

Economic Bulletin



A Quarterly Publication of the Central Bank of Timor-Leste

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I. Recent Monetary and Credit Development

I. a. Money Supply

The economic growth has been predicted to be recovered in 2014 after slowing down in the year before. The positive performance of budget execution was the main drivers of this development. Fiscal expansion during last several years besides contributed to GDP growth has been also support the monetary and credit development in the country.

The monetary data of the country shown the continued expansion in monetary development. While data of March 2015 reflected a decrease in the growth rate of broad money, however the tendency is continue with the constant growth since 2010. The decline, in some extend, was followed by both positive credit development from the banking system to private sector, and the increase in its net foreign assets (NFA), although the NFA of financial system is decreasing.

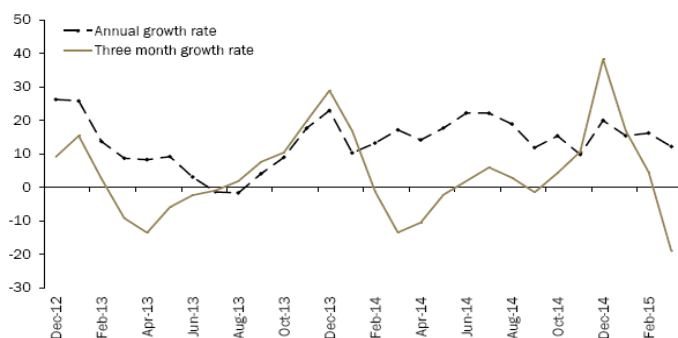
The decline of broad money also result of increase in cash withdrawal by depositors and transfer for payments of its liability. This can be seen its phenomenon in the evolution of deposit both of corporations and individuals. Deposits of corporations decline by 29% in the quarter compare to 66.7% increased in the previous quarter, while individuals' deposits were declined by 10.8% compare with 24% arose in the last quarter.

Credit to private sector grew by 7% in the quarter, in the meantime the net foreign assets of banking system grew by 40.9%. This performance has shown the risks of credit condition at our country, indicated by the flows of most of the deposits to foreigners

However, with the series of annual growth rate of other depository institution's loans to the household and mostly to private sector, the expectation of continue upward in the movement of loans to non financial corporations while small but is remarkable. In fact, the banking system continue with its concern of the issue of non-performing loans and therefore still tighten their credit analysis, and as the risk is considering maintain high cause the spread of the interest rate to be large.

The need to improve the behaviors, on the repayment of loans, in conjunction with the effort to pass the land and property law is requiring beside to reduce the risk it also could optimizing the role of financial intermediary.

Chart 1. Broad Money Growth
(Percentage change)



Source: BCTL

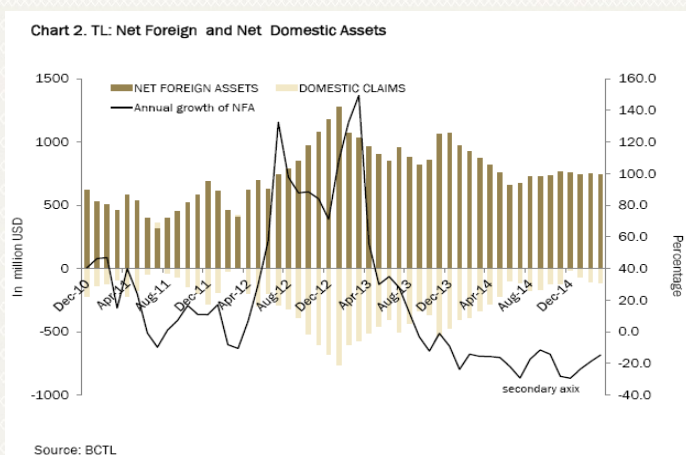
The annual growth rate of broad money rose by 12% following 20% increase in last December 2014. This affects the claims of commercial banks abroad to increase, then the net foreign assets.

The quarterly growth rate of broad money declined by 19.1%, reversing an upward growth of 38.2% observe

in the last fourth quarter of 2014. The reduction mostly was driven by all deposits include in broad money, demand, time and saving deposits. Demand deposits are the main driver, accounted about 21.6%, and saving deposit about 16.9%, while time deposit was about 14.6%. The currency in circulation (centavos) continues growing, rising by 3.6%, following a 6.8% increase in the last December 2014.

I. b. Net Foreign Assets

Further, the quarterly growth rate of net foreign assets (NFA) were declined, reduce by 2.1%, reversing an increase of 4.5% observed in the last December quarter. It also decline in terms of annual basis, reduce by 14.7% following by 29.4% in December 2014. In fact this progress mostly due to huge decrease in the BCTL's claims on nonresidents, down by 24.5% (in quarterly basis), following a 11.2% decline observes in



the last quarter. While, the others depository corporations' claims on nonresidents was increased, rose by 12.4%, following 12.8% growth observed in the last quarter.

The main driver of the evolution of BCTL's claims on nonresidents in the quarter was from the decline in its securities investment abroad. The securities declining in the quarter by 100% following a decrease of 0.02% in the last December 2014. Other deposits, while has a small amount compare to the security investment, has contributed to this downward changes, reduce by 1.6%. While, the transferable deposits and cash reserve were rising by 25% and 32.6% respectively.

The BCTL's liability to non-resident also was decreased, mostly due to exchange rate changes in the SDR allocation with the IMF, has reduced by 4.4%.

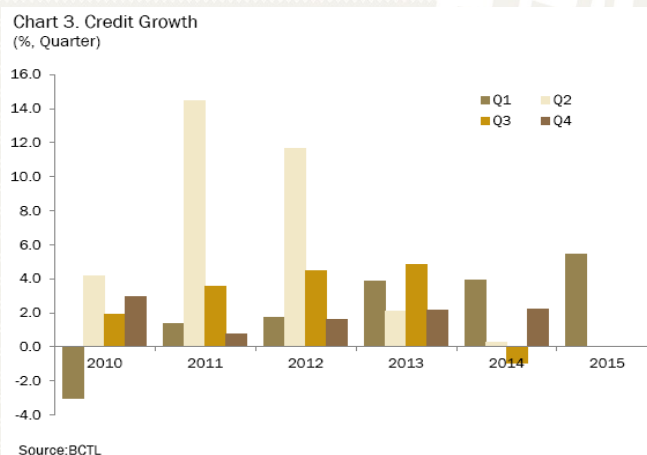
Further, the main driven of increase in the commercial banks' claims on nonresidents is the other deposit, grew by 30%. While, transferable deposits and holdings of foreign currency was declining by 13.7% and 26.9% respectively.

I. c. Net Domestic Assets

Domestic assets mostly comprises by claims on central government (net) and claims on private sector. Net claims on central government contain credit and liabilities to central government from the financial system. Actually, there is no credit from the financial system to the government of Timor-Leste, therefore the net claims on the central government in the monetary statistics point of view is negative, which means that all corresponding amount is government deposits or depository corporation liabilities to the central government. Simultaneously, claims on the private sector consist of credit to domestic private sector and others claim. If there is credit to non-resident it will be recorded on claims to non-resident under NFA.

Observing the 'Timor-Leste Monetary Survey' (table 4) we can conclude that, the 'Domestic Claims' in 1st quarter 2015 mark a huge growth, rising by 654.8% in quarterly basis to March 2015. However, it was declining in year on year basis by 65.3%. The development of this domestic claim is representing an increase in the liabilities of depository institutions, especially the central bank, to central government.

In the part of credit from commercial banks to private sectors, it is observed that there was a slight increase, while slow, in the utilization of bank credit by the private sector. The annual growth of credit rising by 5.4% in the total amount of credit awarded during the first quarter 2015, as against 9.4% in the corre-



sponding period of March 2013-2014. Part of subdued increase is accounted by sharp rise in provisioning by banks for non-performing loans, which is deducted from gross lending to arrive at the reported net figure of borrowing. On quarterly basis it increased by 5.6%.

The sector that absorb more resources in the quarter, representing 45.7% of the total credit, was the individ-

Table 1
Commercial Bank Outstanding Credit to Private Sector
(in thousand USD)

Sector	2014		2015	Change from Dec 2014	March Share (%)
	March	December	March		
Agriculture, Water and Forestry	1,334	8,280	8,389	1.3	4.5
Industry and manufacturing	2,264	3,477	3,033	-12.8	1.6
Construction	36,521	41,823	43,481	4.0	23.3
Transport & Communication	20,480	17,606	16,431	-6.7	8.8
Trade and Finance	34,899	12,724	15,199	19.5	8.1
Tourism and Service	6,978	11,363	14,848	30.7	8.0
Individuals	74,621	81,428	85,247	4.7	45.7
Total	177,097	176,701	186,628	5.6	100.0

Source: BCTL

ual sector, which increase in the growth rate during the quarter by 4.7%. The second sector that absorbed more credit was the construction with the share of 23.3%, followed by transport and communication by 8.8%, trade and finance by 8.1% and tourism and services by 8%. In fact, the Agriculture, Water and Forests, absorbing the second lowest credit from our banking system, after industry and manufacturing, record only 4.5% of the total credit.

I. d. Inflation

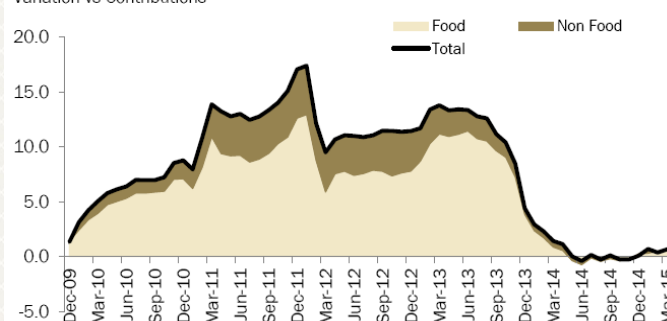
The annual inflation rate continues to slowing down since December 2013, which was of 4% after achieve, in media, for last three consecutive December of 13%. At seven successive months, start at June to December 2014, the inflation performance was negative, in average was of 0.3%. This negative inflation which continues at seven month consecutively, except September that was 0.0%, could be already considering deflation. At three month from January to March 2015 the inflation stood at 0.5% (year on year basis). The graph below has shown the deep decline in inflation after December 2013.

An analysis was performed to see the result of inflation in relation to the contribution of its components to the

headline inflation. The analysis focussed on the influence of food and non-food to headline inflation. After recalculation, the price evolution of food seems to be more affect the evolution of inflation in Timor-Leste at the whole ways of inflation's experience rather than non-food inflation. That could be reasonable as the weighted of food in the CPI basket of Timor-Leste are too high, situate at 64% of the total CPI (new series, based year = Dec. 2012).

The contribution to the evolution of inflation from items of food recorded, in average for 7 years, about 5.5%, while non-food just about 1.9%. For March 2015 food contributed about 0.6% to the slight increase of

Chart 4. TL - Total Inflation
Variation vs Contributions

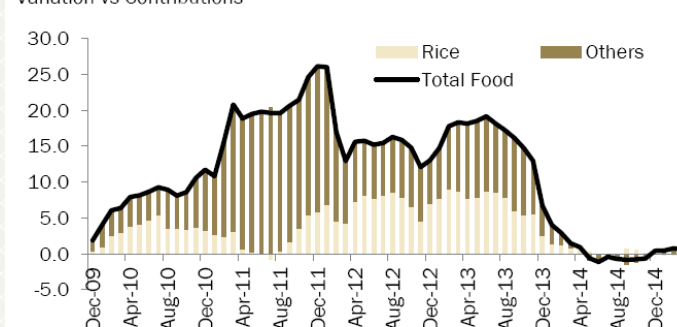


Source: National Directorate of Statistics and Staff BCTL analysis

the headline inflation, while non-food about 0.1%. The differences of 0.2% could be due to the monthly change in the weighted of CPI. So, the interpretation of that analysis is that; the increase in the headline inflation mostly is contributed by food and its decline also is affected by slowing down in the price of food.

The analysis on contribution of food inflation could be breakdown in to items of rice and others (meet, fish, milk, oils, fruits, vegetables, etc.). The following graph demonstrates the significant effect of sub item of rice on its contribution to the food inflation, especially from

Chart 5. TL - Total Food Inflation
Variation vs Contributions



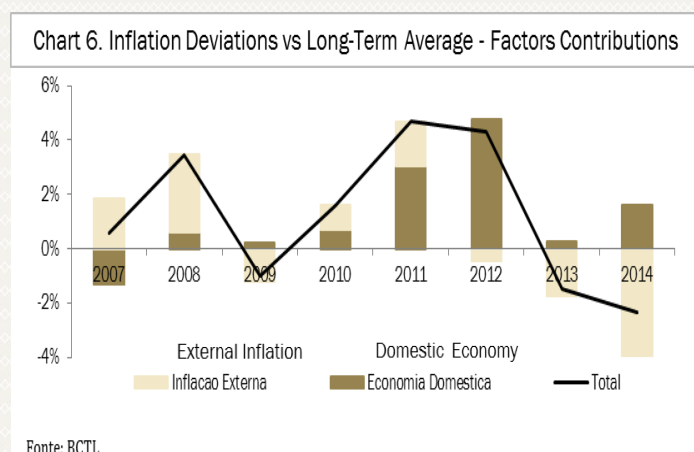
Source: National Directorate of Statistics and Staff BCTL analysis

April 2012 to August 2013, contributed almost half compare to others items of food. In average, rice contributed about 0.4% to the slowing down of food inflation during 2014 to date, while others items of food represent 0.1%.

Can be seen also the patterns of both graph (4 and 5) are the same. Demonstrated how the evolution of food price influence the headline inflation.

According to BCTL's empirical model, inflation slowdown in 2014 was mostly due to a substantial decrease of external inflation in 2014 (-1%), well below the average of the last decade, explained by the depreciation of regional currencies versus the dollar and decrease of commodities' international prices in 2014. The depreciation of partners' currencies resulted in lower prices for goods and services imported into our country. This effect was also reinforced by the impact of the domestic economy slowdown in 2013 and 2014, mostly evident in 2013

The chart below compares the impacts of both factors in terms of the 2 drivers of domestic inflation, which presents the deviations of inflation versus its long-term average, explained by the 2 factors.



As can be seen, inflation slowdown in 2013 and 2014 is mostly due to the decrease in external inflation in the 2 years. As also can be seen, domestic economy does not influence inflation trends in 2013, but, in 2014, the substantial economic growth recovery comes back to exert upward pressures on prices. Note that this pattern inverts the trend registered in 2011 and 2012, when the high expansion level of domestic demand explained the larger part of high inflation pressures in our economy.

II. Timor-Leste's Financial Sector

Timor-Leste's financial system continue growing in recent years, still there is an enormous potential for growth. The system remains relatively small in relation to the economy, when compared with ASEAN and even in some Pacific Island countries. This implies that many financing needs cannot be met and that much of the country's economic potential remains unfulfilled. However recently the central Bank has launched its Financial Sector Master Plan which sets out a comprehensive roadmap for the development of the financial sector over the decade to 2025.

II. a. Commercial Banks

The asset base of the banking system and its key elements posted strong growth; particularly the deposit base, while lending to private sector consistently stood with slight growth in a long period of time, declined over the first quarters of 2015 compare with correspondent quarter of 2014. In fact, there is still no assets of the banking system is shifted towards the investment as banks continued to not invest in government papers and bonds, further there is no papers or bonds are issued by the government of Timor-Leste.

Most of deposit of the banking system is deposited abroad, push the country foreign assets to increase. While, an small percentage amount of assets is recently started investing in foreign government securities

As of March 2015, the total number of banks stood at 4, which comprises by 3 branches of foreign banks and 1 local bank (the BNCTL). Hence there is an increase of Subsidiary of the branches of foreign banks and BNCTL's branches. The total subsidiary at the

	2010	2011	2012	2013	Dec-14	Mar-15
Total Assets	340.5	403.3	555.2	665.3	805.1	788.7
Liquid Assets	280.3	325.5	451.4	534.8	667.0	638.4
Investments	0.0	0.0	0.0	0.0	4.0	4.0
Total Loans	110.9	131.4	155.8	176.9	176.7	186.6
Non-performing loans	46.3	47.7	48.0	49.5	47.4	46.7
Provision for Loan Losses	59.5	63.5	62.4	58.4	55.8	54.0
Deposits	302.9	322.1	414.6	507.1	583.3	592.9
Capital	-6.1	-1.0	10.4	20.1	39.1	40.2

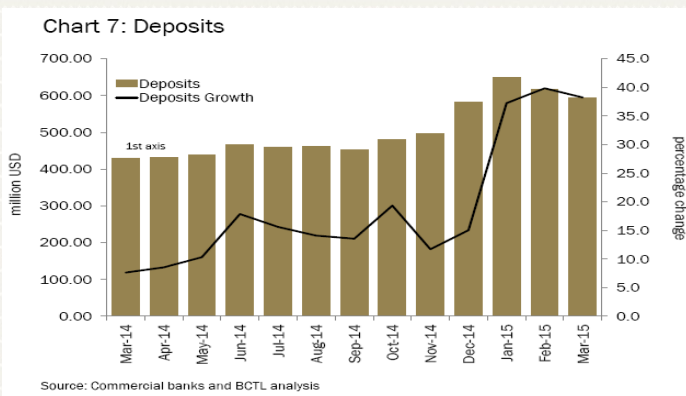
Source: Commercial Banks balance sheets and BCTL analysis

end of March 2015 are 18 while branches of BNCTL are 15, with the total of 33, an increase of 6.5% compared to 2014.

Total assets of all banks showed a net expansion of USD 187.6 million during one year from March 2014 and stood at USD 788.8 million. Hence the asset base of the banking system increased by 31.2% over the year to March 2015, while declined by 2% over the last December quarter.

The trend of total deposits of the banking system continue increases, reached 38.3% growth at March quarter of 2015 to stood at USD 592.9 million, after record a 15% growth in last December 2014.

The annual income as percentage of assets (RoA, or Return on Assets) was 0.5% in March 2015, the same as in March 2014, while lower than December 2014 of 1.12%. This decrease in ROA for March, compared to December 2014, was essentially due to the deep decline in banks' income, without an equivalent reduction in assets. The assets of the banking system reduced by 2% while the income dropped about 53%. In the other side, the banks continue to have liquidity ratios above the minimum required by the BCTL, with an excess of liquidity ratios of 70.3% in the quarter of March 2015.



II. b. Microfinance Institutions

Microfinance is an important market-oriented strategy of the financial sector to broaden the financial access and support the objective of economic and social development. Timor-Leste is amongst the few countries globally that have national strategy which identifies drivers and challenges to achieve both targets along with an implementation plan drawn along side with industry stakeholders to monitor progress against the national strategy plan.

As a result of endeavours of the past few years, micro-

finance in Timor-Leste has come a long way from a nascent stage to a small industry, which is now well-poised to grow. While the total number of the MFIs in the country just 2, but there is 25 numbers of branches with the continue growth in its indicators.

Indicators	Number of MFIs	Numbr of branches	Gross loan portfolio	Deposits
2011	2	11	1,801	2,721
2012	2	24	2,769	2,949
2013	2	24	3,691	3,567
2014	2	25	5,484	4,514
Mar-15	2		6,529	4,666

Source: MFIs and BCTL analysis

The industry witnessed an overall positive trend, albeit mild, in respect to the growth in its major indicators, with the continued growth in the deposits indicator that grew, in average for four years, by 18% on YoY basis. On quarterly basis, it grew by 1.7% in March 2015. It is encouraging that the MFIs have made progress during these years. A mix of vibrant and mature MFIs primarily contributed to the overall deposit growth of the sector. Gross Loan Portfolio (GLP) recorded a significant growth during the year to December 2014, rising in average by 12.6%, while for March quarter of 2015 rose by 5.6%.

III. Interest Rate

Banks earn returns to shareholders by accepting and managing risk, including the risk that borrowers may default or that changes in interest rates may narrow the interest spread between depositors and borrowers. Historically, borrower defaults have created the greatest losses to commercial banks, therefore interest margins have remained relatively high in Timor-Leste. The weighted interest rate of loan remained stood, in average, at 13.2% in almost 10 years, while the deposit rate about 1%, resulting the margin of 12.2% in average. The reduction of default and the establishment of land and properties laws are expected become one of the solution. Although credit risk is likely to remain the dominant risk to banks, we expected technological advances and the emergence of new financial products have provided them with dramatically more efficient ways of increasing or decreasing interest rate.

Table 4:
Timor-Leste Monetary Survey
Millions of US Dollars

	Dec-13	Mar-14	Dec-14	Mar-15	Percentage change	
					1 Q ago	1 Y ago
NET FOREIGN ASSETS	1071.85	868.73	756.78	741.06	-2.08	-14.70
CLAIMS ON NONRESIDENTS	1148.43	948.60	832.40	820.85	-1.39	-13.47
LIABILITIES TO NONRESIDENTS	-76.58	-79.87	-75.62	-79.80	5.52	-0.09
DOMESTIC CLAIMS	-469.02	-335.02	-15.40	-116.27	654.80	-65.30
NET CLAIMS ON CENTRAL GOVERNMENT	-650.79	-523.94	-207.17	-318.45	53.72	-39.22
CLAIMS ON CENTRAL GOVERNMENT	0.00	0.04	0.00	0.00	0.00	-96.63
LIABILITIES TO CENTRAL GOVERNMENT	-650.79	-523.98	-207.17	-318.45	53.72	-39.23
CLAIMS ON OTHER SECTORS	181.77	188.92	191.76	202.18	5.43	7.02
CLAIMS ON PRIVATE SECTOR	181.77	188.92	191.76	202.18	5.43	7.02
BROAD MONEY LIABILITIES	500.15	432.60	599.82	485.09	-19.13	12.13
CURRENCY OUTSIDE DEPOSITORY CORPORATION	6.76	7.63	9.78	10.13	3.63	32.87
TRANSFERABLE DEPOSITS	272.71	230.14	333.16	261.05	-21.64	13.43
OTHER DEPOSITS	220.69	194.83	256.88	213.91	-16.73	9.79
SECURITIES OTHER THAN SHARES	0.00	0.00	0.00	0.00		
DEPOSITS EXCLUDED FROM BROAD MONEY	0.19	0.20	0.36	0.38	5.75	90.63
LOANS	0.08	0.08	0.50	0.19	-62.50	150.00
SHARES AND OTHER EQUITY	45.07	48.37	89.41	90.16	0.84	86.41
OTHER ITEMS (NET)	57.34	52.47	51.28	48.97	-4.51	-6.67

Source: BCTL

Memorandum item: Petroleum Fund Assets 14,985.98 15,670.70 16,538.62

PRO FORMA BALANCE SHEET As at 31 March 2015


DESCRIPTION	\$'000
ASSETS	
Cash and cash equivalents	296,386
Marketable Securities	-
Investments	26,602
Property, plant and equipment	1,369
Other assets	5,599
TOTAL ASSETS	329,956
LIABILITIES	
Government deposits	195,640
Provision transfer of surplus to Government	-
Other deposits	73,908
Other liabilities	5,241
Currency issued	10,207
Total liabilities	284,996
EQUITY	
Capital	40,000
Reserves	4,525
Retained earnings	435
TOTAL EQUITY	44,960
TOTAL LIABILITIES & EQUITY	329,956

Nota:

1. At 31 March 2015 the balance of Petroleum Fund account managed by the BCTL was \$16.827 million. This is to recognise the reporting requirement under IFRS.

2. The Summary statements above are presented in accordance with article 58.6 of BCTL Law 2011/5 and have been prepared on an accrual basis from the financial records of BCTL as at 31 March 2015. These Financial Statements are unaudited.

Dili, 17 April 2015


Sara Lobo Brites
Acting Governor


Fernando da Silva Carvalho
Chief Accountant