	43.2
Total	192,692	216,703	184,734	-4.1	-4.1	100

Source: Commercial banks and BCTL analysis

Chart 9
TI Loans to private sector

Annual percentage change; percentage point contributions



Source: Commercial banks and BCTL analysis

second sector that received more credits in the quarter, shown an expansion of 28.5% with 2% contribution to the total growth of credit. In fact the tourism and service sector has shown negative growth consecutively in the last two quarter, however it seems that the nominal credit for this sector continue shown an increasing tendency. We believe that the banking system is on track with the government objective to invest in the tourism sector as an priority sector to achieve its goal as an upper middle income country by 2030.

Unfortunately, most of the other sectors had the negative growth in the quarter, and therefore contributed to the decline in the growth rate of the total credit conceded. The credit to agriculture sector has dropped again in the quarter, recorded a reduction of 16%, after performed an increase growth of 22.3% in the last quarter of June. The industry and manufacturing sector continue with decline trend, has reduced by 2.6%, after record a reduction of 26.6% in the last quarter. This sector and transport and communication sector are sectors that representing the smallest share of the total credit in the economy for the quarter, placed at 1.4% and 1.1% respectively.

The effort continues been made to support the expansion of the credit to the economy, include the hard effort in reducing the non performing loans by commercial banks.

II. d. Interest Rate

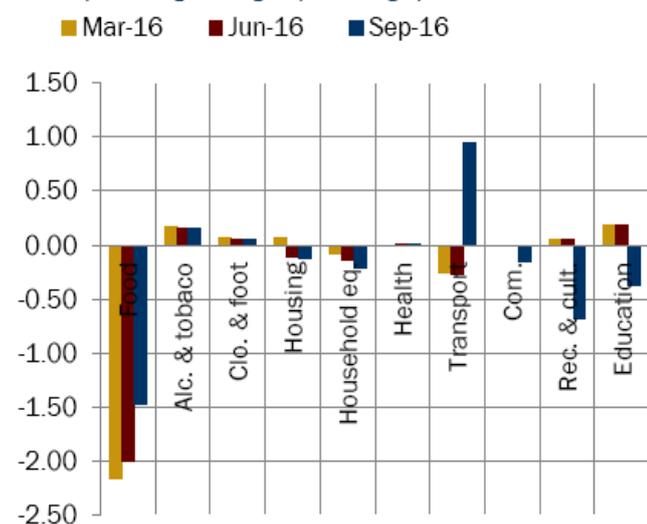
There are some risk are considered when the money lender or banks will lend the money. Two of them are the risk of borrower may not pay back the loan and the risk of inflation. So, the banks or the lender will assume a risk that the borrower may not pay back the loan. It is therefore, the interest rate provides a certain compensation for bearing risk. In terms of the inflation risk, it normally considered that the price of goods and services will increase in the future when the loan is paid back. Thus, the money's original purchasing power would decrease. Therefore, the interest rate that banks will applied protects against future rises in inflation. We are certainly assured that commercial banks in Timor-Leste are highly taking into consideration these risk in determining their lending rate, especially the risk of borrower may not pay back the loan, we believe the risk of premium is applied, with some moderate consideration to the inflation risk. Adding to the factors in which commercial banks in Timor-Leste determining the interest rate, the weighted average interest rate of loan in the country stood at 14.5% in September quarter, increase from 14.3% observes in the last quarter.

II. e. Price and inflation

The headline inflation continues with the negative rate up to September 2016. According to the General

Chart 10
TL Inflation (Dili)

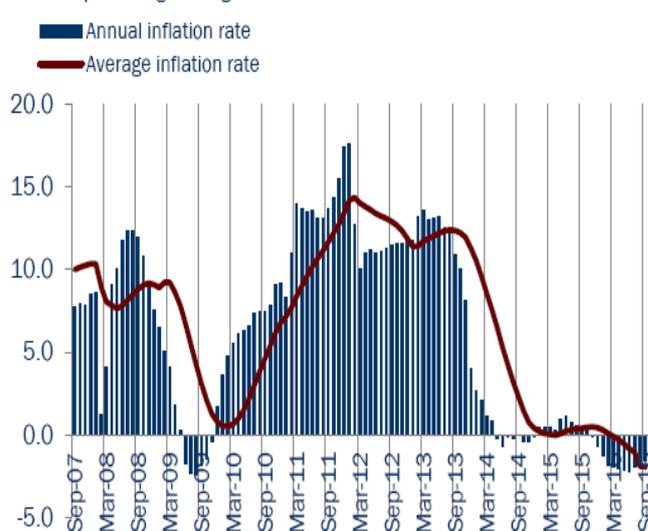
Annual percentage changes; percentage point contributions



Sources: General Directorate of Statistics and BCTL analysis

Chart 11
TL Inflation (Dili)

Annual percentage changes



Sources: General Directorate of Statistics and BCTL analysis

Directorate of Statistics of Timor-Leste, the annual CPI inflation rate (Dili) increased to -1.5% in September 2016, from -2.2% in June. This was mostly the result of upsurge in the price of goods with significant weighted within the CPI basket, the food price and mostly the transportation cost, while there were still decline in others related price of goods and services, however does not influence too much the headline inflation as its weighted too small.

The transportation cost reflected the main change in the quarter. Transport related prices increase by 14.5% compared to the decline of 5% recorded in June quarter. Contributed by 0.95% to the recover in the decline of inflation rate in the quarter. In fact energy price, the WTI crude oil prices, has increase compared to first three months of 2016.

The price of food still declined but slowed down, has reduced by 2.3% compared to 3.1% recorded in the last quarter. Food items contributed by -1.5% to the decline in global inflation, compared to -2% in June.

III. Commercial Banks

The total asset of the banking system and its key elements continue posted strong growth; particularly the deposit base, while lending to private sector consistently stood with slight growth in a long period of time, in fact decreased in September quarter 2016 compared with correspondent quarter of 2015.

Table 2
Highlights of the Banking System

in million USD

	Sep-15	Jun-16	Sep-16	change from Sept 15	change from Jun 16
Total Assets	806	1,072	1,046	30	-2
Liquid Assets	652	902	876	34	-3
Investments	4	9	9	126	0
Total Loans	193	188	185	-4	-2
Non-performing loans	45	31	28	-37	-9
Provision for Loan Losses	56	43	40	-29	-7
Total Liabilities	766	1,023	996	30	-3
Deposits	627	834	818	31	-2
Capital	40	49	50	25	2
Liquid assets requirement (15%)	115	153	149	30	-3
Income	35	28	39	11	41
Expenses	31	18	26	-16	43
Net income	4	9	13	237	37
ROA (%)	0.5	0.9	1.2		

Source: Commercial Banks balance sheets and BCTL analysis

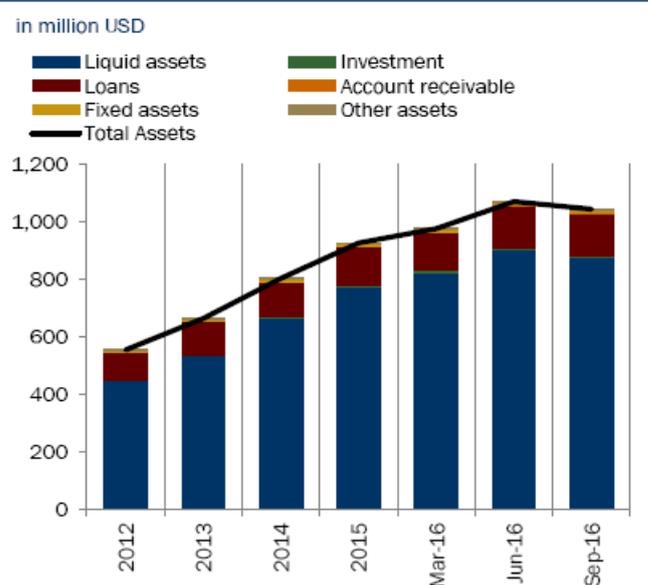
The total assets of the banking system showed a net expansion of USD240 million during the year from September 2015 and stood at USD1,046 million in September 2016. Hence, the assets of the banking system increased by 30%, followed an upsurge of 40% recorded in the last June quarter. In the same time, the annual trend of total deposits of the banking system continue to increase, has achieved USD818 million at the end of September 2016. Indicate an annual growth of 31%, after revealed a 41.6% growth in the last June quarter, denote about 78.3% of total assets at the end of September 2016. While, most of the deposits are placed abroad. The placement abroad recorded about 95.5% of total deposits or about 74.7% of total assets.

Total lending of commercial banks up to the quarter of September 2016 were of USD184.7 million, just recorded a negative annual growth of -4%, followed a decline growth of 0.5% at the end of June 2016.

The income during the quarter of September 2016, as percentage of assets (RoA, or Return on Assets), was of 1.2%, rising from 0.9% recorded at last quarter of June 2016.

The banks continue to have liquidity ratios above the minimum required by the BCTL, with an excess liquidity ratios of 73% in the quarter under review. The requirement actual held was of USD875.5 million compared to the liquid assets required of USD149.4 million (15%).

Chart 12
TL Banking Systems; Assets Development



Source: BCTL

Table 3
TL Balance of Payments Statistics

In million US Dollars					
	2011	2012	2013	2014	2015
Current Account Exclude other primary income	- 888	- 823	- 660	- 724	- 740
I. Current Account	2,352	2,736	2,390	1,093	239
Goods and Services	- 1,758	- 1,558	- 1,051	- 1,197	- 1,215
Goods, fob	- 373	- 638	- 620	- 603	- 635
Exports of goods, fob	29	33	18	16	18
Imports of goods, fob	- 402	- 672	- 637	- 618	- 653
Services	- 1,415	- 920	- 431	- 594	- 580
Exports of services	79	69	70	74	74
o/w: Transportation	1	1	1	1	2
Travel	24	21	29	35	51
Imports of services	- 1,494	- 989	- 501	- 668	- 653
o/w: Transportation	- 45	- 76	- 71	- 67	- 72
Travel	- 49	- 73	- 40	- 93	- 83
Construction	-	- 276	- 160	- 200	- 157
Primary Income	3,577	3,862	3,327	2,134	1,290
o/w: Other primary income (income from	3,240	3,559	3,050	1,817	979
Secondary Income	533	432	114	156	164
Credit	636	538	228	332	319
o/w: incoming worker remittances	11	23	71	76	57
Debit	- 103	- 106	- 114	- 175	- 155
o/w: out going worker remittances	- 83	- 84	- 91	- 140	- 124
II. Capital and Financial account, Exclude Reserves	- 2,249	- 2,220	- 2,544	- 1,364	58
Capital account	26	23	20	14	29
Financial account	- 2,275	- 2,243	- 2,564	- 1,378	29
Direct investment	80	26	37	37	30
Portfolio investment	- 2,401	- 2,274	- 2,553	- 1,385	151
o/w: PF investment abroad	- 2,407	- 2,280	- 2,556	- 1,385	151
Other investment	46	5	48	30	152
Grand Total (I+II)	103	516	- 154	- 271	296
III. Errors and omissions	- 48	- 94	- 43	- 105	- 77
IV. Change in Reserve Assets	- 55	- 422	197	376	- 220
Global result (I + II + III + IV)	0.00	-	-	-	0.00
Memorandum Item					
a) Reserve Assets Position	462	884	687	311	438
b) Change in Reserve Assets+Net Portfolio Investment (Petroleum Fund)	2,462	2,704	2,587	1,384	- 151
c) Sovereign Wealth Fund (Petroleum Fund) Assets Position Value as of end-period	9,310	11,775	14,952	16,539	16,218
Current account (in percentage of non-oil GDP)	205	212	182	78	16

Source: Banco Central de Timor-Leste (BCTL)

Table 4
TI Monetary Survey

in millions of USD

	Sep-15	Jun-16	Sep-16	% point cont. % change	
				1 Y ago	1 Y ago
NET FOREIGN ASSETS	704.57	1011.81	962.90	36.7	36.7
CLAIMS ON NONRESIDENTS	785.17	1091.31	1038.14	35.9	32.2
LIABILITIES TO NONRESIDENTS	-80.60	-79.50	-75.24	0.8	-6.7
DOMESTIC CLAIMS	-27.99	-289.06	-208.50	644.9	644.9
NET CLAIMS ON CENTRAL GOVERNMENT	-240.35	-500.14	-419.61	640.5	74.6
CLAIMS ON CENTRAL GOVERNMENT	0.00	0.00	0.00	0.0	126.8
LIABILITIES TO CENTRAL GOVERNMENT	-240.35	-500.14	-419.61	74.6	74.6
CLAIMS ON OTHER SECTORS	212.36	211.08	211.11	4.4	-0.6
CLAIMS ON PRIVATE SECTOR	212.36	211.08	211.11	-0.6	-0.6
TOTAL ASSETS	676.58	722.76	754.41		11.5
BROAD MONEY LIABILITIES	522.29	576.94	601.18	15.1	15.1
CURRENCY OUTSIDE DEPOSITORY CORPORATIONS	11.19	13.66	14.16	0.6	26.6
TRANSFERABLE DEPOSITS	291.81	333.69	356.31	12.3	22.1
OTHER DEPOSITS	219.29	229.59	230.71	2.2	5.2
SECURITIES OTHER THAN SHARES					
DEPOSITS EXCLUDED FROM BROAD MONEY	0.66	3.81	2.76		318.3
LOANS	0.06	0.00	0.00		
SHARES AND OTHER EQUITY	97.67	111.96	114.67		17.4
OTHER ITEMS (NET)	55.94	30.05	35.80		-36.0
TOTAL LIABILITIES	676.62	722.76	754.41		11.5

Source: BCTL

Memorandum item: Petroleum Fund Assets 16,437 16,466 16,605 1.0