

Autoridade Bancária e de Pagamentos de Timor Leste
Banking and Payments Authority of East Timor (BPA)

Annual Report

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Autoridade Bancária e de Pagamentos de Timor Leste
Banking and Payments Authority of East Timor

Avenida Bispo Medeiros, PO Box 59 Dili Timor Leste

ANNUAL REPORT AND FINANCIAL STATEMENTS

Period ending 30 June 2002

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Introductory Note

It is impossible to deny the great sense of pride about the mission that has been assigned to us, but at same time we also feel a deep sense of responsibility at the moment of publication of the first Annual Report of the Banking & Payments Authority (BPA) of East Timor, in accordance with the provisions of Article 56th of Regulation n. 2001/30, which gives BPA its legal existence.

BPA was created in November 30th, 2001 by the abovementioned Regulation, so at the end of fiscal year 2001/02 (June 30th) was just seven months old. Because BPA is the successor of the former CPO (Central Payments Office), this report covers the full twelve months that composed the fiscal year and not only the short span of BPA existence.

Creating an institution the goal of which is to perform the role of a quasi central bank was always going to be a challenging endeavor. By doing this in East Timor, we have been confronted with additional difficulties: an almost complete absence of physical infrastructure (lack of proper premises for the bank operations, lack of reliable means of communications), difficulty (even impossibility) of recruiting local staff skilled and/or experienced in banking activities, scarcity of training opportunities, a small and uncharacteristic banking sector, (itself in its first steps of reconstruction after the events of 1999) and the co-existence (during a significant period) of different currencies (Australian dollar, Indonesian rupiah, Portuguese escudo, American dollar) with exchange rates that were not always consistent

The local and international staff of BPA tackled all these challenges. After enduring a difficult initial period, we believe that we can say that now BPA is well positioned to face the new tasks that the future will pose for us.

For all the positive achievements realized during the fiscal year of 2001-02 BPA acknowledges the fundamental contribution received from multi-lateral institutions (such as the International Monetary Fund and the Asian Development Bank), as well as the close cooperation with the political and administrative bodies of East Timor, namely UNTAET and its Transitional Administrator, the first and second Transitional Governments and the present Constitutional Government.

It is indisputable that in every new country (or even before it gains independence, such as East Timor until May 20th) the establishment of new institutions is always a challenging endeavour. It is also true that monetary and financial stability are of paramount importance for the general process of social and economic development. The experience of the last five years in the Southeast Asian countries showed how precious this stability is and how destructive its absence can be.

For all these reasons we consider that BPA (as the public organization with the role of quasi central bank and the mandate to preserve economic stability) has an ethical, moral and institutional obligation to do whatever is achievable to guarantee the proper functioning of East Timorese banking and financial system, thereby creating one of the necessary conditions for the progressive and sustainable elimination of the shortcomings that are still present in this country.

1 - BPA ACTIVITY

Contents

1.1 - Overview	5
1.2 – Dollarization of the national economy	7
1.3 – Department of Banking Supervision	12
<i>Box: Evolution of the East Timorese banking system</i>	<i>15</i>
1.4 – Department of Payments and Banking Operations	17
1.5 – Accounting Division	20
1.6 – IT Division	21
1.7 – Human Resources and Training Division	21
1.8 – Corporate Services Division	25
1.9 – Legal Affairs Office, Economics and Statistics Division and Internal Audit	25

1.1 – OVERVIEW

After a lengthy period of preparation and discussions, the legal document that created the Banking and Payments Authority of East Timor (BPA), Regulation n. 2001/30, was finally approved and published on November 30th, 2001. As a consequence, BPA replaced the previous Central Payments Office (CPO). It must be stressed that the legal standing of BPA, established as a “distinct autonomous public legal entity” (Section 2.1 of the Regulation), represents a clear evolution compared with the previous legal framework of CPO and was a necessary step to develop a proper environment for the activity of the institution that now performs the role of quasi central bank in East Timor.

The **legal framework** was not however fully and expeditiously translated into practical terms because the highest level of BPA’s governance (its Governing Board) was only appointed in April 2002 (with a reduced composition); at same time the position of General Manager (that was vacant at the commencement of BPA) was also only filled in April 2002.

Regardless of these limitations, BPA did not waste time in developing and consolidating its activities in order to efficiently achieve the goals that were intended to be accomplished.

It seems undeniable that the most important task during the first year of BPA’s life was the implementation of the currency policy, namely, the implementation of the US dollar as the only currency with legal tender status in East Timor.

This activity, know as “**dollarization**”, is described in more detail later in this report. It demanded the mobilization of the full strength and resources of BPA between August 2001 and April 2002 and was - we dare to say - a success even greater than our original expectations, measured by the present general and almost exclusive use of the USD as the means of payment in East Timor.

Also very promising was the development of the activity of the **Payments and Banking Operations Department**, reflected by an ever-increasing volume of operations ranging from the processing and clearing of cheques and inter-bank payment orders, the execution of domestic and international payments related with the public administration activities, the cash payment of civil servants and the important task of importing and distributing to the public and commercial banks the USD coins and banknotes needed for the smooth flow of economic transactions.

In the **Banking Supervision** area the emphasis was given to the build-up of an appropriate and modern bank-regulating framework (in the wider sense - including the money changers). Simultaneously much of effort was dedicated to the training (in-house and abroad) of the bank examiners.

The progress achieved on the **Accounting** area was remarkable, allowing an almost “real-time” use of accounting information for management purposes. This was achieved despite the difficulties arising from the changing characteristics from CPO to BPA (related with the fact that the latter is, differently from the former, an entity with financial autonomy).

The **Human Resources** and **Corporate Services** units also contributed to the development of BPA, notwithstanding their limited resources and the multiplicity of areas of responsibility of senior management until the appointment of a provisional Director of Administration, in June 2002.

The **IT Division** had the important mission of assuring that from the very beginning of BPA, our institution could benefit from the intensive use of modern information technology.

The staff of **Economic and Statistics Division**, **Legal Affairs** and **Internal Audit** were recruited very recently. For this reason the contribution of these areas to the global activity of BPA was limited. Taking into consideration the limited experience of these staff, their short time in BPA was very much used for training purposes (besides their participation in the later stages of the “dollarization process”).

1.2. - DOLLARIZATION OF THE NATIONAL ECONOMY PROGRAMME

A. Objective, Rationale and Financial

In January 2000, the USD was declared the legal tender of East Timor; as a result of the promulgation of Regulation 2000/7. It immediately meant that the business of the Transitional Government would be transacted in dollars, including salaries and revenue collection. The Central Payments Office (CPO) was charged with implementing the Regulation.

The US dollar was selected by the Timorese because it supports low inflation, keeps domestic interest rates low, encourages foreign investment, and provides a basis for strong economic growth. It is also the currency in which the majority of East Timorese exports are made, and therefore provides an element of fiscal and economic stability.

The Office of Communication and Public Information (OCPI), at that time began a public education initiative on the characteristics of the dollar, through posters and notices. The electronic media was just being developed and the reach of the campaign went barely beyond the centre of the capital city, Dili.

Alongside the US dollar, three more currencies co-circulated, viz. the Australian dollar, Indonesian Rupiah and Portuguese Escudos. For a while the Rupiah provided the small change for the US currency transactions, as only dollar notes were available locally.

With the passage of Regulation 2001/14 on 20 July 2001, an enforceable legislation became available to support an effective dollarization campaign. This regulation specified a deadline of 20 August 2001 for compliance with its provisions, including price and currency conversion.

The BPA immediately developed a major campaign to educate the public, and undertake other activities to implement the currency policy. Significant technical assistance was received from the International Monetary Fund, and financial support for the promotional elements of the project was received from USAID, and the balance of the costs being met from public funds.

Although a budget of USD 150,000 had been appropriated (which included a large provision to reflect the currency exchange risks that were being faced), the net direct cost of the dollarisation project was less than USD 10,000, after allowing for support from USAID and profits from the sale of Rupiah.

The gross direct costs of the programme – from the formation of BPA on 1 December 2001 – excluding grants, were as follows:

Travel Costs and Allowances	USD 16,276
Advertising	9,280
Consultancy Fees	10,668
Market Surveys	396
Rupiah Repatriation Costs	487
Baucau Office Costs	1,353
Promotional T-Shirts	340
Other (net)	(1,432)
Net Cost of Programme	USD 37,368

In addition, approximately USD 70,000 of promotional costs, including posters, contract staff, presentation equipment, safes and consultancy services, were funded by USAID.

B. Strategy

The CPO developed a five-point strategy to achieve the desired objectives. As a result, the dollarisation programme contained five major initiatives, each of which is discussed in further detail in the next section of this report:

1. The provision of a legislative framework for the use of the US dollar as the official currency of East Timor, and to allow the smooth repatriation of Rupiah.
2. The education of the public in the features and use of the new currency.
3. The distribution of the new currency widely throughout East Timor.
4. The withdrawal of the previous currency.
5. The enforcement of compliance with the Regulations in the usage of the US dollar.

The adoption of a strategy that addressed all aspects of currency conversion required careful planning and allocation of resources. The BPA is grateful for the contribution of technical support from the International Monetary Fund, and for the funding of the field teams staffed by Timorese nationals by USAID. The existence of a dedicated project team supplemented as required by permanent BPA staff allowed the dollarisation project to be implemented in an efficient and cost-effective manner.

C. Implementation

In order to implement this strategy the BPA, working with the government and various government agencies, designed and implemented a programme that included activities to address each component of the overall strategy, and this was developed into a series of sub-projects with activities, as follows:

1 - Regulatory and Legal Framework

In order to provide the necessary legislative and legal framework, several pieces of legislation and/or agreements were developed, including:

- ?? Regulation 2000/07 that established the US Dollar as the legal tender of East Timor
- ?? Regulation 2000/06 established the Central Payments Office as the authority responsible for the provision and distribution of currency
- ?? An Agreement was signed with Bank Indonesia to enable the opening of correspondent banking facilities, and enabled the repatriation of Rupiah bank notes and coins.
- ?? Regulation 2001/14 concerning the importation of currency, established the US dollar as the sole legal tender in East Timor.

2 - Promotional Activities

The second major activity was the education of the public in the use of the US dollar. This intensive campaign was undertaken continuously throughout East Timor for a period of ten months up to May 2002.

The campaign involved the preparation of materials and visits to all Districts and Sub-Districts, and centred on publicising the provisions of the regulations and the features of the new currency.

Highlights of the campaign were:

- ?? Direct presentations to East Timorese citizens (600 presentations attended by over 100,000 citizens)
- ?? Publicity through posters – “Dollarise it!” and “Our new Currency”, and lapel buttons “Dollarise it!”. About 100,000 posters were distributed.
- ?? Radio and television advertising – Radio UNTAET interviews and features
- ?? The production of a VCD featuring various public figures and local market identities which was broadcast and shown throughout the country.
- ?? Seminars with NGOs, business associations, and Department of Education
- ?? Dollarisation cartoon in CARE publication for schools.
- ?? Publication of market information - exchange rate and price advertisements in newspapers
- ?? Liaison with the press – Press conferences, publication of lists of “Frequently Asked Questions”

The campaign was well supported by the East Timor leadership, including politicians, administrators and church leaders. Regular meetings of the Council of Ministers in the Districts included dollarisation on their agenda, and the high profile thus achieved was determined to be a significant factor in the public’s decision to use the US dollar. The BPA wishes to acknowledge with gratitude the support of USAID funding which was provided to directly support the promotional activities in the overall programme.

3 - Supply of US Dollars

The third activity supporting the programme was the importation and supply of new currency. Making US dollars, in the form of bank notes and coins, freely available throughout East Timor became a significant activity – particularly as there are no commercial banking facilities outside Dili. The BPA sent teams throughout East Timor to make change available in markets and shops. Meantime, the introduction of the new currency was characterised by the following initiatives:

- ?? Civil service salaries were paid in US dollars throughout the country. This ensured a regular flow of US dollars to all Districts.
- ?? A major coffee growing cooperative elected to pay its suppliers in US dollars from an early stage, and the BPA provided banking and cash facilities to the cooperative to support that decision.
- ?? A coin exchange programme was introduced throughout East Timor.
- ?? Both banks operated ATMs that supplied US dollars to their accountholders.
- ?? The BPA established service points – in particular the opening of an office in Baucau to provide a temporary presence in that city for currency matters during the latter part of the promotional campaign.

4 - Withdrawal of Rupiah

The fourth activity involved the purchase and repatriation of Rupiah to Indonesia. This activity provided considerable challenges to the BPA, as a number of factors were beyond its control, such as the exchange rate, the fact that Rupiah were used to purchase commodities and goods from Indonesia, and the population at large were familiar with the Rupiah notes and coins.

An Agreement was signed with Bank Indonesia to allow the repatriation of Rupiah, and the BPA acknowledges the support and commitment of Bank Indonesia to working together with the BPA to implement the programme.

The major initiatives undertaken within this activity included:

- ?? Providing the public throughout East Timor with regular opportunities to exchange Rupiah for Dollars.
- ?? In support of this, BPA teams visited districts for a total of nearly 1,000 man-days
- ?? The BPA provided an ongoing over-the-counter service for the purchase of Rupiah in Dili
- ?? The BPA worked closely with one major bank, Banco Nacional Ultramarino, and the East Timor Currency Bureau, to collect Rupiah. BPA undertook to buy all the Rupiah purchased by these commercial enterprises.
- ?? The physical repatriation of Rupiah to Indonesia. The BPA wishes to acknowledge the part played by the UNTAET in providing transportation of the Rupiah notes and coins to Denpasar. In total, nearly 3 tonnes of Rupiah were repatriated to Indonesia through the BPA.

The ongoing commitment of BPA to the purchase of Rupiah resulted in the eventual disappearance of that currency from East Timor, except for some usage (as is to be expected) in the border areas and the enclave of Oecussi.

With the lack of a financial infrastructure, and uncertainty concerning the repatriation dates, it was not generally possible for BPA to manage the currency exposure on its Rupiah purchases. One repatriation shipment was sold forward during a period of volatility in September 2001 in order to reduce the exposure. Although BPA consistently bought back Rupiah from the East Timorese public at rates the same as those available in the Jakarta money markets (so that it was not the intention of BPA to profit from the programme), the timing of the conversion of the repatriated currency back into US dollars in Jakarta on days when the Rupiah was particularly strong enabled BPA to realise an overall profit of about USD 28,000 on its Rupiah currency purchasing activities.

5 - Monitoring, Compliance and Enforcement

The final activity supporting the overall programme was the monitoring and enforcement of compliance with the laws and requirements. For much of the dollarisation programme, BPA's emphasis was on education and persuasion of the public to use the US dollar.

The first element of this activity was to take steps to prevent the free movement of Rupiah across the border, and the East Timor Customs Services were active in this activity. Several seizures of illegal currency were made, with the seized money being deposited in the government account.

By November 2001, it was clear that there was a willingness on the part of the people to adopt the US dollar, but the commercial sector (shops, markets) was still offering goods priced in Rupiah, in general because these goods had been obtained from Indonesia. Therefore the BPA conducted a study to determine the supply chain for goods imported to East Timor, and implemented a programme of imposing sanctions on major importers.

Highlights of the compliance activities were as follows:

- ?? Seizure of restricted foreign currencies by Border Control from persons carrying more than the regulated amounts without the required permit.
- ?? Supervision of business transaction practices by BPA personnel – both informally and through formal inspections.

- ?? Obtaining market intelligence through formal and informal surveys. A major nationwide survey was undertaken by the Statistics Office in October 2001, and the results from the survey used to realign the dollarisation programme, and to focus resources on those areas where acceptance of the US dollar was low.
- ?? Administration of fines and sanctions imposed on businesses. About 20 business were sanctioned, and each of these businesses was subsequently re-visited and found to be operating in compliance with the law.
- ?? A survey of over 500 businesses nationwide in March 2002 showed that more than 91% of businesses outside the border districts were using the US dollar exclusively, and other businesses were using the US dollar in conjunction with the Rupiah. None of the businesses, including those in the border districts, were found to be using Rupiah only.

In summary, the widespread acceptance of the US dollar as the currency of choice by the public was attributed to a number of factors. First, the intense educational campaign carried out dollarization teams throughout the territory successfully informed the population about the features of the new currency. Secondly, the program greatly benefited from the visible support by the Timorese leadership through the media and during Council of Ministers' town hall meetings in the various districts. Finally, enforcement measures carried by BPA staff resulted in wider dissemination of information about the specific provisions of the new currency regulation in the country and government's clear intention to implement them without delay. Collectively, these activities have reinforced each other to build a momentum that allowed the program to be successfully concluded before the achievement of full independence of East Timor on 20 May 2002.

1.3 - DEPARTMENT OF BANKING SUPERVISION

The Department of Banking Supervision was established in June 2000. The responsibilities of the Department include the licensing, regulation and supervision of banks and currency exchange bureaux. The Department is organized into three areas: licensing, off-site examination and on-site examination. Headed by the Deputy General Manager of Supervision, the Department has five professional positions and one clerical position occupied by East Timorese staff.

Employees have been involved in the development of all areas of the Department and have been trained in all areas, although we have a person responsible for licensing and another person responsible for off-site examination.

The legal framework for banking supervision was established by Regulation 2000/8 of 25 February 2000, on the licensing and supervision of banks. The BPA has already issued 19 instructions to implement the Regulation, including five new instructions issued during this year. Those five instructions are related to business hours for banks, providing the minimum opening hours for banks during official working days; real estate investments, providing authorization for banks to engage in the financial activities of acquiring, holding and disposing of real estate investments; credit documentation, providing the basis for credit documentation; remuneration of members of the governing board and senior management of newly licensed banks; and a chart of accounts for banks operating in East Timor.

The instructions, which were given the highest priority, address the most important issues emphasized by the Basle Committee's Core Principles for effective Banking Supervision.

The Regulation 2000/5 of 20 January 2000 established the legal framework for licensing and supervision of currency exchange bureaux. An instruction on the licensing of currency exchange bureau has been in place since last year. Two additional instructions, on the qualification of administrators of currency exchange bureaux and on the reporting by currency exchange bureaux, were issued during the year in reference.

The Department was also responsible for the issue of the instructions that complemented the Regulation 2001/14 of 20 July 2001, on the official currency and legal tender of East Timor. The instructions are concerned with importation of foreign currency, licensing of currency exchange traders and transactions with foreign currency deposit accounts.

A key responsibility of the Department of Supervision is the licensing of banks and currency exchange bureaux. During the year two branches of foreign banks, fully licensed, continued to operate in East Timor, the ANZ – Australia & New Zealand Bank and Caixa Geral de Depositos, which incorporated the former BNU- Banco Nacional Ultramarino. In both cases, BPA has an agreement from the home country supervisor regarding the consolidated supervision of the bank and the inclusion of the branch in East Timor on a global consolidated basis. However, the BPA retains the authority under the Regulation to supervise the branch offices of foreign banks.

An application for a license from the Micro Finance Institution of East Timor was processed and a preliminary approval granted for the establishment of that institution under the provision of Section 2.6 of the Regulation 2000/8. In consequence, the institution cannot use the word “bank” and the total deposit liabilities cannot exceed the equivalent of one million dollars. The institution, which is being established with the technical assistance of ADB – Asian Development Bank, will concentrate its activities on micro-credit and is considered an important step towards provide banking services in the districts. The institution is owned by the Foundation for Poverty Reduction in East Timor, which Board of Trustees is composed by representatives from the ADB, the donors’ community, the government and the private sector.

The BPA issued a new license for the GlobalX Currency Exchange Bureau, which has already started business. However, after the implementation of the single currency regime, the market for currency dealers reduced and the East Timor Currency Exchange Bureau, which had been licensed in early 2001, was not operational from February 2002.

The Department of Supervision stands prepared to monitor the banking system. Basic reporting requirements have been introduced by Instructions issued by the BPA to facilitate the off-site surveillance of the banking system, including the monitoring of banks compliance with key prudential standards.

The Department has also put in place a Chart of Account for the banking system. Accounting standards and procedures, reporting and publication forms, including the required minimum notes to the financial statements, are being prepared.

An application for the analysis of bank risks has been adopted and spreadsheets have been prepared by the BPA to input the data from the bank reports.

A high priority of the Department is the development of a complete set of bank reports on the statement of conditions, “Call Report”. Based on the prudential requirements and standards of supervision, and considering the application requirements, the forms have already been planned.

Manuals on the Examination of Banks and on the Reporting of Examination Findings have been written and the staff is being trained on their use. The staff has been adequately trained to conduct on-site examinations and the first assignment is already planned and underway.

In consequence of the Regulation 2001/14 of 20 July 2001, on the official currency and legal tender of East Timor, the Department of Supervision was assigned with the responsibility of issuing the permit for physical importation of foreign currency according to the provisions of the Regulation, review any administrative decision of seizing foreign currency physically imported without a permit and enforce compliance with the Regulation.

The Regulation restricted the importation of foreign currency in cash, either notes or coins. No person is allowed to import into East Timor an affected (restricted circulation in the issuer country) or non-affected foreign currency, exceeding the equivalent of USD 500 and 2,000, respectively, as defined on the BPA Instruction CPO/CEB/2001/2 of 30 July 2001, unless such person has obtained a permit in advance from the BPA. Cash currency importation exceeding those limits was seized by the authorities.

During the year under review the BPA issued four permits for importation of Australian dollars in the total amount of AUD 1,280,000 for the payment of salaries of Australian Army when returning to Australia. Such currency was not to be circulated in East Timor.

Administrative authorities of the Customs Service were also responsible for the implementation of the Regulation. The BPA was responsible for the review of administrative decisions. The BPA received requests for review of the decisions from interested parties. As a result, a total amount equivalent to USD 8,000 has returned to the owners and the equivalent to USD 19,607 has been seized and transferred to the public revenues, after the BPA review. Such amount does not include seized money where a review from the BPA was not requested.

The Department of Supervision has proposed a draft of a Law on the Prevention of Money Laundering. As it is well known, money laundering is the process of legitimizing large sums of money derived from unlawful activities. It is a worldwide problem, which arises from the activities of so-called “organized” crimes. Information is essential to combat money laundering and the involvement of banks and other financial institutions is important to gather the information required to combat money laundering. A decree that creates a financial intelligence unit, with representatives of Police, Ministry of Justice, Ministry of Finance and Banking and Payments Authority, has also been drafted as well as the forms to report financial transactions that exceed a certain amount and any suspicious transactions.

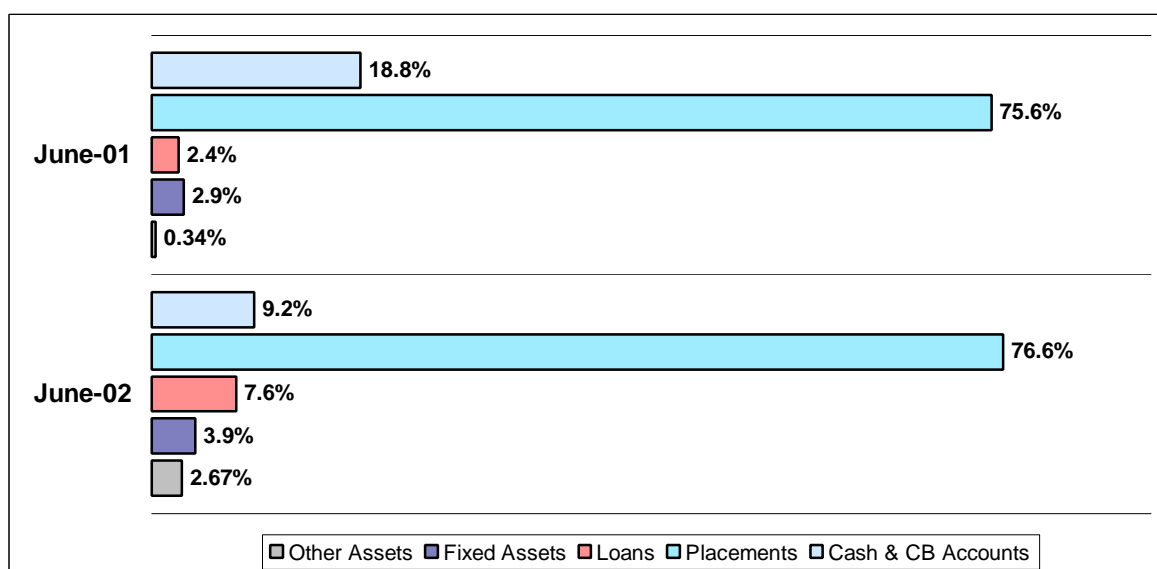
Text Box

Trends in East Timor Banking System

Composition of Assets

Total assets of the banking system as at June 30, 2002, equalled USD 57 million or increased of 1.8 per cent compared to the same date of last year. The main factor contributing to this growth as shown in Figure 1 was placement with banks that grew by 3.2 per cent reaching USD 44.0 million in June 2002 and representing 76.6 per cent of the total assets. Meanwhile, loans which represents 7.6 per cent of the total assets only, also increased significantly to USD 4.3 million as at June 2002, or 222.7 per cent when compared to June 2001. Out of this total 97.3 per cent were allocated to commerce/services sector including credit to individuals and 2.1 per cent to he agriculture. Loans to small enterprises channelled through banks but sourced from the Trust Fund for East Timor amounting USD 2.6 million and loans from Micro Finance Institution of East Timor are not included above. The data are obtained from the interim financial statement of banks, unaudited.

Figure Bx 1: Composition of Assets



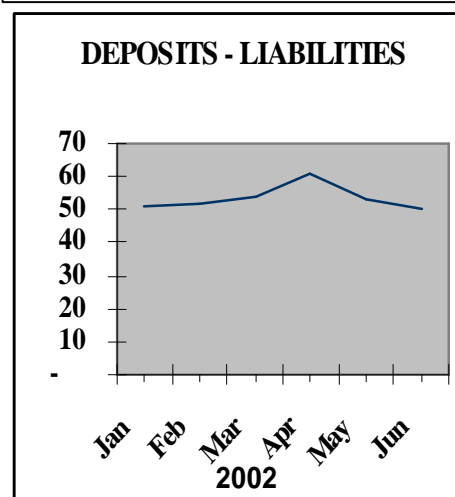
Concentration of assets in placement with banks abroad is due to general lack of legal framework related to credit activities e.g. company law, bankruptcy law, land and property law, provision on contracts, etc.

Composition of Liabilities

The composition of liabilities, as reflected in Figure 3, reveals only minor changes, with respect to the percentages represented by deposits, central bank deposits and due to other banks compared to June 2001.

Deposits from the public constituted the main source of funding for the banking sector, namely, USD 50.4 million, which represented 87.7 per cent of the total funding. With respect to the amount, 71.6 per cent was

Figure Bx2: Trend on Deposits



attributed to demand deposit, 16.7 per cent to saving deposits and 11.7 per cent to term deposits.

However, it increased by 0.4 per cent only when compared to June 2001. As can be seen in Figure 2, deposits have increased significantly on April when compared to the previous months probably due to the preparation of the celebration of the Independence Day.

Figure 3: Balance-Sheet Structure

As at June 2002 and 2001								
Assets				Liabilities				\$ 000
Items	Jun-02	Jun-01	%	Items	Jun-02	Jun-01	%	
Cash & CB Balances	5,288	10,619	-50.2%	Due to Central Bank	3,120	2,056	51.8%	
Placement with Banks Abroad	44,078	42,710	3.2%	Due to Other Banks Abroad	3,761	3,326	13.1%	
Loans and Advances	4,356	1,350	222.7%	Due to Depositors	50,432	50,240	0.4%	
Fixed Assets	2,252	1,616	39.4%	Other Liabilities	395	803	-50.8%	
Other Assets	1,537	190	708.9%	Accumulated Profits/(Losses)	- 197	60	-428.3%	
Total	57,511	56,485	1.8%	Total	57,511	56,485	1.8%	

Profitability

The main sources of income for the banking sector consist of interest income, foreign exchange gains and transaction fees. Income derived from these sources amounted USD 2.0 million as at June 2002. Compared to the same period of previous year it has increased by 25.0 per cent. Interest and similar income was registered with the amount of 0.8 million or 40.3 per cent of the gross operating income as at June 2002 and increased by 27.7 per cent when compared to the same period of last year. Meanwhile, interest expenses as at June 2002 amounted only USD 0.1 million or decreased by 25.2 per cent compared to the previous financial year.

According to bank's report interest rate for loans was relatively high, roughly 19 per cent per annum, due to the risks that the banking system challenges and the interest rate on deposits ranged from 0.25 per cent to 0.75 per cent per annum.

The administrative and personnel expenses reached USD 1.9 million by the end of June 2002 or 3.3 per cent of the total assets. Compared to the same period of year 2001 they have increased by 52.2 per cent. As a consequence of this high operational expense, the accumulated losses of the banking system at June 2002 reached USD 197,000.

1. 4.- PAYMENTS AND BANKING OPERATIONS

Government Account

During the year progress was made in the development of the account relationship with the East Timor government – primarily through the Ministry of Finance.

At the beginning of the fiscal year government cheques were issued for the first time. The great majority of the government cheques were encashed through the BPA tellers, but a number were also presented through the clearing-house, and a few through an international correspondent bank. During the year, over 3,100 government cheques were processed.

BPA also handled the government's foreign payments through its international correspondent banks, and completed about 1,250 international remittances.

The BPA, as in the previous year, continued to manage the payment of salaries to government employees. With the development of the Dili Clearing House, a campaign to encourage government employees to open accounts at commercial banks and use the direct credit facilities proved reasonably successful, and by the end of the year, over 25% of all government salary payments were being settled through the commercial banking system. The remaining salary payments continued to be made in cash, and a computer application was developed to automate the salary payment process, and to provide a greater degree of control over the teller cash balances.

Other initiatives, such as the establishment of Letter of Credit facilities, the development of the safe custody facility, support of the government's independence medallion project, and the establishment of facilities for the East Timor Customs Service to handle seized money, were also developed during the year

Currency Distribution

At the beginning of the fiscal year, East Timor had three currencies – the Indonesian Rupiah, the Australian dollar and the US dollar in widespread use. The programme for implementing the single currency regime is described elsewhere, and in association with that programme, the BPA significantly developed its currency importation and distribution programme. During the year, some USD 64 million in US bank notes, and USD 700,000 in US coins were imported and placed into circulation.

Systems to forecast the demand for currency were developed, and the vault management capability enhanced. The process of forecasting, ordering and distributing new bank notes went smoothly, and experiences of cash outages or long-term holdings of currency in excess to demand were kept to a minimum. The changing environment – brought about by the change to the USD, large movements of international staff in and out of East Timor, gave rise to significant variances in demand from month to month, though following East Timor's achievement of full independence a more stable pattern of currency usage began to emerge. The following table sets out the amount of currency imported during the fiscal year 1 July 2001 to 30 June 2002:

Table 1: US Currency Imports for Year ended 30 June 2002

Denomination	Value
Notes: USD 100	26,000,000
50	17,500,000
20	11,500,000
10	4,600,000
5	3,500,000
1	850,000
Coins: 25 cents	400,000
10 cents	200,000
5 cents	100,000
1 cent	100,000
Total	\$64,750,000

Despite BPA's promotional efforts, the one-cent coin has not been accepted by the people of East Timor, with the result that large quantities of these coins continue to be held in stock.

Up to independence, the importation of currency was being undertaken in the name of the United Nations, and since independence BPA has negotiated and established a relationship with an international bank (with United States authorities knowledge) for the ongoing supply of currency.

One consequence of the currency policy is that BPA is not only required to meet the cost of currency at face value, but is required to pay substantial transportation and insurance costs and the costs were substantially increased after the events of 11 September 2001. Aside from the share of costs borne with regard to government cash payments, BPA was obliged to pass on a fair share of the costs to the commercial banks reflecting the cost of supplying currency. The banks in turn passed the costs on to members of the public giving rise to some public concern at these costs.

Correspondent Banking

The BPA expanded its number of correspondent banks during the year to be able to undertake its payment and currency activities. In particular, account relationships were established in Jakarta for the processing of purchases of Rupiah, and to facilitate remittances to beneficiaries in Indonesia, as a service to both the government and the commercial banking sector.

In order to allow a degree of management (hedging) of the currency exposures that arose during the Rupiah purchase programme, BPA established a forward sale arrangement with a Jakarta bank, and established similar back-to-back arrangements with a commercial bank in Dili.

Towards the end of the year, BPA commenced negotiations to establish account facilities with the Federal Reserve Bank of New York to allow the further development of BPA's payments and investment activities.

Dili Clearing House

The Dili Clearing House had been established in April 2001, and developed consistently during the year. Although only a limited number of payments are cleared daily, the clearinghouse operated smoothly every business day. Values and volumes of items exchanged in the clearinghouse were as follows:

Table 2: Volume and Value—BPA Clearing House

Mês	Number		Value (USD'000) ¹		returned	
	Total	Daily average	Total	Average value	Number	Value
Julho 2001	96	4	759	7,9	-	-
Agosto	118	6	719	6,1	-	-
Setembro	163	9	1.039	6,4	-	-
Outubro	235	10	1.514	6,4	-	-
Novembro	243	12	1.073	4,4	-	-
Dezembro	254	13	992	3,9	-	-
Janeiro 2002	294	13	1.486	5,1	-	-
Fevereiro	307	15	1.840	6,0	-	-
Março	340	17	1.555	4,6	-	-
Abril	351	16	1.858	5,3	-	-
Mai	400	19	3.049	7,6	-	-
Junho 2002	405	20	2.691	6,6	-	-
Total	3.206	13,5	18.575	5,8	-	-

¹ Excludes UNTAET payroll transfer, a single item of approximately USD 1.8 million per month.

On one occasion it was necessary to invoke “failure to settle” arrangements and settlement was able to take place in an orderly manner.

Vault Facilities

The increased amounts of currency being imported – particularly in the form of coins – caused significant pressure on the existing vault facilities, and for a period of time the vaults were not large enough to hold the currency on hand. Even when the currency could be accommodated, the storage was cramped, and gave rise to difficulties in undertaking routine cash verification procedures.

The situation is still far from satisfactory, and ways and means of achieving an acceptable standard of currency storage remains a management priority.

Various initiatives to enhance security of the vaults and surrounding areas were implemented during the year.

Payments of Indonesian Civil Service Pensions

The BPA was the nominated agent in an agreement between the Indonesian Government and UNTAET (later UNMISSET) for the making of pension payments to Timorese residents who formerly worked in the Indonesian civil service. The first of the payments was received at the end of the fiscal year, and BPA working together with CISPE, UNMISSET and one of the commercial banks started the payment of pensions in the last week of June 2002.

Administrative infrastructure

The implementation of an on-line computerised accounting system from the beginning of the fiscal year significantly enhanced the quality and timeliness of financial information and controls available to the Banking & Payments Department. The implementation of new procedures based on a formal division of duties between the banking, settlement, and accounting sections, enabled a smooth and reliable flow of transaction processing to be achieved.

With the introduction of full double-entry bookkeeping some of BPA’s banking relationships were able to be realigned, and the management of financial assets and liabilities rationalised.

Cash management and operational matters were subject to regular inspections by BPA’s internal audit section.

The resulting level of processing accuracy – as measured by customer queries and complaints of which there were almost none – was excellent, and reflected the commitment of BPA’s staff to a high level of quality.

1.5 - DIVISION OF ACCOUNTING

BPA continued to consolidate the progress achieved in accounting and financial reporting systems. The implementation of a computerized accounting system started in July 2001 and went live on 1 October 2001. Management was therefore in position to upgrade from single entry to the more conventional double entry method. Up to 30 November 2001, CPO, the forerunner of BPA was accounted for as an agency through the Ministry of Planning and Finance. The first set of financial statements for BPA as an autonomous institution were prepared on accrual rather than cash basis and in accordance with International Accounting Standards for the period from 1 December 2001 to the close of the financial year on 30 June 2002. The computerized accounting package has also enhanced data verification through automated reconciliations and integrated

financial reports management. Formal procedures for daily data input, verification and reconciliation were also developed. As a result, BPA can now on daily basis generate balance sheets, profit and loss accounts, statements for Ministry of Planning & Finance and financial institutions together with debit and credit advices. In addition, the system produces periodic budgetary performance reports to support management decision-making process.

Besides the development and strengthening of internal control procedures, an accounting policy document was prepared and will be adopted by the Governing Board in the near future. This document will not only streamline and ease in the treatment of accounting transactions, but will also be a useful document in the training process and transfer of skills to National staff.

The international staff involved the accounting function of BPA also commenced a series of training seminars in accounting for staff drawn from Banking Supervision, Auditing and Accounting departments. The initial feedback from participants demonstrated that the seminars were quite useful in the capacity building process and transfer of skills to Timorese national staff.

1.6 - DIVISION OF INFORMATION TECHNOLOGY

The IT Division continued to develop the technical infrastructure of BPA throughout the year. Major projects included the implementation of an accounting package, as described elsewhere. Then, with technical support from the Asian Development Bank, custom applications were developed for the licensing of currency imports, the payment of government salaries, and an application to support bank supervision.

Later in the year a prototype payroll system for paying BPA staff in-house was developed and implemented.

A programme of acquiring desktop computers for all core staff members is now substantially advanced. This programme was supported by the donation of 10 computers from Asian Development Bank, and more recently from the transfer of a number of computers from UNTAET as part of its donation to the East Timorese government.

Three national staff were recruited in March 2002 to establish the Division. Up to that time, all IT functions had been carried out by international staff.

1.7 - HUMAN RESOURCES AND TRAINING DIVISION

Organizational Structure

The Banking and Payments Authority is organized in four departments: Banking and Payments System, Financial Institution Supervision, Accounting and Administration. The Department of Administration has just been constituted to take over the duties related to Corporate Services and Human Resources, which used to be under the authority of the heads of the two first mentioned departments.

The Research and Economics Unit as well as the legal advisor and the internal auditors report directly to the General Manager of the BPA.

The organizational chart of the Banking and Payments Authority can be seen in one of the next pages.

During the fiscal year 2001-2002, sixteen new staff members joined the BPA after the conclusion of two rounds of recruitment. As a result, the total staff of the BPA by the end of the year was composed of 41 East Timorese. The staff occupies all the middle management,

professional and clerical positions of the institution. A new round of recruitment has been launched looking for seven new staff, including the Director of Administration.

During the UNTAET mandate eight international staff had been assigned to the institution, including four senior IMF advisors, who are occupying the managerial positions of the BPA. After independence, the UN and the International Monetary Fund agreed on the continuity of the international technical assistance to the BPA for a initial period of eighteen months.

The IMF and the Asian Development Bank have also provided short-term technical assistance for specific projects as the implementation of the single currency regime and the development of central banking applications.

Training

On-the-job training has been offered to the staff by all the departments of the BPA. Formal training activities in East Timor and abroad have also been included in the training matrix for the year 2001-2002.

An expert from the Reserve Bank of Australia visited East Timor in September 2001 to determine the specific training and technical assistance needed by the BPA and which had not been provided yet. The expert's report has proven to be very useful on the planning of training needs.

Since most of the training programs offered for central banks are conducted in English, the BPA has emphasized the training on that language. Staff has been attending English classes in-house and courses organized by the Civil Service Academy. On June 30, twenty one staff were enrolled at different levels of that course.

Four staff were attached to the Banco de Portugal for training on banking supervision and Payments Systems. Two staff received similar training with the Central Bank of Finland.

The IMF – Singapore Training Institute has offered opportunities for training on “Issues in Payment Systems”, “Foreign Exchange Operations”, “Monetary and Financial Statistics” and “Balance of Payments Statistics”. The IMF has also provided training in East Timor on “Credit Quality” and “Foreign Exchange Regimes”.

The JICA – Japanese Cooperation Agency and the Singapore Cooperation Program provided training on “Financial Derivatives” and “Contemporary Development in Banking and Finance”. Two staff attended the “Banking Supervision Foundation Course” promoted by Bank Negara Malaysia.

One staff is currently enrolled in a MBA course in Australia under the AUSAID scholarship program.

Other developments

The staff of the BPA was included in the civil service payroll until March 2002. However, with UNTAET Regulation 2001/30 of 30 November 2001, which established the BPA as an autonomous institution, the Information Technology division with assistance from the Human Resources division developed its own system of staff identification, registry and payroll management. The system was put in place in April 2002. A new and more complete application is being developed now with technical assistance from the ADB.

Procedures for performance appraisal were put in place and refined during this year. The performance appraisal process, including the forms, had been fully discussed with the staff. An international expert in Human Resource provided a two-days seminar on the subject. Actual

appraisals were conducted in June and December 2001 and involved the staff self-appraisal, the appraisal by the immediate supervisor and the head of the department and finally included the discussion of the appraisal with the staff.

BPA HUMAN RESOURCES STRUCTURE
(30 June 2002)

A - Management:

General-Manager: ^{a)}

Luís Manuel Quintaneiro (from 1 April 2002)

Deputy General-Manager (Banking Supervision):

Elias Moacir da Costa (from 18 June 2000)

Director-Geral Adjunto (Payments and Banking Operations):

Samuel Vesey Robinson (from 2 July 2001)

Acting Chief Accountant: ^{b)}

Moses Tefula (from 4 June 2002)

Acting Director of Administration:

Mohamed Yassin (from 1 June 2002)

B – Local Staff [total: 41]:

11 level 5 technical staff

11 level 4 technical staff

12 level 3 technical assistants

4 level 2 Administrative staff

3 level 1 assistants

C – International Staff [total, including Management]: 7

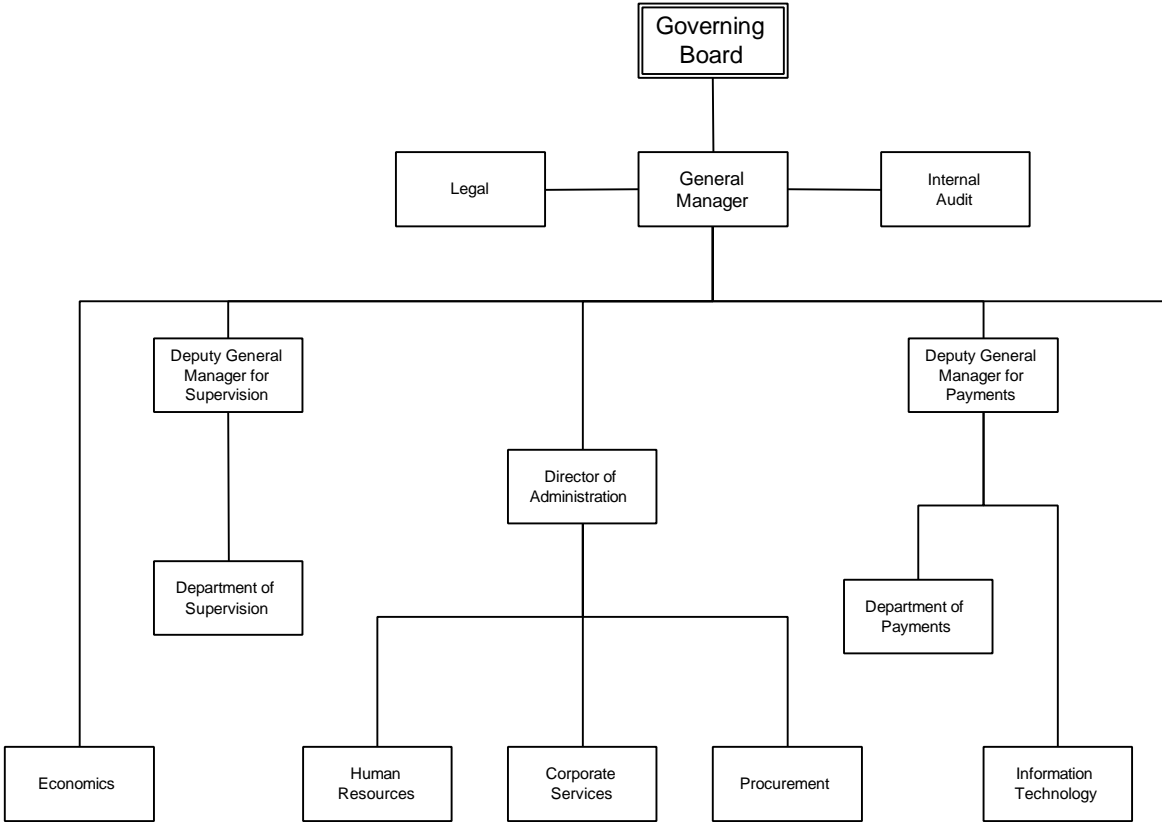
Notas:

a) The General Manager (of the then CPO) position was filled until 17/Sept/2001 by Fernando De Peralto.

b) The Chief Accountant position was filled until 31 May 2002 by Jean-Claude Pauwels.

Autoridade Bancária e de Pagamentos de Timor Leste
Banking & Payments Authority of East Timor

Organizational chart



1.8 - CORPORATE SERVICES DIVISION

The Corporate Services Division, operating with only limited numbers of staff, maintained the BPA physical infrastructure throughout the year.

In the five months to 30 November, the CPO (predecessor to BPA) was an agency of government, and most services were centralised. With the passing of the BPA Regulation BPA's autonomy was established, and with it the need to realign the administrative processes.

The time taken to implement some provisions of the BPA Regulation, in particular the transfer of budgeted funds, significantly affected the range of activities that the Corporate Services Division were able to undertake, and some delays in the implementation of necessary works were experienced.

A backup generator was installed in July 2001 to provide a continuous power supply, and contributed to improvements in productivity. The security of the BPA offices was upgraded in late 2001, and the server room was expanded to accommodate the necessary equipment to operate the BPA network and data management environment. The construction of access to the rear of the property allowed the transportation of containers of currency to the loading dock. Progress was also made on establishing a reliable water supply. Cleaning, gardening and security services were contracted out to third parties, with the management of the relationship being undertaken by Corporate Services.

As part of the process of implementing the autonomy provisions of the BPA Regulation, a Procurement Division was established in May 2002, and consultancy services obtained to develop the necessary procedures, recruitment and training programmes. By the end of the year, the procurement function was operating effectively, though still awaiting the recruitment of Timorese staff.

The division also maintained four BPA motor vehicles and two full-time drivers are on the payroll.

1.9 - LEGAL OFFICE, ECONOMICS & STATISTICS and INTERNAL AUDIT

These three functional units of BPA are still in the initial stages of implementation, either because they have only recently been created (Economics & Statistics Division) or because they have a very small number of staff. In either case the staff members are currently being trained to fulfil their functions.

In the Legal Office priority is being given to the training of its one staff member. When recognising the considerable changes that have taken place in the East Timorese legal system during the UNTAET administration and following the achievement of full independence, the need for legal training can be appreciated.

The Economics and Statistics Division was created in March 2002 with the recruitment of its first staff members. There are ambitious plans to develop this function, based on the paramount importance of developing the economic analysis skills that are necessary in a *quasi*-central bank.

The Internal Audit Unit has faced a considerable challenge, given the almost complete lack of local staff with training and experience in this field. Nonetheless, some elementary internal audit functions have been implemented, and several inspection reports were produced as a result of audit work carried out in the Payments Department and Accounting Division. BPA has been developing contacts to obtain the assistance of an international consultant to spend several months in East Timor to train the Internal audit staff and establish procedures for a reliable internal audit system. The external audit was carried out by an international audit firm.

2 – ACCOUNTING AND FINANCIAL REPORT

Contents

Statement of Compliance.....	25
Balance Sheet	26
Profit and Loss Statement	27
Cashflow Statement	28
Notes to the financial statements	29
Independent Audit Report	36

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR

STATEMENT OF COMPLIANCE

The Management of Banking and Payments Authority of East Timor declare that the Financial Statements on pages 2 to 4 and the Notes from pages 5 to 11 which form an integral part of these Statements, conform to the requirements of Regulation 2001/30 and present fairly the true financial position and performance of the Banking and Payments Authority of East Timor as at 30 June 2002.

Luis Quintaneiro
General Manager

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**BALANCE SHEET**

30 JUNE 2002

	Notes	June 2002 US \$	Nov 2001 US \$
Current Assets			
Cash and Bank	2	29,123,089	27,593,959
Accounts Receivable		200	70,639
Total Current Assets		<u>29,123,289</u>	<u>27,664,598</u>
Fixed Assets			
Fixed Assets at Cost	4	796,014	691,932
Provision for depreciation	4	(48,786)	
Net Fixed Assets		<u>747,228</u>	<u>691,932</u>
TOTAL ASSETS		<u>29,870,517</u>	<u>28,356,530</u>
Liabilities			
Deposit Liabilities	5	22,835,249	22,697,951
Other Liabilities		204,102	3,059
TOTAL LIABILITIES		<u>23,039,351</u>	<u>22,701,010</u>
NET ASSETS		<u><u>6,831,166</u></u>	<u><u>5,655,520</u></u>
Equity			
Capital Account	6	6,364,664	5,000,000
General Reserve Account		466,502	0
Currency Translation Reserve		0	(36,412)
Capital Expenditure Reserve		0	691,932
TOTAL EQUITY		<u><u>6,831,166</u></u>	<u><u>5,655,520</u></u>

The accompanying notes from pages 29 to 35 form an integral part of this statement.

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**PROFIT AND LOSS STATEMENT
FOR THE PERIOD ENDED 30 JUNE 2002**

	Notes	US \$
Income	7	
Income from Financial Assets		155,459
Income from Government		581,231
Fees and Charges		233,650
Other Income		53,069
TOTAL INCOME		1,023,409
Expenses		
Interest Expenses and Bank Charges		128,240
Distribution of Currency		277,707
Personnel Expenses		49,445
Administration Expenses	8	52,729
Depreciation of Fixed Assets		48,786
TOTAL EXPENSES		556,907
NET PROFIT		466,502
General Reserves		466,502
Retained Profit		0
Dividends		0
TOTAL		466,502

The accompanying notes from pages 29 to 35 form an integral part of this statement.

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**CASHFLOW STATEMENT
FOR THE PERIOD ENDED 30 JUNE 2002****Note 3**

	Notes	US \$
<i>Cashflow from operating activities</i>		
Operating Profit		466,502
Adjustments		
Revenue Appropriation		40,396
Depreciation		48,786
<i>Cashflows from Operating activities</i>		<u>555,684</u>
Changes in Accounts Receivable		70,439
Changes in Deposit Liabilities		137,298
Changes in Other Liabilities		201,043
Changes in Foreign Exchange Reserves		36,412
Net cash from operations		<u>1,000,876</u>
Purchase of Fixed Assets	4	(40,896)
<i>Cashflows from Financing Activities</i>		
Proceeds from Capital Injection		569,150
Change in Cash and Cash Equivalents		<u>1,529,130</u>
Opening Cash and Cash Equivalents		<u>27,593,959</u>
Closing Cash and Cash Equivalents		<u><u>29,123,089</u></u>

The accompanying notes from pages 29 to 35 form an integral part of this statement.

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR

NOTES TO THE FINANCIAL STATEMENTS

30 JUNE 2002

1. Summary of Significant Accounting Policies

(a) Basis of preparation:

The Financial Statements have been prepared in accordance with the accounting policies of the Banking and Payments Authority of East Timor (BPA) and the relevant International Accounting Standards to comply with Regulation No. 2001/30. Unless stated otherwise, the policies followed in these statements are consistent with those adopted in the previous year by the Central Payments Office (CPO), the predecessor institution to BPA.

This is the first set of financial statements presented by BPA as an autonomous institution, and they cover a period of 7 months from 1 December 2001, the date BPA was established to the close of the financial year on 30 June 2002. No comparative figures for the previous year are available for the Profit and Loss Account as CPO was accounted for as a Government agency through the Central Fiscal Authority. The comparative figures for previous year in respect of the Balance Sheet are the opening balances transferred from CPO.

(b) Unit of Account and foreign currency:

All amounts are expressed in United States dollars, the currency of the Democratic Republic of East Timor. Any minor differences are due to rounding up cents to the nearest dollar. Transactions involving foreign currencies have been converted at the rates ruling on the transaction dates. Monetary assets and liabilities have been translated at the rates of exchange ruling at the end of June 2002. The significant foreign currency exchange rates as at 30 June 2002 were; USD 1 = IDR 8,650; USD 1 = Aus \$ 1.7729.

(c) Income Recognition:

Interest income, fees & charges and other income have been recognized on accrual basis of accounting where it has been ascertained that the economic benefits will flow to the entity and that it can be reliably measured. Income from Government is recognized upon approval of the annual budgetary appropriation by Parliament.

(d) Fixed assets:

Fixed assets have been recognized under the historical cost convention.

(e) Depreciation:

Depreciation has been provided on a straight-line basis in order to *write off* the cost of depreciable fixed assets over their estimated useful life spans, using the following rates:

i.	Premises (enhancements)	5%
ii.	Plant	20%
iii.	Office equipment	12.5%
iv.	Computers & electronic equipment	25%
v.	Vehicles	20%

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR

NOTES TO THE FINANCIAL STATEMENTS

30 JUNE 2002

(f) Income Tax:

BPA is exempt from taxes on its income under the provisions of Section 61, Regulation 2001/30.

(g) Employee Entitlements:

There was no pension scheme for BPA employees during the period under review.

(h) Dividend Policy:

No dividend is payable until BPA is fully capitalized in accordance with the provisions of Section 12 of Regulation 2001/30.

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**NOTES TO THE FINANCIAL STATEMENTS**

30 JUNE 2002

2. (a) Analysis of Cash and Bank Balances (By Institutions)

	<u>Rating</u>	<u>June 2002</u>	<u>Nov 2001</u>
Domestic Cash and Bank			
Cash	AAA	5,636,968	8,680,200
Other Central Banks	Aa2	20,836,539	14,465,728
Resident Banks	Aa3	2,447,318	4,003,972
Non-Resident Banks	Aa1	1,301	20,242
Total Domestic Cash and Bank		<u>28,922,126</u>	<u>27,170,142</u>
Foreign Currency Cash and Bank			
Central Banks	B3	140,095	19,165
Foreign Cash	Aa2	1,805	1,662
Foreign Cash	B3	55,682	55,324
Resident Banks	-	0	312,685
Non-resident banks	Aa1	3,380	34,981
Total Foreign Currency Cash and Bank		<u>200,963</u>	<u>423,817</u>
TOTAL CASH AND BANK		<u>29,123,089</u>	<u>27,593,959</u>

(b) Analysis of Cash and Bank Balances (By Country exposure)

The country exposure has been determined according to the home country of the parent institution in which funds are held, or the issuing country of the currency held.

<u>Country</u>	<u>June 2002</u>	<u>Nov 2001</u>
USA	5,641,649	8,735,423
Australia	20,838,343	14,467,389
Indonesia	195,777	74,489
Portugal	2,447,318	4,316,657
TOTAL CASH AND BANK	<u>29,123,089</u>	<u>27,593,959</u>

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**NOTES TO THE FINANCIAL STATEMENTS
30 JUNE 2002****3. The Cashflow Statement**

In view of the special nature of BPA in the context of central bank operations, the Cashflow Statement does not provide significant additional information besides the disclosures already contained in the Balance Sheet and the Profit and Loss Account, but it has been presented as a matter of record to satisfy the requirements of International Accounting Standard No.7. Moreover, besides the exemption from corporate taxation, BPA is still in its formative stages and has not yet engaged in investment activities, dividend payments and management of liquidity, which would warrant disclosure on the impact of cashflows.

4. Fixed Assets

The valuation of fixed assets as at 1 December 2001 has been determined by BPA Board based on physical inventory and taking into account diminution from a commercial perspective, whereas the value as at 30 November 2001 was calculated based on the cash accounting convention. The Ministry of Planning and Finance officially transferred ownership of assets valued at USD 795,514 as part of the Government's contribution to the capital account of BPA.

The value of fixed assets excludes the land and base cost of buildings, but represents capitalized value of enhancements only.

	Premises	Plant	Office Equipment	Computer Equipment	Vehicles	Total June 2002	Total Nov 2001
Opening Balance	529,472	38,396	56,115	22,428	45,521		
Directors Valuation 1 December 2001	498,672	70,248	42,868	72,786	70,545		
Additions	0	0	11,750	29,146	0		
Disposals	0	0	0	0	0		
Depreciable Value	498,672	70,248	54,618	101,932	70,545		
Depreciation	(14,545)	(8,196)	(3,983)	(13,833)	(8,230)		
Net Book Value	484,127	62,052	50,635	88,099	62,315		

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**NOTES TO THE FINANCIAL STATEMENTS**

30 JUNE 2002

5. Liabilities and Interest Rate Risk

Deposit Liabilities	Basis of Interest	June 2002	Nov 2001
Foreign Currency Liabilities	NIL	131,279	54,724
Government of East Timor	***	19,167,741	20,476,551
Financial Institutions	***	3,536,229	2,160,369
Non-Financial Institutions	NIL	0	6,307
Total Deposit Liabilities		<u>22,835,249</u>	<u>22,697,951</u>
Other Liabilities			
Accounts Payable	Not applicable	109,846	571
Withholding Tax	Not applicable	2,352	
Pension & Salary Payments	Not applicable	91,904	
Operating Accounts	Not applicable		2,488
Total Other Liabilities		<u>204,102</u>	<u>3,059</u>
TOTAL LIABILITIES		<u>23,039,351</u>	<u>22,701,010</u>

***Federal Reserve Bank of New York Repurchase Rate less 65 basis points

All liabilities will mature within six months or less.

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**NOTES TO THE FINANCIAL STATEMENTS**

30 JUNE 2002

6. Changes in Equity

The Currency Translation Reserve and Capital Expenditure Reserve accounts were established by the Central Payments Office as a transitional arrangement to convert from cash basis to accrual accounting in compliance with Regulation 2000/6. The balance of the Capital Expenditure Reserve has been transferred to the Capital Account, and that of the Currency Exchange Reserve to the Profit and Loss statement.

Capital Account	June 2002	Nov 2001
Opening Balance	5,000,000	5,000,000
Cash Subscriptions	569,150	0
Fixed Asset Contribution	795,514	0
TOTAL	6,364,664	5,000,000
General Reserve Account		
Opening Balance	0	0
Transfer from Profit & Loss Acc	466,502	0
TOTAL	466,502	0
Currency Translation Reserve		
Opening Balance	(36,412)	0
Currency Gain (Loss)	36,412	(36,412)
TOTAL	0	(36,412)
Capital Expenditure Reserve		
Opening Balance	691,932	689,473
Additions (Transfers)	(691,932)	2,459
TOTAL	0	691,932
TOTAL EQUITY	6,831,166	5,655,520

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR**NOTES TO THE FINANCIAL STATEMENTS**

30 JUNE 2002

7. Analysis of Income**Income from Financial Assets**

Interest on deposits – Foreign Central Banks	148,377
Interest on deposits – Foreign Commercial Banks	2,266
Interest on deposits – Domestic Commercial Banks	4,816
Total Income from Financial Assets	155,459

Income from Government

Service Fee and Commission	140,600
Revenue Appropriation	440,631
Total Income from Government	581,231

Charges and Cost Recoveries

233,650

Other Income

Bank License Application Fees	3,000
Annual Bank License Fees	20,000
Currency Gain	30,069
Total Other Income	53,069

TOTAL INCOME**1,023,409****8. Administration Expenses**

Office Expenses	17,939
Travel	1,394
Training Expenses	318
Professional Fees	8,386
Vehicle Expenses	5,317
Repairs & Maintenance	12,944
Water & Energy	2,819
Housekeeping	3,612
TOTAL	52,729

9. Governing Board Members' Remuneration

The three members of the Governing Board as at 30 June 2002 are remunerated under the auspices of United Nations and IMF technical assistance programme at no cost to the Democratic Republic of East Timor, and their emoluments have not been included in the Financial Statements.

BANKING AND PAYMENTS AUTHORITY OF EAST TIMOR*Report of the external auditors*

9-11 Cavenagh Street
Darwin NT 0800
Australia

Tel 61 8 8982 1444
Fax 61 8 8982 1400

GPO Box 3470
Darwin NT 0801

INDEPENDENT AUDIT REPORT

To the Members of the Board
Banking and Payments Authority of East Timor

Scope

We have audited the financial statements of the Banking and Payments Authority of East Timor for the period ended 30 June 2002, as set out on pages 2 to 11. These financial statements are the responsibility of the Members of the Board of the Banking and Payments Authority of East Timor. Our responsibility is to express an opinion on these statements of financial position based on our audits.

We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The audit opinion expressed in this report has been formed on the above basis.

Audit Opinion

In our opinion, the financial statements present fairly, in all material aspects, the financial position of the Banking and Payments Authority of East Timor as at 30 June 2002 and the results of its operations and cash flows for the period then ended in accordance with International Accounting Standards.

Ernst & Young
Ernst & Young
Aminul Islam
Aminul Islam
Partner

DARWIN
Date: 10 October 2002

12

Liability limited by the Accountants Scheme, approved under the Professional Standards Act 1994 (NSW)

Note: the above document is a *facsimile* of the original; the BPA accounts to which it refers to were audited from documents written in English

3 – The economy of East Timor: recent evolution

Contents

International framework	37
Production, prices and national statistical system	39
Foreign trade	41
Exchange rate	43
Public finance and monetary issues	44

International framework

At a time of growing globalisation of international economic relations, no country can think of its economy and economic policy without taking into account the evolution of the world economy, in general, and the region with which it has most of its economic exchanges, in particular. East Timor is no exception and although its situation has been largely conditioned by the exceptional situation it has experienced since 1999, the truth is that the national economic authorities and all others with an intervention in the economic process and in the decision making process of economic policies, need more and more to take into account the evolution of the global economic environment that influences the economy of East Timor. The aim of this section of the text is to give a contribution to the knowledge of this environment.

International Economy

According to the last *World Economic Outlook* published in September 2002 by the International Monetary Fund, the economic evolution at the beginning of this year seemed to point to a recovery from the slowing down that begun during the first trimester of 2000 and, as a consequence of the September 2001 events in New York, reached its lowest point in the last trimester of 2001.

However, since the end of March of this year, the international financial markets have suffered important downturns --- in the 6 months between end of March 2002 and end of September, the fall of stock market prices was about 21% in the USA and 27% in the Euro zone --- denoting a lack of trust on the part of economic agents in the consistency of the recovery of their national economies. This should occur at a slower pace than forecasted. In fact, recent estimates point to a growth of production on the more industrialised economies of 1.4% in 2002, with forecasts for an increase to up to 2.3% in 2003.

On the other hand, Asia's developing countries (which include China, India, Indonesia, Malaysia, Philippines, and Thailand) will have a steeper growth pattern than the previous group: 6.1% in 2002 and 6.3% in 2003, versus a growth of 5.6% in 2001. These rates denote a certain capacity to keep a high growth pattern in spite of a slowing down in

demand from the more industrialised countries. Part of the explanation of this fact is the growing intensification of international trade amongst East Asia countries (including Southeast Asia), giving them some ability to resist, as a group, the slowing growth in industrialised countries, where they continue to send a very important part of their exports.

This trend is equally seen inside the so-called ASEAN-4 group (which includes the Philippines, Indonesia, Malaysia and Thailand): in this group, the rate of growth, that was only 2.6% in 2001, will increase to up to 3.6% in 2002, and up to 4.2% in 2003.

So generally speaking, we can say that the economic evolution of East Timor's neighbouring countries has been positive.

Australia

Estimates are that Australia's production will grow 4% in 2002, well above the 2.6% of 2001; it should further increase to 4.2% in 2003. The main reasons for this are investment and export growth, with these growing 2% in 2002 and 8.4% in 2003.

After a long period of devaluation against the USD (from early 1997 to mid-2002), the Australian dollar (AUD) began to appreciate as a result of both the difficulties of the American currency, the positive outlook for the Australian economy and also the level of interest rates (5.1% in loans up to 3 months), higher than those at the United States (1.8%).

Indonesia

Indonesia's production experienced a slow recovery after the 1997-1998 crises, with a growth rate of 3.3% in 2001. Before the attack in Bali the forecasts for growth for 2002 and 2003 were 3.9% and 3.8%, respectively. These rates, which are the lowest in ASEAN and give an idea of the problems Indonesia is still facing in restructuring its economy, will tend to be even lower due to the consequences of the attack --- namely in the tourism sector. Another sign of difficulties in the economy is the inflation rate: 12.1% in 2001 and 10.3% in 2002.

However, these difficulties are not enough to portray a pessimist perspective of the country's economic evolution in the near future. Actually, a rise in domestic demand and some revival of exports help predict better days in the future, despite the unemployment rate being firm at high levels (6% in 2001 and 6,5% in 2002), direct foreign investment being in a clear downturn since 1998 and the predictable impact of the bombing in Bali.

As for the Rupiah (IDR) exchange rate against the American Dollar (USD), it has so far moved positively because from an average of 10255 IDR/USD in 2001, it will reach, according to some forecasts, 8864 IDR/USD at year end, due in part to the downturn of the American currency in the international market and in part to the reasonable behaviour of the Indonesian economy.

Singapore

After reaching "heaven" in 2000, when it grew at the impressive rate of 10.3% as a result of an increase of 14% in public expenditure and an 18.4% increase in exports, Singapore production came down to "hell" in 2001, with a negative rate of 2.1% of the national product. This slowdown derived from the simultaneous and significant decrease in family consumption, State expenditure, investment and exports. But the passage through "hell" was short-lived and in 2002 production should grow 4.8%, with a slight decrease (to 4.6%) in 2003. This evolution resulted in higher unemployment rates, which went up from 3.3% in 2001 to 5.1% in 2002; the forecast is that it will come down to 4.3% in 2003. This economic environment provided the way for a very slow price change: the estimate for 2002 and the projection for 2003 are - 0.5% and 1%.

The Singapore dollar (SGD) had an average annual exchange rate of 1.79 SGD to the USD. In 2002 and 2003 the average exchange rates will not be much different. This shows a great stability of the SGD/USD exchange rate, being the result of an exchange rate policy that tries to keep a stable parity between both so it doesn't harm Singapore's exports to the United States - namely in the computer sector, on which the country is very dependent.

Production, prices and national statistical system

The analysis of the economy of a country performed at a "central bank" tends to favour the study of short term versus long term structures. This text is no exception but in East Timor's case this task is particularly difficult due to the lack of sufficient pertinent statistical information.

Limitations in the availability of statistical information for economic analysis, are reason enough, to begin this analysis by emphasising the need for the country's authorities to give more importance and urgency to the passing of a law on the statistical system, and in particular, to give the public services in charge of this job --- mainly the Statistics Unit, as the coordinating body, the data collector and the authority responsible for the system -- the human and material resources necessary for the accomplishment of its mission. In the context of the country's economic situation this "demand" may seem out of proportion, but the truth is that the existence of relevant and reliable statistical data is the main tool for a good diagnosis of the economic (and social¹) situation, which, in turn, is the first phase of the process for designing an effective economic policy.

Two examples of the difficulty of analysing the economic situation are the (almost) non-existent reliable data on national accounts (production, final demand and income) and the available data on prices.

Prices

The ability to reliably calculate the growth in the CPI (Consumer Price Index) and, consequently, information about inflation, implies the use of weight coefficients that reflect the relative weights of a family's different categories of consumption items (food --- its main item ---, dwelling expenses, power, etc) in their total expenditures. But because there is no up-to-date information on these weights, the CPI now uses the weights of the family expenses from the 1995 inquiry (SUSENAS) (eg: imported rice: 21.9%; detergents: 18.9%; gas: 12.76%).

However, the evolution of East Timor since then, has certainly changed this structure but it is not known exactly how and by how much. Beyond the changes produced following the 1999 referendum --- for example, the presence of a significant expatriate community with its own consumption patterns and the imitation effect it has produced in the East Timorese community, and the increased degree of concentration of Timorese population in the main cities (particularly Dili), --- other changes have occurred during 2000 and 2001 that might have changed the consumption structure significantly: an increase in nominal income due to new and higher levels of salaries (now higher than

¹ We note that the need for gathering economic data should not be to the detriment of gathering social data, needed by other departments and social agents, e.g. information about living conditions of the population, particularly the rural, majority in the country. But the reverse is also true...

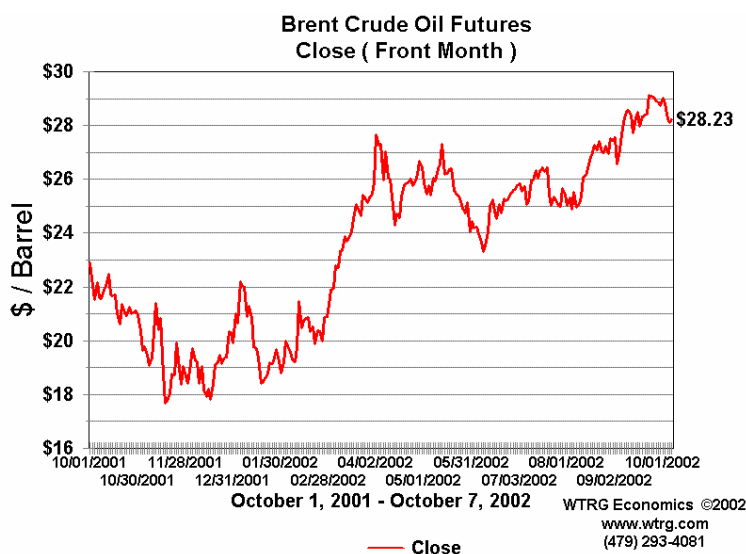
during the Indonesian administration) and to the rents paid by "internationals" to Timorese that equals, at least 3 or 4 salaries for "nationals".

As a result of these developments, it is likely that the present CPI does not reflect effectively the change in the price level of several items, and the respective proportions that are presently consumed by the Timorese population. Another sign giving cause for doubt is that the published figure for the 2001 inflation rate is 0%. However, those who lived here during the process of the rapid implementation of the USD as the national currency for payments, "feel" that that rate doesn't correspond to the reality, due both, to the fact that they "felt it" in their purchasing power, or by remembering some anecdotic cases of some businesses simply changing the currency name from "AUD" to "USD" without changing figures in spite of AUD being worth about half of the latter². If we add to this, some anecdotal cases regarding the rates of conversion from Rupiah to USD, we have a range of situations that cast doubts on the accuracy of the published inflation rate --- only possible, most probably, because the CPI deficiencies cause it to be insensitive to such phenomena.

Finally, it may be added, that in last months (start of the 2002-03 fiscal year) a new increase in some prices may have occurred in connection with a change of the Customs Taxes and Duties as well as the Service Tax. The increase of about 20% in their value was, apparently (but unduly!?) used by some businesses to raise their prices by percentages close to the tax rise, even if it was completely unjustified, as they should reflect a much lower increase (about 2 to 3%?). The conjunction of that raise with the depreciation of the USD was used as a cover to raise some prices; apparently, this raise was not visibly reflected on the CPI.

Another factor that may have contributed to the increase of several prices --- and has the tendency to become even more important if the raise of instability in the Middle East, particularly Iraq, is confirmed --- is the rise of energy prices.

In fact, the price of crude has been rising significantly since it reached USD 18.00 per barrel in November 2001. The price has actually risen since then to more than USD 28.00 per barrel of *Brent Crude*, a rise of more than 50%.



Considering that transportation costs are relatively high³ in East Timor, these increases could have had pressures for price hikes that have not been translated into CPI.

² In reality, it meant an almost doubling of the prices of goods

³ Until arrival in Dili or on the distribution around the country due to the road transport conditions in the country.

Production

Regarding national accounts, the problem is possibly even more acute because there is limited availability of data both in quantity and quality. If we consider the performance of some productive sectors and qualitative information gathered from several economic agents, it is believed that the fall in economic activity for 2002 will be worse than the figures being published in some publications on the national economy, where it is forecasted to be only -0.5%.

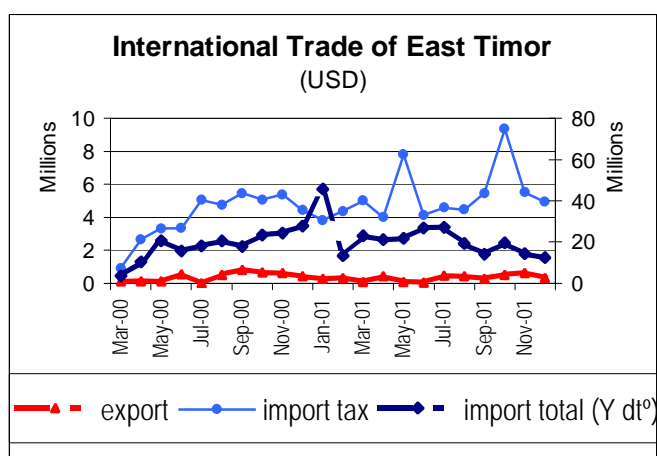
As referred to earlier, the mainly methodological remarks we make are made with the intention of calling attention, more explicitly than usually seen in other publications on the East Timor economy, not only for the paramount importance of having reliable statistical data available and the resulting need to improve the national statistical system. These remarks also call attention to the need to be very careful when analysing currently published data because they can cause errors in the diagnosis of a situation, this diagnosis being one of the most important phases in the process of setting an economic and social policy.

From the point of view of the analysis of the East Timor economic situation, these facts lead to two hypotheses that the lack of good statistical data does not allow to confirm or deny with (almost) no margin for error: it is possible that the present slow down in the economy is actually greater than the published numbers may lead one to believe, and that actual rate of inflation for 2002 may be greater than the one resulting from the published CPI due to deficiencies in its calculation. Although price hikes may have actually occurred, we recognize that a fall in economic activity is an important factor for a general deflation in the price index or, at least in some sectors, for example it has been clearly observed in the hotel and restaurant sectors.

Foreign Trade

In common with price data, the available statistics for East Timor's foreign trade do not allow a detailed analysis of the situation and the fact that a very significant part of the international goods flow has been, to date, determined by UNTAET and other institutions (e.g., NGOs) presence in East Timor does not help, adding to that difficulty of analysing the foreign trade data.

The figure at right represents the country's foreign trade, highlighting the totals for exports and imports, being those that were actually taxed⁵ – the rest being imports for consumption of UNTAET, NGOs and the Provisional Administration of East Timor and other organisations that import goods but that are tax exempt for a variety of reasons.



⁵ Ex. The ones that eventually paid the due import and transactional taxes.

Please note that total imports, which have a scale much higher than exports and actually taxed imports, must be read using the vertical axis at right. All the available values are on Table 1.

From the Table it is evident that the reduced coverage (about 10% in 2000 and 6.6% in 2001) of the total of taxed imports by total exports, being mainly coffee (73% in 2001), with the remaining being goods and equipment re-exported by UNTAET as it reduced its operations. The coverage rate of total imports by exports is insignificant, as it can be seen on Figure 1.

Naturally, this situation of East Timor foreign trade must be seen as part of the exceptional situation of the country's economic life during the past few years, and cannot be understood to be a sample of what East Timor's foreign trade structures will be in the future.

TABLE 1 - INTERNATIONAL TRADE OF EAST TIMOR (USD)

Date	Import		Export			Import tax. / total (c) / (b) % (g)	coverage rate (d) / (c) % (h)
	total (b)	taxed (c)	total (d)	coffe (e)	others (f)		
Jan-01	45,670,285	3,831,683	273,630	264,840	8,790	8.4	7.1
Fev-01	13,327,805	4,374,877	329,964	325,986	3,978	32.8	7.5
Mar-01	22,940,017	5,012,328	104,196	76,672	27,524	21.8	2.1
Abr-01	21,129,157	3,996,332	417,759	86,254	331,505	18.9	10.5
Mai-01	21,780,982	7,802,752	100,818	71,607	29,211	35.8	1.3
Jun-01	26,840,491	4,128,595	54,381	19,860	34,521	15.4	1.3
Jul-01	27,343,333	4,671,377	472,253	395,330	76,923	16.9	10.3
Ago-01	18,866,704	4,496,965	427,764	398,168	29,596	23.2	9.6
Set-01	13,930,799	4,912,573	281,710	206,825	74,885	38.7	5.2
Out-01	19,411,832	8,022,928	517,971	499,610	18,361	47.8	5.5
Nov-01	13,946,098	5,626,999	644,907	291,605	353,302	38.6	11.7
Dez-01	12,549,164	5,029,453	330,086	265,414	64,672	40.0	6.7
Jan-02	13,041,146	5,080,373				39.0	
Feb-02	15,042,094	4,135,894				27.5	
Mar-02	67,324,210	4,606,872				6.8	
Abr-02	64,443,966	5,818,876				9.0	
Mai-02	32,705,311	7,019,671				21.5	
Jun-02	15,036,084	4,869,866				32.4	

Source: Customs of East Timor

Considering the high volume of exempt imports belonging to UNTAET and other institutions, taxed imports represent only 28% in 2001 and 23% in the first half of 2002, showing a stable performance --- about USD 5.3 million monthly for 2001 and 2002--- only deviating on a few highs (May and October 2001 and May 2002). It is probable that with the progressive return of the country to normality, the rate of exempt goods will be considerably reduced, which will improve the fiscal revenue as revenues from foreign aid tends to slow down.

The five main countries where reported 2001 imports came from (total value: USD 258.4 million) were Australia, with almost USD 125 million (48.4%), Indonesia, with USD 78 million (27.5%), Singapore, with USD 14.6 million (5.7%), Portugal, with USD 8.8 million (3.4%) and Vietnam with USD 8 million (3.1%, mainly rice).

By type of product, only seven of the total imported goods (such information only exists for taxed imports) represent more than UDD 10 million each:

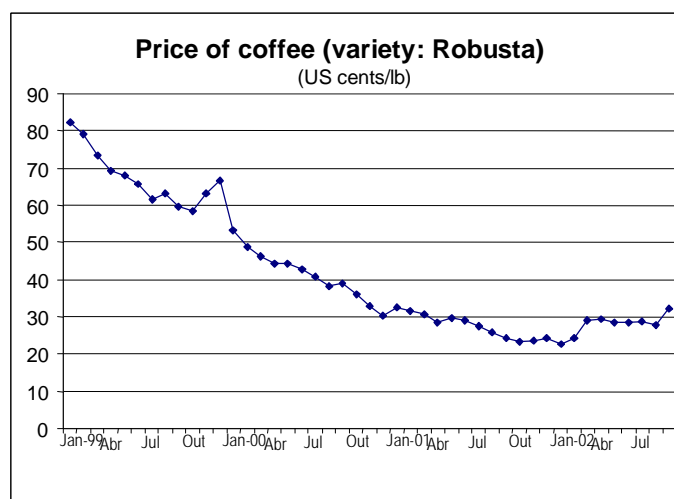
	USD
Wood and wooden articles:	30.4 million
Other vehicles and spare parts	26.9 million
Machines and electric equipment	25.5 million
Boilers, electric equipment, etc	22.3 million
Cereals	11.7 million
Paper and paper pulp	11.7 million

With less than USD 10 million there are: articles of iron and steel (USD 9.9 million); and fuels (USD 8.4 million).

With the possible exception of rice (included in the cereals), the majority of the products were for consumption by the administration of the country (furniture, vehicles, computers, paper, etc) and goods for re-construction.

Timorese exports (almost USD 4 million in 2001) were mainly to Indonesia (about USD 1.3, around a third of the total exports), Australia (USD 0.8 million, 22%), United States (USD 41 million, 25%) and Portugal (USD 0.7 million, 17%).

Coffee, which represents almost $\frac{3}{4}$ of total exports, had a decline in its monthly average price for the last few years. By Sept 2002 it was USD 32.08cts/lb pound, after hitting its lowest point at US 22.81cts in January 2002 (in January 1999 its price was USD 82.99cts per pound). Such evolution suggests a review of the coffee policy in East Timor, with a wager on quality without disregarding a downsizing of the industry (at least in those areas where coffee trees are in bad shape and where its replacement by more valuable commodities such as vanilla, would actually be an advantage).



Exchange rate

As with the information on foreign trade, East Timor main trade partners are Australia, Indonesia and Singapore. For this reason we focus on their currencies, while

following closely the progress of the USD exchange rate against the two bigger partners in international trade: European Euro (EUR) and Japanese Yen (JPY).

The depreciation of the USD against the most other currencies during the year ending September, is well illustrated on Table 2. This devaluation hit its highest by the middle of this year (Jun/Jul), when the Euro almost reached complete parity with USD and the three regional currencies reached also their best values against the USD, with Indonesian Rupiah reaching the monthly average of 8712Rp/USD in June; at the same time AUD/USD exchange rate was 1.76 and SGD/USD reached 1.75 in July. The highest rate for Yen also happened by July 2002.

		EUR/USD	JPY/USD	SGD/USD
Jul 2001		1.16	124.50	1.82
Aug 2001		1.11	121.24	1.76
Sep 2001		1.10	118.64	1.75
Oct 2001		1.11	121.44	1.81
Nov 2001		1.13	122.47	1.83
Dec 2001		1.12	127.42	1.84
Jan 2002		1.13	132.66	1.84
Feb 2002		1.15	133.59	1.83
Mar 2002		1.14	130.98	1.83
Apr 2002		1.13	130.77	1.83
May 2002		1.09	126.33	1.80
Jun 2002		1.05	123.26	1.78

Note: Prof. Werner Antweiler, Univ. of British Columbia, Vancouver BC, Canada.
The values represent the cost, in each currency, of one USD

As mentioned earlier, this USD depreciation may have been partially responsible for the increase in East Timor prices at the beginning of the second semester of this year.

More recently there has been a reverse of the trend until June/July, with USD registering small gains against several currencies. The possibility of a degradation in the international political situation can, as on other occasions, cause a rise on the demand of USD as a safeguard currency, causing its rapid appreciation. For East Timor, which depends very much on imports to be paid in this currency but that exports only small quantities of goods, this evolution may allow it to save some resources or to buy a bigger volume of foreign goods. Given the current conditions in the export sector of the country, it should have very little affect.

Public Finance and monetary issues

According to information published by an IMF Mission that was in East Timor in August 2002⁶, the global deficit of the Consolidated Fund for East Timor (CFET) was USD 20 million for 2001/02, corresponding, according to the estimates of the national accounts, to 5.4% of GDP.

This value was lower than estimated by USD 14 million due to two factors: firstly, because of a bigger than forecasted reduction in expenses on both personnel (due to a slower cycle of contracting new public employees) and current consumption of goods

⁶ See *Update of economic conditions and policy issues* prepared by the IMF Mission to ET, August 2002

(partly as a result of the transfer of UNTAET assets following the end of the mission); and on the other hand, due to the fact that fiscal revenues exceeded the budgeted amount by around USD 2 million.

East Timor's monetary situation is strongly influenced by the fact that a foreign currency (USD) was chosen as the country's legal tender. To this, it may be added that the credit availability in East Timor is in its early stages mainly because the country does not yet have the necessary legal and juridical structure to deal with economic and commercial development. From these two factors results a financial behaviour that almost entirely depends on foreign relations, not only of a commercial nature (particularly imports, as exports are very limited) but also the unilateral transfers: donor contributions and flows through international organisations active in East Timor.

Another element is the impossibility to precisely account for the amount of currency in circulation; even knowing precisely the value of the USD (notes and coins) imported and distributed by the BPA to the public and commercial banks over the fiscal year (USD 64 million), the fact that a significant percentage of imports are still being paid in cash, and the flows associated with the travelling of the international personnel, in and out of the country, being relatively large do not allow for an accurate estimate of the aggregate.

As a result, the only aggregates that can be accurately determined are the ones representing bank balances. According to these, at the end of June 2002, there were USD 50.4 million in private deposits (individuals and enterprises), of which around $\frac{3}{4}$ were current accounts. Government and other public institutions held USD 3.1 million in deposits, while the aggregate external net position of the commercial banking sector was very much in credit. Funds invested abroad were around USD 44.1 million while liabilities were only USD 3.8 million. Meanwhile BPA had assets abroad (mainly deposits in other central banks) of USD 29.1 million, more than enough to satisfy its total liabilities of USD 23 million), which essentially are government deposits.

Regarding the rate of interest observed in East Timor, it had been hoped that they would follow the behaviour of the US rates in international markets, which being low at the beginning of the year, have decreased significantly during the following 12 months, being at present the lowest in the last 4 decades. While this decrease in the interest rates has been passed on to depositors (passive operations), the same did not happen to lending, where the high interest rate (around 19%) presumably reflects the risk due to the lack of appropriate conditions (namely real guaranties and their legal structure) for the provision of credit.