Chapter 01

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This chapter evaluates the major global economic developments in 2023 as well as the economies of Timor-Leste's main trading partners, together with the more relevant international trends in global financial and commodity markets for our economy.

After these evaluations, the chapter further looks into the spillovers of main transmission channels of external development to domestic economy, detailing the influences observed in 2023 and the prospects expected for 2024 and 2025. This analysis is based mainly on the most recent IMF's estimates and perspectives, presented in its update version of "World Economic Outlook" released in January 2024 and October 2023.

In terms of the most relevant developments described in this chapter, we highlight the following:

> Development of global economies remains slow in 2023 after the remarkable recovery in 2021 from the global pandemic covid-19. The world economy's GDP grew 3.1% in 2023, after the huge deceleration in 2022, but remains below the 20 years historical (2000-2019) average growth of 3.8% across broader income group.

> The estimation of the IMF shows that the GDP growth in developed countries has already below pre-pandemic levels in 2023 as tightening policy starting takes effect in addition to the impact of the on-going war in Ukraine and the increase of tension in the red sea, but the GDP growth in developing countries in 2023 remain above 2019's pre-pandemic level by 0.5 percentage point.

> In terms of projections for 2024 and 2025, the IMF expects a stable growth of the world economy as well as the economies of some countries and regions in 2024 before they increase again in 2025. The IMF specifically forecasts that the world economy will grow 3.1% in 2024 and 3.2% in 2025. This projection is made among other things based on the perpetuation of the increasing geoeconomic fragmentation, policy adjustments, household consumption booming and normalized supply chains which bring down the logistical cost and delivery time back to pre-pandemic level underpin the IMF perspectives.

> Even so, the Fund has also warned that the world's economy continues to face downside risks, having highlighted the crisis in China property sector, volatile commodity price and a sharp repricing risk in emerging markets which could further appreciate the US dollar, trigger capital outflow and increase the cost of borrowing.

> Inflationary pressures remained a remarkable high although has slowdown in 2023, especially evident in the US, Eurozone, Japan and ASEAN economies, to record levels in recent decades. In these four blocs, annual inflation reached values well above 3%, which tends to be the benchmark for most central banks, with average inflation in the US and Eurozone standing at 4.1% and 5.6% in 2023.

> However, the IMF foresees a gradual convergence of average inflation rates in 2024 and 2025 towards 3% and 2%, admitting that the current inflationary episode will tend to be "temporary". This scenario is based on the understanding that the current inflationary pressures result, above all, from the still persistent productive and logistical constraints, and that the economic policy authorities worldwide will be able to reverse the respective stimulus programs in 2024 and 2025, moderating and adapting the expansion of aggregate demand to the productive capacity of the various economies.

> Asian economies once again performed above world average in 2023, which was due to the China reopening from the pandemic and the recovery of production processes and economic

activity which resulted from robust domestic demand in the region. In line with its global optimism, the IMF expects the continued substantial and widespread recovery of economic activity in the region in 2024 before a modest slowdown in 2025 due to slowdown in China, and predicting that the bloc will continue to lead the world in terms of economic growth.

> In the monetary and bond markets, 2023 was marked by a general fall in 2-year interest rates in the US and Europe, in line with the deceleration of inflationary pressures and the current development of the economic recovery, especially in the US.

> In the foreign exchange markets, the dollar ended up registering a modest appreciation against the main international currencies especially yen and yuan in 2023, driven by the upward trend in the dollar interest differential. In the Asian context, there was a general appreciation of the US dollar against Asian currencies, within a background of regional exchange market stability.

> Global equity markets ended up accumulating substantial gains in 2023, benefiting from the current development of the economic recovery, supported by the success of macroeconomic stabilization policies and the substantial reduction in investor pessimism.

> Global commodity market ended up with accumulating modest losses in 2023, in line with slowdown of world economic progress, resulting from sluggish economic activities, high bank interest rates and long-term geoeconomic fragmentation due to the geopolitical tension in addition to strong oil output growth in the US and ample supply of natural gas in Norway and Northern Africa.

> The performance of the petroleum fund's investments seems to benefit from the rise in world share prices and the fall of 2-year interest rates in 2023, but was penalized by fall in the prices of oil and gas in the global markets, minimizing its revenue from oil and gas sectors.

1.1

Major World Economies

1.1.1. Economic Growth in Major World Economies

Despite facing many persistent challenges, the world economic growth remains in the positive shape, it grew 3.1% in 2023. Consequently, the global level of gross domestic product (GDP) remains above the pre-pandemic growth of 2.8% recorded in 2019, prolonging the record in 2021 and 2022.

The world economy remains in the positive shape despite facing many persistent challenges in 2023.

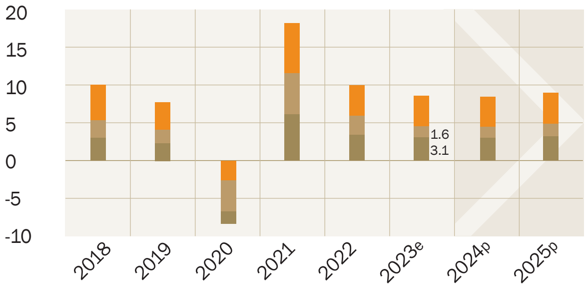
Although positive, the global economic development in 2023 remain slow and in decelerating path after a strong recovery in 2021, following the global pandemic and its respective economic and social impacts in 2020. The estimate growth remains below the 20 years (2000-2019) historical average growth of 3.8% across broader income group.

However, the global economies remain slow and in deccelerating path after strong recovery in 2021

According to IMF, this slowdown was the result of globally synchronous central bank contraction monetary policy to tackle the high inflationary pressures, withdrawal of fiscal support amid high debt, extreme weather events and idiosyncratic development such as property crisis in China which categorised as cyclical in nature. It is also the result of long-term consequence of global pandemic Covid-19 and increasing geoeconomic fragmentation due to geopolitics tension including the tension in the red sea.

Chart 1.1

GDP growth – 3 major blocks

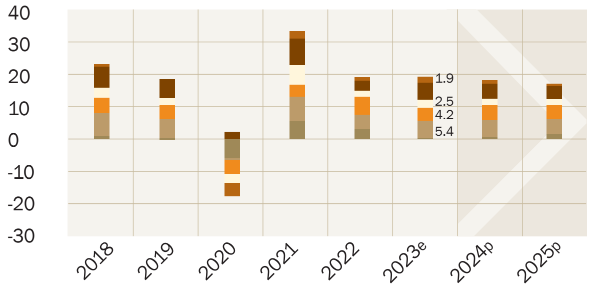


% variação ano
- World
- Developed Economies
- Emerging Economies

Source: IMF WEO

Chart 1.2

GDP growth – selected regions and countries



% annual change
- E.U
- Emerging Asia
- ASEAN-5
- US
- China
- Japan

Source: IMF WEO

The growth of world advanced economies was slower than the world average

The IMF estimation shows that the economies in developed countries in aggregate grew 1.6% in 2023, while emerging economies grew 4.1%. By comparison, the growth in advanced economies was slower than the world average, decelerated by 1.0 percent point from 2.6% in 2022 while in emerging market and developing economies, the growth was remained same as recorded in 2022, but remains higher compared to the world average and to the advanced economies.

It should be noted that the deceleration was stronger in advanced economies due to weaker economic performance in Euro area amid the stronger growth than expected in the US economies, confirming the impact of the tightening policy as well as the impact of on-going war in Ukraine, as evident with weak consumer sentiment, lingering effect of high energy prices and weak interest-rate sensitive manufacturing and investment in the Euro area. Constant growth in emerging market and developing economies reflect the property crisis in China amid the improvement in consumption and services as well as improvement in some emerging and developing countries. High interest rates and currencies depreciation in some low-income economies further contributed to this constant growth, contributing to overall output loss of >6.5% in other emerging market and developing economies.

At the regional level, noticeable economic performance of the Asia-Pacific economies was observed, relative to global peers. The GDP of Emerging Asia and the five ASEAN largest economies grew 5.4% and 4.2% in 2023, remain at the 2019's growth level although the growth of the five largest ASEAN economies slightly lower by 0.1 percentage point than the growth in 2019.

Noticeable economic performance of the Asia-Pacific was observed in 2023 relative to their global peers.

With regard to the developed world especially the US and the eurozone, as already mentioned that the US economy has performed more robustly than the economies in the Eurozone, growing 2.5% in 2023, while the economy of the eurozone is still 0.5%, where all still below the 2019's growth level, reverse the growth level in 2021 and 2022, especially the Eurozone which already above the growth in 2019.

Charts 1.2 presents the comparative economic performance of the four largest world economies, which help us to confirm the above-average performance. Among the four largest economies, the economies of China outperform the economies of the US, Eurozone and Japan. In 2022, the growths were almost same between the Eurozone (3.3%) and China (3.0%) with Japan had the lowest growth (%1%), but in 2023, Eurozone had the lowest growth among the world four largest economies.

Unlike the Euro area, the economies of the US, China and Japan were accelerating in 2023, accelerated by 0.4 percent point, 2.0 percentage points and 0.9 percentage point from their respective growths in 2022. Strong external demand due to recovery in domestic demand, inbound tourism and automobile export due to the supply chain normalization contributed to Japan's economic acceleration while acceleration of China economies was contributed by growth in industry value added and rebound in consumption and services in addition to fiscal support mentioned previously. The expansionary in the US was supported by fiscal policy easing and boosting of domestic consumption.

It should also be noted that although the China's economy was expanding, it faced a slowdown compared to estimation made in the earlier, due to property crisis and labour market uncertainty. It was revised downward by 3.7 percent points from estimated growth of 8.9% made in the first quarter of 2023.

In terms of growth prospects, the IMF expects the economy continue to have broadly stable growth in 2024 with a peak up in 2025. The IMF specifically forecasts that the world economy will grow by 3.1% in 2024 and 3.2% in 2025, the values which are slightly higher by 0.4 percentage point and 0.5 percentage point compared to the average growth of 2.7% recorded during 2018-2022.

The IMF's global outlook for 2024 and 2025 remains optimistic and broadly stable.

The IMF furthermore expects that the economies will stable in emerging and developing economies and slightly slower in advanced economies in 2024, then will peak up in 2025. It has projected that the advanced economies expect to grow by a respective of 1.5% and 1.8% in 2024 and 2025 while emerging market and developing economies is expected to grow by 4.1% and 4.2% in 2024 and 2025, respectively.

Regionally, the IMF expects the economies of Euro area will accelerate in 2024 and 2025 while the economies of five ASEAN major economies, the emerging and developing Asia and the US will slow in 2024 and 2025 as their growth rates lower than their estimated growth for 2023. Specifically, the economies in Eurozone expects to grow by 0.9% and 1.7% in 2024 and 2025 while the five ASEAN major economies expect to grow by 4.7% and 4.4% in 2024 and 2025, the economies of emerging and developing Asia will grow by 5.2% and 4.8% and the economies of the US will grow by 2.1% and 1.7% in 2024 and 2025, respectively.

Contrary to 2023, the economies of China and Japan expected to decelerate in the next two years as their growth rates lower than their growth rates in 2023 and 2024, follow the path of their peer in the US. As shown in Chart 1.3.1 that the economies of China expect to grow by 4.6% and 4.1% in 2024 and 2025 while the economies of Japan expect to grow by 0.9% and 0.8% in 2024 and 2025. In 2023 the economies of China and Japan were estimated 5.2% and 1.9%, respectively.

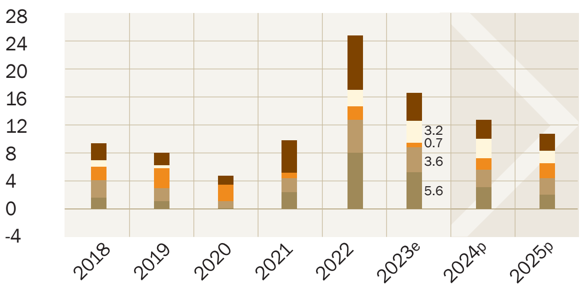
Several factors were contributing to these projections in overall. In advanced economies, they are the lagged effect of monetary tightening, gradual fiscal easing, a softening in labour market slowing aggregate demand in the US, stronger household consumption and inflation deceleration especially in the Euro area. In emerging and developing economies including most of the ASEAN five major economies, contributing factors for the growth in 2024 and 2025 was attributed to the property crisis in China.

It is also important to notice that an upward revision was observed compared to estimation made in October 2023, due to greater resilience in the US economies as well as in some large emerging market and developing economies than was expected. However, there are also upside and downside effects of these estimations. On the upside effect, faster disinflation could lead to further easing financial condition by easing the monetary policy which can push the growth further and revise at a later date with great cost. On the downside effect, geopolitical tension, supply disruption and still high inflation pressure could prolong tight monetary policy, resulting in disappointing growth projection.

1.1.2. Inflation in Major World Economies

The following graphs show the evolution of annual average inflation rates and price levels in five of the main world economies.

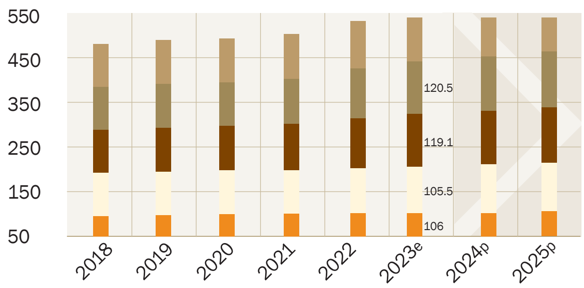
Chart 1.3.1
Inflation rates – 5 selected economies



% annual change
- E.U
- ASEAN-5
- China
- Japan
- U.S

Source: IMF WEO

Chart 1.3.2
Price level inflation – five selected economies



2019 = 100
- China
- Japan
- US
- E.U
- ASEAN-5

Source: IMF WEO

As shown in chart 1.3.1 that inflationary pressure registered a notable decline in 2023, especially in China, the US, Eurozone and in the five ASEAN largest economies after multidecade high observed in 2022, due to the tighten monetary policy, decline in commodity prices and largely normalization of supply chain which bring down the logistic cost and delivery time. Moreover, easing in labour market tightness with a decline in job vacancies and greater labour supply in part due to the strong inflow of migration also contributed to this inflation pressure declination. However, with exception of China, the annual average inflation still remains high, reached values well above 3%, which tend to be the benchmark for most central banks to not reverse the current monetary policy sharply and quickly, with average inflation in the US and Eurozone standing at 4.1% and 5.6% in 2023.

Global inflationary pressures fall in 2023 due to the contraction monetary policy, fall in commodity prices and due to the largely normalized supply chains.

These still high average rates obscure the sustained and worrying growth of inflationary pressures observed throughout 2023, with the year-on-year inflation rate in December 2023 being already on average above 2%. This value, which has not been observed during 2015-2021, reveals the scale and dimension of the current inflationary episode. However, it should be noted that inflation levels in the Chinese economies have been kept relatively low during 2021-2023 compared to its global peers, with its 2023's average inflation being 0.7%.

As already reported in 2021 annual report that the robustness of the global economic recovery and the high stimulating degree of the implemented monetary and fiscal stimulus policies in the major developed economies contributed to the worsening of global inflationary pressures observed in 2021. Moreover, aggravate inflationary risks in most economies also resulted from the persistence of social and economic restrictions, together with the worsening of constraints and failures in global logistics and production chains alongside the significant recovery in global demand.

It should also be noted that inflation in emerging market and developing economies was higher than those in advanced economies. This was due to as indicated in the IMF report that advanced economies take advantage from their improved monetary policy framework and communication strategy which facilitate disinflation, where inflation in advanced economies was influenced by forward looking inflation considering their monetary policy, unlike backward looking which very significant in emerging market and developing economies, indicating that current inflationary pressure influenced significantly by previous inflation in emerging markets and developing economies. The difference also occurred due to lower exposure to shock to commodity price and exchange rate and also because of unstable fiscal position such as high public debt and persistent deficit.

The IMF anticipates that inflationary pressures will gradually decline in 2024 and 2025.

In terms of perspectives, the IMF foresees a gradual convergence of average inflation rates in 2024 and 2025 towards 2% in practically all world economies, which constitutes the policy reference of many central banks. This means the Fund admits that the current inflationary episode will tend to be temporary, with annual inflation in the US and in the Eurozone expected to slow down to 3.3% and 2.8% in 2024 and to 2.2% and 2.4% in 2025 as more money would be demanded.

China's inflation will slightly be accelerating in 2024 and 2025, contrary to the US, Japan, Eurozone and ASEAN5

Similarly, inflationary projection of the five ASEAN largest economies and Japan are expected to slow down from 2.5% and 2.9% in 2024 to 2.4% and 1.9% in 2025, respectively, contrary to inflationary projections in the Chinese economy which admit a slight acceleration in annual inflation to 1.7% in 2024 and 2.2% in 2025. This is also supported with inflation of China at the end of 2023 (0.9%) which was higher than annual average of 0.7%, indicating that China's inflationary pressure was accelerating in 2023, confirming its slow growth projected for 2024 and 2025. Unlike the US, China has eased its interest rate in July and August 2023, this could be another reason for China's inflation accelerating in 2024 and 2025.

The scenario is made based on the current inflationary pressures result, above all, from the productive, logistical constraints and geopolitical tension that are still evident, and that the economic policy authorities worldwide will be able to successfully monitor the respective stimulus programs in 2024 and 2025, moderating and adjusting the expansion of aggregate demand to the productive capacity of the various economies.

The IMF expects that the economies of the five major economies will continue to register the same inflation rates in the next biennium, which should continue to register average inflation rates below the mentioned 3% and requires two to three years to reach a target of 2%.

1.1.3. Global Commodity Markets

Unlike 2022, the year 2023 was marked by the general decline in market prices of the main traded commodities.

Commodity prices recorded broad-based loss in 2023.

This price declination occurred naturally in the global context of a substantial pickup in inflationary pressures as mentioned in the previous section, causing low demand. The overall downward trend in non-energy, in line with what had already happened in 2022, especially February onwards, hence, resulted in the contraction of the prices observed since the prices of most of these items recorded their highest values in 2022, following their lowest value being observed in 2015/2016. For countries exporting these commodities, especially developing countries, the decline of international prices represents a negative development, conversely, the rise of the prices of these commodities in international markets represents a positive development.

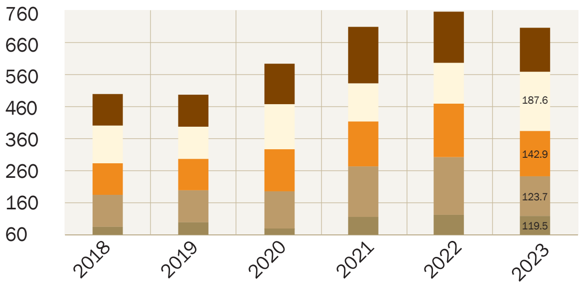
The oil price showed a slightly loss in 2023, a decrease of -3%, due to low demand, in line with modest recovery in world economic activity due to weaker rebound of oil consumption in China, interest rate hikes and growing uncertainty regarding the geoeconomic fragmentation despite the supply side pressure due to OPEC+ countries (the organization of the petroleum exporting counties plus selected non-member countries) cutting 1.3 million barrels of oil per day in addition to a total voluntary cut of 1.3 million barrels of oil per day by Saudi Arabia and Rusia, after being one of the few commodities that recorded a price rise of 7% in 2022.

The loss in oil prices was due to the weaker rebound of oil consumption in China, high interest rate and the strong oil output growth in the US despite the supply side pressures and geopolitical tension.

It should also be noted that this oil price declination was also associated with strong oil output growth in non-OPEC member countries, especially in the U.S. With this development, oil price in overall has already declined to its lowest level since June 2022, evident with annual average price declination of around 17% in 2023 from an average price of $97.10 per barrel in 2022.

Chart 1.4.1

Major commodity prices – level



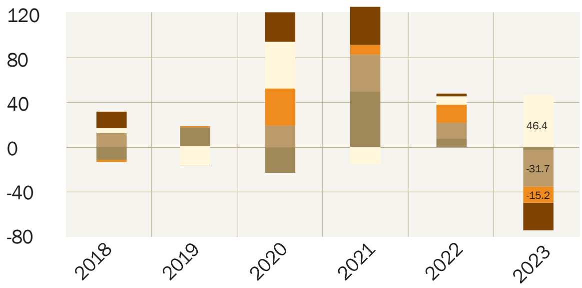
2019 = 100

- Oil
- Corn
- Soybean
- Rice Viet.
- Wheat

Source: World Bank

Chart 1.4.2

Major commodity prices



% annual change

- Oil
- Corn
- Soybean
- Rice Viet.
- Wheat

Source: World Bank

The recovery in oil prices over the last few years and price declination in 2023, clearly highlighted the structural difficulties in the transition of the world's energy model. The recent reinforcement of the measures adopted towards the development of renewable energy sources and the reduction of CO_2 emission levels coupled with oil production cut in OPEC+ countries in addition to increase geoeconomic fragmentation limited the production and supply of fossil fuels worldwide.

This greater rigidity of supply and the inability to accommodate a global demand that has proved to be relatively stable, means that the world energy markets are increasingly impacted by greater price volatility and an increasing cost of supplying oil, gas, coal and liquid fuels. This trend is expected to be persistent in the medium term, while the necessary technology is developed and the necessary investments are made to underpin the effective energy transition and decarbonization of the world economy.

1.1.4. Major Global Financial Markets

In terms of financial markets, we start the analysis with trends across major bond markets, especially those for treasury bonds, which helps us to assess trends and changes, as well as expectations, of monetary policies, economic growth and inflationary pressures of the various world economies.

Two-year interest rates decline in the US, in line with declining inflationary pressures and strong economic performance.

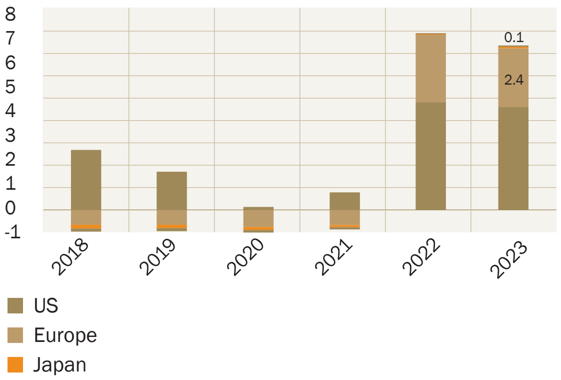
There was a decrease in two-year rates in 2023, especially in the US and the Germany markets, as a result of decelerating inflationary pressures and the expectations of a slight reversal of the monetary policy cycle in the major economies. This trend counteracted the widespread and broad rise in interest rates recorded in 2022, following the implementation of highly stimulating monetary programs to stabilize the world's economies.

Generally, two-year interest rates, short-run interest rates, which are more sensitive to changes in monetary policy, slightly decline in 2023 after a remarkable increased in 2022, especially in the US and Germany. In economies where the level of short-term interest rates was below the zero threshold (0%), this fall was minor to the respective central banks which prefer to maintain their accommodative position for longer.

Two-year interest rates are more sensitive to changes in monetary policy than 10-year rate.

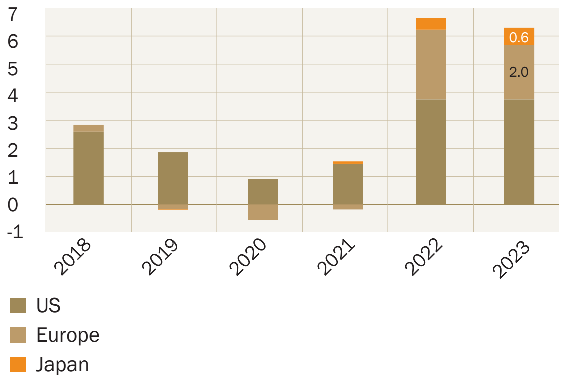
In the case of the US, the fall in two-year interest rates was substantial, having decreased from 4.43% at the end of 2022 to 4.25% at the end of 2023. Despite this fall, two-year interest rates in the US well above their pre-pandemic levels, which was 1.57% at the end of 2019. This development, clearly shows that the monetary stimulus program of the Federal Reserve System (the Fed), including its key rates, is still at dissimulating levels for the US economy although its economic performance was better than those in the Eurozone.

Chart 1.5
2-years interest rates (%)



Source: Bloomberg

Chart 1.6
10-years interest rates (%)



Source: Bloomberg

Given the deceleration level of inflationary pressures in the US at the end of 2023, the Fed needs to implement a continue and notable recovery in monetary stimulus throughout 2024, in order to maintain the current economic recovery growth without compromising to stabilize the inflationary expectations.

However, it should be noted that the Fed had already stated that it goes to adopt “higher-for-long” approaches which means that policy to bring the interest rates down sharply may not happen soon. This is evident with the Fed increased its policy rate along the central bank of European Union, Bank of England and Bank of Canada in July 2023.

Unlike two-year interest rates, 10-year interest rates in the US slightly increased in 2023.

In the case of 10-year interest rates, with the exception of Germany, there was a slight increase in 2023 compared to 2022, thus maintaining the rise recorded in the previous years. Like the two-year rates, the 10-year interest rates in the US market, valued at 3.88% at the end of 2023, well above the pre-pandemic levels, as this interest rate was 2.68% and 1.92% at the end of 2018 and 2019, respectively.

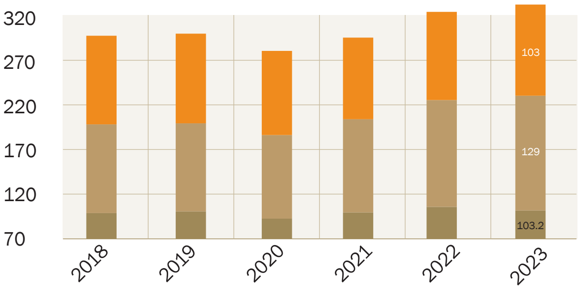
It should also be noted that the reference for German 10-year bonds was also positive in 2022 and 2023, reversing the negative rates during December 2014-December 2021, meaning the interest rate was increased substantially in 2022 and 2023. The 10-year interest rate in Germany was already 2.02% at the end of 2023, greatly above its pre-pandemic level of -0.19% in 2019.

In both two and 10 years, interest rates in the US remained at levels well above those observed for the Eurozone and Japan, similarly to what has happened since 2013, which seems to result from the perpetuation of the viewpoint that the US economy should continue to register a relatively better performance over the next few years.

As is common, bond markets developments, together with the economic developments that had been analysed, also determined a large part of the changes registered in the main foreign exchange and equity markets worldwide.

O mercado acionista norte-americano – representado pelo Dow Jones – registou ganhos de 13,5% em 2023, depois de ter registado uma queda de 9,0% em 2022. Estes rendimentos têm sido suportados pelo otimismo relativamente aos sectores dos serviços e da indústria, que representa uma parcela crescente e mais significativa deste mercado, quando comparado com outros mercados acionistas mundiais.

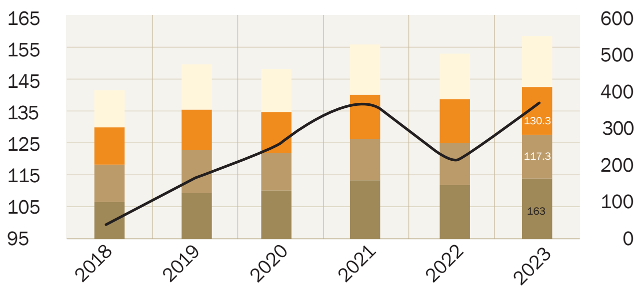
Chart 1.7
Major currencies against USD



2018=100
Euro
Yen
Chinese Yuan

Source: Bloomberg

Chart 1.8
Stock markets



US
E.U
Asia
Australia
Average

Source: Bloomberg

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In the foreign exchange markets, the dollar appreciated against the yuan and the yen, but lost value against the Euro, contrary to the generalized appreciation seen in 2022, indicating that demand for the US dollar in Japan and China were higher than in the Euro area. These changes resulted from the growing global inflationary pressures seen in 2021 and 2022. This fact, evidenced by the rise in US interest rates compared to other blocs, tended to reinforce the demand for dollars in the foreign exchange markets, which offer higher rates of return than most debts from other developed countries.

The high interest rates in the US market contributed to the appreciation of the dollar against the major world currencies.

In equity markets, all of the selected markets continue to record a strong performance in 2023, and that, reversing the values loose seen in 2022. As shown in chart 1.8 that the average equity markets accumulated gains in 2023, with the US and Asian markets outperformed their European and Australian peers.

The major world equity markets recorded notable gains in 2023, reversing the values loose recorded in 2022.

The US equity market - represented by Dow Jones - recorded gains of 13.5% in 2023, after experiencing a decline of 9.0% in 2022. These returns have been supported by the optimism regarding service and industry sectors, which represents a growing and more significant portion of this market, when compared to other world's equity markets.

In addition to the US, the overall equity market recorded gains of 14% in 2023, with the US and Asian markets – gaining almost same percentages, 13.5% vs 12.5%. The European markets, representing by the UK recorded gains below its global peers, having risen only 2.8% in the year.

In sum, the US and the Asian stock markets outperformed the other selected markets in 2023, having continued to benefit from the greater dynamism of its economy, despite the recent confusing and disturbing political episodes.

1.2

Asian Economic Developments

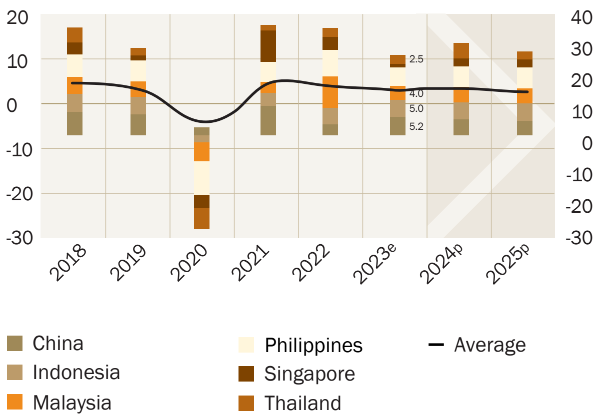
After analysing the wider global macroeconomic development in the previous section, it is vital to detail the assessment of economic developments across the Asian countries, especially ASEAN, as the main trading partners of Timor-Leste are located in this region.

The largest Asian economies experienced a remarkable deceleration in 2023, after a 5.1% growth recorded in 2022.

The analysis of this section specifically focuses on five ASEAN major economies and China, whose economy has increasingly taken a more global and regional relevance. From these six economies, Indonesia continues to be the Timor-Leste's main trading partner, which justifies some further specific comments and assessments on its economic developments.

Chart 1.9.a

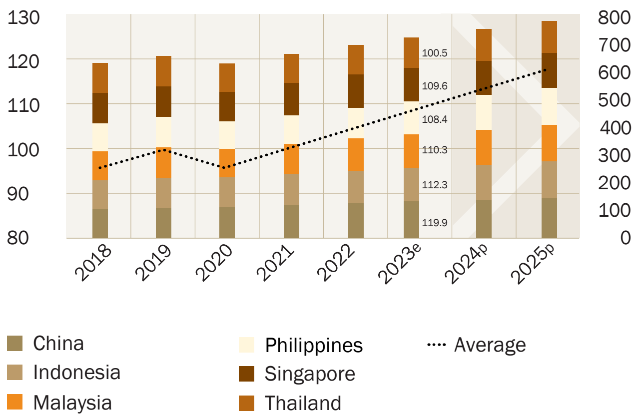
GDP growth rates - % annual change



Source: IMF WEO

Chart 1.9.b

Price level GDP – 2019 = 100



Source: IMF WEO

In terms of relevant developments for these economies, the GDP of the six countries registered a generalized deceleration, with average economic growth estimated at 3.8% in 2023, compared to an overall growth of 5.1% recorded in 2022, as a result of slowdown in Indonesia, Malaysia, Philippines and Singapore

The Asian economies hence record a moderate slowdown in 2023, when compared to the economies in the Euro area, which was due to the negative contribution of service sectors in high income countries in the region and also due to the property sector crisis in China.

The deceleration in Asia has been a moderate than in the Euro area.

It also important to mention that, in 2023, all these selected Asian countries - had an annual GDP level that was greater by >9% than that of 2019 (pre-pandemic), with special emphasis on Thailand, whose GDP in 2023 was only 0.5% above the 2019 level while China, its GDP level in 2023 was 20% above that of 2019.

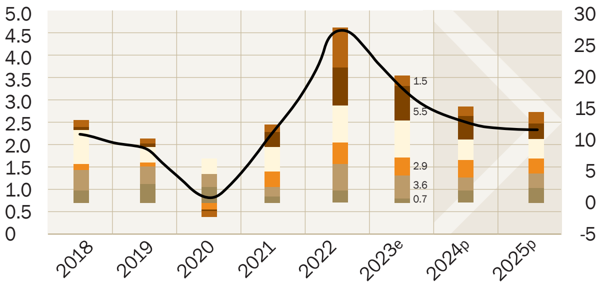
The economy in developing Asia and the pacific in overall was expanding as their growth in 2023 higher than in 2022 due to robust domestic demand, China reopening after the pandemic, rebounding of tourism and stable financial condition although the export sector is still weak due to global economic slowdown. From the supply side, growth in Asia was supported by agriculture, industry and service sectors.

In terms of prospects, contrary to the global growth, the IMF expects the economic activity in the region to expand modestly in 2024 before slowing down in 2025, predicting that the region will continue to lead the world in terms of economic growth. In this regard, the IMF expects that all the six economies will continue to regain their 2019's GDP levels in the coming two years, predicting an average growth rate in the six economies of 4.4% in 2024 and 4.0% in 2025.

The prospects for economic growth in the region remain optimistic for 2024 and 2025.

Chart 1.10.a

Inflation rates - % annual change

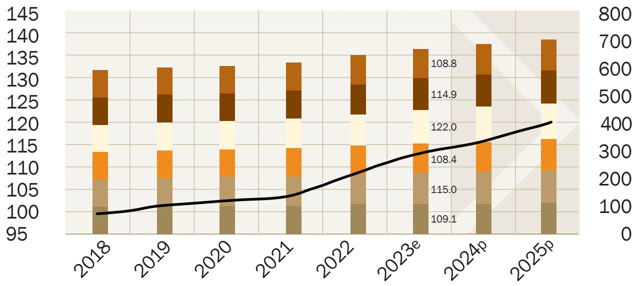


China
Indonesia
Malaysia
Philippines
Singapore
Thailand
Average

Source: IMF WEO

Chart 1.10.b

Price level inflation – 2018 = 100



China
Indonesia
Malaysia
Philippines
Singapore
Thailand
Average

Source: IMF WEO

The same forecasts also indicates that, at the end of 2025, it is expected that China, Indonesia's, Malaysia's and the Philippines' GDP to be 30%, 24%, 20% and 22% above the value of the 2019, which are the economies with the highest growth rates. On the contrary, Thailand is expected to be the lowest growth economies by 2025 in the region, as its output will only be about 7% above its 2019 level.

Inflation in the region dccelerated in 2023, in line with the global trend.

In line with the global trend, inflation in the region decelerated in 2023, contradicting the high inflationary pressured seen in 2022. The average inflation rate of the six Asian economies fall to 3.3% in 2023, compared to 4.6% in 2022 and 2.1% 2021. It is also important to note that only three economies – China, Malaysia and Thailand – recorded below the average inflation rates, valued at 0.7%, 2.9% and 1.5%, respectively while the rest, their inflation rate remain above the six economies average.

The IMF expects the materialization of a scenario of general inflation stability in the region for 2024 and 2025, with average annual inflation remaining below 2%, annually. Despite the geopolitical tension, oil supply pressured and logistical constraints due to the ongoing war, the Fund believes that Asian economies and their monetary authorities will be able to guarantee that price stability is continue to maintain during the next two years.

The rise in inflation rates in the various economies and the average appreciation of the dollar against the six Asian currencies, amounting to 0.4% in 2023, after an appreciation of 6.3% in 2022 explained, in turn, the decrease in regional inflationary pressures, when measured in the US dollar terms.

These relevant developments of the main macroeconomic indicators - economic activity and inflation - help to explain and as are also explained by the developments registered in the two main financial markets, the regional foreign exchange and bond markets.

Regional currencies on average deppreciated against the US dollar in 2023.

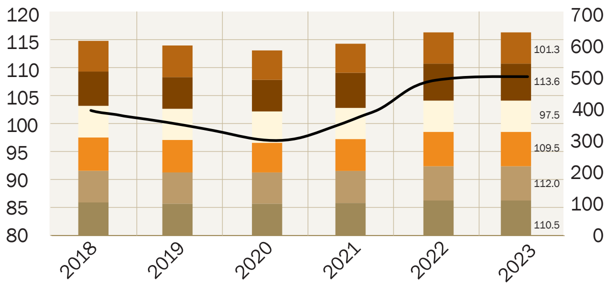
In exchange markets, despite the high volatility recorded throughout the year, 2023 ended up being marked by the 0.4% average depreciation of regional currencies against the dollar, with Indonesian, the Philippines, Singapore and Thailand currencies being the only currencies with annual appreciation rates of 1.5%, 0.2%, 1.8% and 0.9%, respectively. High interest rates in the US contributed to the appreciation of the US dollar against these overall Asian currencies.

In contrast with the US and Germany, 2-year interest rates in the region in overall increased in 2023, prolonging the rise recorded in 2022.

Bond market interest rates, represented here by two-year bonds, registered a general increase in the region in 2023, in contrast with the US and Germany, thus prolonging the rise recorded in 2022.

Chart 1.11

Exchange rate of ASEAN5 + CHY vs. USD



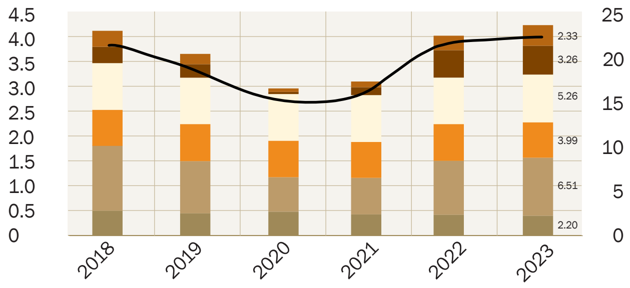
2019 = 100

Indonesia
Malaysia
Philippines
Singapore
Thailand
China
Average

Source: Bloomberg

Chart 1.12

Two-year interest rates



% year

China
Indonesia
Malaysia
Philippines
Singapore
Thailand
Average

Source: Bloomberg

The average two-year interest rate of the six economies rose from 3.73% in 2022 to 3.93% at the end of 2023, well above the level observed at end of 2019 (3.39%) and was the highest one since the level observed at the end of 2013 (4.03%). The rose in two-year interest rates in the various economies resulted from the rose in reference rates by some central banks and also from their economic performance and prospects. It should also be noted that the interest rates in the region are almost similar to the US, showing that the markets in the region followed the dollar market changes. Furthermore, the interest rates in the region are still above the rates observed in Japanese and Germany markets, reflects their better relative economic performance.

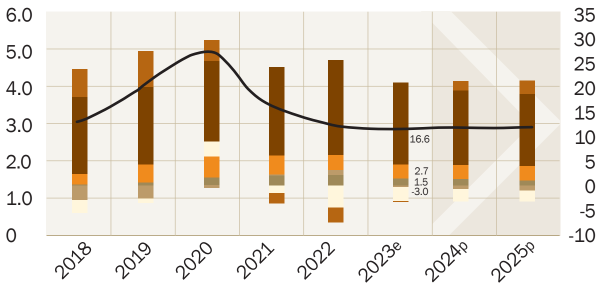
Regarding the current external account balances, it can be concluded that the partner countries continued to maintain substantial external surpluses in 2023, with the exception of Indonesia, the Philippines and Thailand, which recorded a respective current external account deficit of -0.3%, -3.0% and -0.2 % of their GDP in 2023. It should also be noted that, although there was a slight reduction in the region's average external surplus in 2023 compared to 2022, they managed to maintain positive current external account balances, despite the strong disruptions to economic activity and trade worldwide, indicating that they have surplus of saving for other countries.

The regional current external accounts remained in surplus in 2023, with the exception of Indonesia, Philippines and Thailand.

For 2024 and 2025, the IMF continues to predict stability in net external balances in the region, although it is important to note that the Philippines and Indonesian economies continue to record current external account deficits, with Indonesia specifically to continue experienced increased external account deficit in these two years. In contrast, Thailand is expected to have surplus of saving in the next two years, following the path of its peers in these economies.

Chart 1.13

Current external account balance



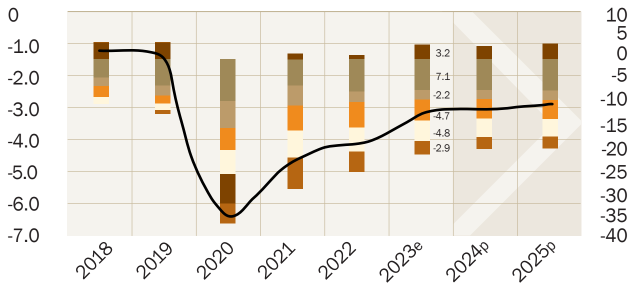
% PIB

China
Indonesia
Malaysia
Philippines
Singapore
Thailand
Average

Source: IMF WEO

Chart 1.14

Fiscal balance



% GDP

China
Indonesia
Malaysia
Philippines
Singapore
Thailand
Average

Source: IMF WEO

In 2023, fiscal balances continued improved in the region, partially offset the fiscal deterioration observed in 2022.

In terms of budgetary balances, 2023 was marked by a noticeable improvement of public deficits in the region, with the average deficit falling from -4.2% in 2022 to -3.1% of GDP in 2023. This improvement cancelled out some portions of the public deficits' deterioration of the various Asian economies in 2022. Consequently, at the end of 2023, public deficits were the lowest one since 2020 but still exceeded the respective average value of -1.1% and -1.5% of GDP, recorded in 2018 and 2019. It should also be noted that Thailand recorded the largest deficit reduction in 2023, which fell from - 4.6% in 2022 to -2.9% of GDP in 2023 with Singapore recorded a fiscal surplus of 3.2% of its GDP. It is also worthed to note that Singapore is only recorded a fiscal deficit in 2020 due to the pandemic covid-19 impact.

For 2024 and 2025, the IMF expects a gradual reduction in budget deficits in the region, anticipating an average deficit of -3.0% and -2.8% of GDP in 2024 and 2025, respectively. As a result, most economies should maintain a stimulative fiscal policy stance over the next two years, which will certainly help to explain the strength of economic growth in the next biennium. This also means that the focus of the governments in the region in overall is on improving domestic revenue and minimizing deficit without sacrificing their growth.

With the exception of Singapore, which continues to register a budget surplus, the remaining five economies should continue to record deficits around -2% to -7% of their GDP over the next few years. And with the exception of China, the fiscal policies of the partners in the region will continue to be more on fiscal balance improvement, with their respective public deficits as percentages of GDP decreasing in the next two years.

In short, in line with the global trends, the economic development of the main trading partners in the region were slower in 2023 as their growth rates was lower than in 2022 but remain above the 2020 level which made it possible to recover completely from the 2020's fall in economic activity.

It is also important to note that the relative stability of regional currencies against the dollar and the maintenance of external surpluses in most economies, although in tandem with the maintenance of moderate public deficits in the region, will continue to provide a substantial scope for macroeconomic adjustment and policy flexibility in these Asian economies.

However, this does not mean that this general background does fully apply to the Indonesian economy, the largest trading partner of Timor-Leste. In one hand, we highlight the vigorous recovery of its economy, which has already managed to recover since the 2021, maintaining its pre-pandemic GDP level of 2019, as well as its price and foreign exchange rate stability. On the other hand, the country continues to record a deficit in public accounts, -2.2% and an external deficit of -0.3% of GDP in 2023.

In terms of outlook, the IMF continues to expect the current performance for the Indonesian economy to be maintained over the next two years, with an average annual growth rate of 5.0%, as well as in maintaining a stable and moderate inflation rate of 2.5% per year. Although public and external deficits are expected to continue, the IMF forecasts clearly assure that the country will manage to the macroeconomic stability, visible above all in the appreciation of the rupiah, the decrease in inflationary pressures and the fall in external revenues, resulting from the flip in international prices of many commodities the country exported.

In line with the global trend, the economic development of the main trading partners in the region were slower in 2023 as their growth was lower than in 2022.

Naturally, the decrease in the price of raw materials after the pluriannual recovery, particularly visible in 2021 and 2022, is expected to underpin the recovery of economic activity and the earnings of exports in the country. In any case, the continued economic dependence on the export of these products implies that the macroeconomic and financial performance of our neighbouring country will continue to be strongly determined by the development of the commodity price in the global markets and the world economy.

The importance of this partner for our country and economy implies to continue monitor these developments, with the expectation that the continuity of the policy measures introduced by its government and the stricter vigilance by its central bank will continue to gradually reduce the respective macroeconomic risks.

1.3

Timor-Leste Economic Transmission Channels

The major international economic and financial developments described above together with Asian economic developments, which are relevant for Timor-Leste, would be incomplete without understanding the respective repercussions on our economy.

Therefore, this section tries to expose the main transmission channels of the international developments to our economy. At present, it is important to admit that these effects affect some certain sectorial aspects of the economy in the country. This chapter seeks to demonstrate the mechanism of operation of the main channels, specifically: the impact on domestic inflation levels, influence over oil revenues and effects on the petroleum fund's investments valuations. Foreign Direct Investment is certainly one of the variables most influenced by the external context, but the scarcity of effective investments and reliable data in Timor-Leste does not permit us to analyse this relationship properly. Hence, this section mostly developed based on data showed in Figure 1.5, 1.8, 1.10a and 1.11.

We expect that external developments will increasingly shape the domestic economic developments as our economy develops and effectively deepens interdependence relations with the regional economic partners, expanding the number and influence of the various transmission channels.

1.3.1. Imported Inflation

One of the main transmission channels for our economy is the impact of international prices on domestic inflation developments and its respective expectations. As Timor-Leste is an economy with great import activity - imports of goods and services on average accounted 52% of non-oil GDP in 2021 and 2022, therefore, it is very common and related to expect that international prices of imported goods and services will continue to significantly affect domestic inflation along with economic development in the country.

BCTL's inflation model is based on two key drivers - domestic economic performance and average inflation rates across the Asian region.

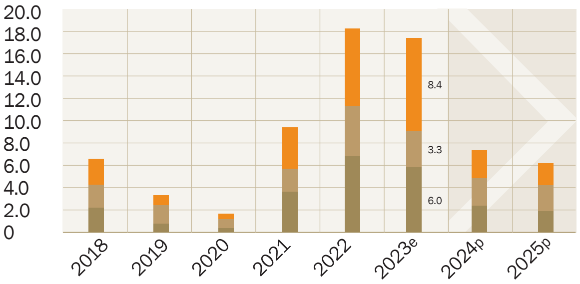
The empirical research and economic modelling of BCTL has confirmed the importance of this channel. One of the studies conducted in 2014 has indicated that a 10% increase of foreign inflation above its average level would result in a cumulative increase of 8.7%, 7.3% and 1.5% of total, food and non-food inflation in the country, respectively, clearly indicating that external inflation affects the domestic inflation. It further shows that economic development in the country influence domestic inflation by 10.7%, 8.2% and 8% of total, food and non-food inflation when domestic economic activities rise $100 million above the long-term average. However, one of the main issues in this context arise from the difficulty in defining an appropriate variable to measure the level of "external inflation" for Timor-Leste, given the large variability of import baskets and of the geographical structure of our imports.

After evaluating with several functional forms for this variable, it was concluded that the most appropriate empirical variable seems to be an average of the inflation rates of the five largest economies of ASEAN and China converted into dollars. In practice, this measure corresponds to an average of the regional inflation rate measured in dollar terms, which at the same time captures the impact of regional exchange rate variations against the dollar and local currency inflation rates.

Foreign inflation tends to influence the inflation trajectory in Timor-Leste.

Chart 1.15

Internal and external inflation



% annual change

- Inflação doméstica FMI
- Inflacao external
- Inflação doméstica INE-TL

Fonte: INE-TL, FMI e BCTL

As can be seen on the chart 1.15 above that domestic inflation tends to reasonably follow the development of foreign inflation rates with lower volatility. It is important to note that the external inflation rate is the average of the six Asian economies as mentioned previously, BCTL's inflation forecasting models use this variable and respective expectations to construct inflation forecasts.

The acceleration and deceleration of external inflation in overall supported the rise and fall of inflation in Timor-Leste.

Additionally, it can be concluded from the above two charts that the rise and fall in the domestic inflation rates in overall, influenced by the rise and fall in external inflation rates. Normally, the relationship is not perfect, as Timor-Leste's non-oil economic developments, especially over the last few years, strongly affect the domestic inflation rate trajectory.

It should also be noted that unlike external inflation and global inflation in general, inflation in Timor-Leste was accelerating in 2023, reflecting higher import taxes and some selected imported goods applied during the first semester of that year. Government doubled the import tax on all imported goods and applied progressive taxes on some selected items such as sugar, cigarette and soft drinks. They were reversed by the current government in the third semester of 2023 after took control the government in June 2023.

In terms of trajectory, 2021-2022 was naturally marked by the intensification of external inflation pressures, which exerted upward pressures over domestic inflation, reversing the trend recorded in 2019 and 2020 towards lower inflationary pressures. Domestic inflation contradicted global trend in 2023, reflecting the fiscal policy of increasing import taxes, adopted by the government at the end of 2022. In 2023, our external inflation metric ascended to 2.0%, resulting from the combination of a 2.4% external inflation rate in local currency terms and a 0.4% average depreciation rate of regional currencies against the US dollar.

As external inflation rates in local currency terms, except 2022 and 2023, are relatively stable over time, it can be concluded that the developments of local currencies against the dollar in the partner countries are, in turn, a very important factor in determining domestic inflation.

Considering the importance of this transmission channel, the future trajectory of external inflation, strongly influence by exchange rate developments, will continue to be one of the most influential factors in determining the evolution of domestic inflation.

The expected stability for regional currencies in 2024 and 2025 is a relevant assumption of BCTL's projected slowdown in domestic inflationary pressures.

In this context, the BCTL expects that, in line with the IMF, regional currencies will remain relatively stable against the dollar in 2024 and 2025 (depreciation of 0.4% per year), which, together with the maintenance of moderate inflation rates of trading partners, around 2.5% per year, leads us to expect that imported inflation will remain stable over the same time horizon (2.1% year), helping to stabilize inflationary pressures in Timor-Leste in both 2024 and 2025. Therefore, BCTL expects that the average domestic inflation rate will slow down over the next two years, gradually decelerating from 8.4% in 2023 to 4.6% and 2.0% in 2024 and 2025, respectively.

As the performance of the domestic economy also contributes to explaining inflationary trends, the domestic growth forecasts will be discussed in the chapter covering domestic economic developments, which also provides greater detail regarding inflation forecasts.

1.3.2. Energy Markets and Oil Revenues

Price of energy commodities such as oil, natural gas and coal in global markets are highly volatile, fluctuating widely between periods both with regimes of high and low-price levels. Charts 1.16 and 1.17 below show these price fluctuations and help us to place the recent developments in energy prices on a longer time-frame perspective. It should be noted that it is common for energy prices to fall by >50% and rise by more than the same percentage within a year, as the 2023's commodity prices demonstrate. In terms of levels, the sharp decline in oil prices from the end of 2014 cancelled out all nominal price gains recorded since 2009.

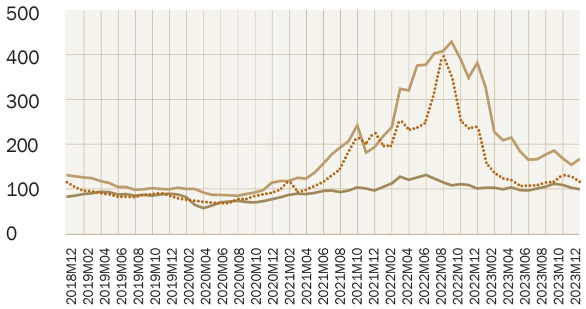
Oil and most commodities' prices recorded a notable fall in 2023, after the sharp increase recorded in 2021 and 2022.

In 2023, there was a remarkable loss of practically all energy resources, with particular emphasis on natural gas and coal. Of the energy commodities considered in the charts below, natural gas and coal are now at their record lowest of the last three years, reversed the high prices recorded in 2020, 2021 and 2022, which clearly confirms the difficulties of energy supply in adjusting and satisfying the global demand's recovery in 2023. The IMF report indicates that low demand, high storage overhang in the past winter, the ample supply of liquified natural gas and of pipeline from Norway and Northern Africa contributed to the natural gas price fall in 2023.

Oil price - brent reference - fall 3.8% at the end of 2023, and annually it fell 17.2%, partly cancelled out the pronounced recovery observed in 2022, caused by economic factors mentioned previously. Even so, oil continues to be traded at lower prices than in 2012, continue minimizing the recovery recorded during 2021-2022.

Chart 1.16

Energy prices – spot level



2012 = 100

— Oil

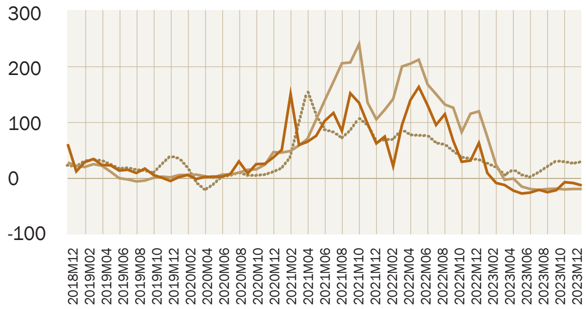
— Coal

··· Natural gas

Source: World Bank

Chart 1.17

Energy prices - % annual change



% annual change

··· Oil

— Coal

— Natural gas, US

Source: World Bank

Future energy prices trends are, however, not easy to anticipate, as it results both from the interdependence between aggregate demand and supply in physical markets, and, increasingly, from the less measurable and unpredictable effects resulting from the financialization of these markets, evident in the expansion of the financial derivatives market and increasing participation of financial intermediaries and speculators. A clear proof of this prediction shortcoming is, clearly, the recent fall in oil prices in 2023, after the substantial rise in 2021 and 2022, whose speed and magnitude were in no way predicted by most market participants and analysts. Transition to green energy and geoeconomic fragmentation due to geopolitical tension, resulted in fragmentation of world commodity markets further complicate the trend of future energy prices to anticipate. Fragmentation of commodity markets especially critical minerals for energy transition also make it more difficult to achieve the goal of decarbonizing world economies.

The country's oil revenues are now practically marginal when compared to the revenues obtained in the past years.

It should also be noted that the impact of energy price fluctuations on the country's oil wealth is now much lower than in previous years. This is due to the fact that oil revenues, taking into account Bayu-Undan, the fields actively in exploration, was ceased to produce completely at the end of 2023. Estimated gross revenues in 2023 amounted to $427 million, which represents a renewed decrease of 61.4% from the 2022's expected gross value of $1,106 million. This is equal to a total volume of around 7.01 million barrel of oil equivalent produced in 2023, a decreased of around 60%, compared to total barrel of oil equivalent produced in 2022, proofing further the depletion of oil and gas in Bayu-Undan. In 2022, the country produced a total of 17.3 million barrel of oil equivalent from the Joint Petroleum Development Area production.

Taking into account this current cease of oil production and uncertainties of future investment in greater sunrise, it is impossible to detail future earning estimation from oil and gas in this report, as has already done in the previous years, the sensitivity analysis of domestic oil revenues in terms of various oil prices. Although there has been petroleum exploration in dry lands such as the one in Covalima, the fields need to be proven both commercially and economically first.

1.3.3. Financial Markets and the Petroleum Fund

Financial asset prices influence the PF ESI, in turn, overall funding of the State Budget.

Lastly, we consider another transmission channel of international financial market developments to our economy, which relates to the Petroleum Fund (PF), established to efficiently manage the oil wealth of the country. The working mechanism of this channel is similar to the price of oil, to the extent that the price changes of international financial assets drive the value of the PF and, in turn, the 'Estimated Sustainable Income' (ESI) of the fund. Insofar as they drive changes in these two aggregates, financial asset prices end up influencing the amount of revenue available to finance the state budget and, consequently, the path and scale of spending and public investment policies.

In 2023 the fund invests 70.13% of its value in bonds and 29.87% in equities.

The PF concluded in the last quarter of 2023 recording a total net financial assets of $18,252 million, which represents a renewed increase of $979 million versus 2022's closing balance of $17,273 million. The Fund is mainly invested in treasury bonds of developed countries as marked with liquidity portfolio and fixed income portfolio (70.13%) and around a third (29.87%) of the fund invested in shares of developed markets' companies.

In 2023, the Fund recorded an overall, after fees and taxes, net profit of $1,642.667 million, reversing the net profit of -$2,050.438 million recorded in 2022, and added to the net profit of $1,144 million recorded in 2021. This performance was practically due to the rise in 10-year bond interest rate, rise in equity price and the marginal impact of the exchange rates appreciation as 2-year bond portfolio recorded a global fall in 2023.

Since the beginning, the fund has broadened its investment universe, starting, first, with only investing in US Treasury securities, it then gradually investing in shares and, finally, extend it to investing in bonds issued by several global Treasuries. This gradual extension of investment was driven by the increasing demand for a higher expected return for the fund and look for greater diversification of its investments in relevant markets.

This institutional development exposes the fund to new risks and markets, but which, by benefiting from the diversification of the prices of the various assets, it allows to build a more solid portfolio whose return is to be more efficient.

The performance of the fund is crucially driven by price changes in global bonds and equities markets.

So far, the Fund invests only in fixed interest rate bonds and equities, so that, received interest and dividends on bonds and shares provide the Fund with a fixed and constant income, at least on 'a priori' basis. Naturally, when investing in bonds and stocks, the Fund benefits from increases in market values of these securities, and on the contrary, it can be adversely affected by eventual negative price changes. Therefore, the Fund's main financial risks correspond to possible losses arising from the fall in the prices of the bonds or socks in which the Fund is invested.

Foreign exchange fluctuations also affect the fund, which has invested in markets other than in the USD.

In addition, since the fund invests in several markets denominated in currencies other than the US dollar, the fund is also subject to exchange rate risks, which understands as the possibility of depreciation of the various investment currencies against the dollar. As already reported previously that financial risks of the petroleum fund include three types of risks namely: equity risk, or risk of falling global stock prices, interest rate risks, which translates to the risk of falling Treasury bond prices; and currency risk, which refers to the risk of depreciation of the investment currencies against the US dollar.

The price changes of petroleum fund assets and the various investment currencies constitutes the true channel of transmission between international markets, the value of petroleum fund and its estimated sustainable investment (ESI) and the economy of the country.

In 2023, the fund recorded a positive performance, mostly due to the gains of its equity investments.

In terms of returns, 2023 was marked with positive return on the fund, which returned 9.60% in terms of its 2023's closing value, reversing the loss recorded in 2022 (-10.36%) and adding to the gains it recorded in 2021 (6.25%). The loss in the Fund's growth portfolio especially in the third quarter cancelled out part of the gains from its investments in 2023, especially from equity portfolio where most of the gains came from.

Bond investments recorded a net gain in 2023, due to the general fall in 2-year interest rates, partially cancelled out the interest rate rise recorded in 2022.

In the European market, representing by Germany, long-term interest rates also fall slightly, but remained in positive territory, prolonging the positive rate recorded in 2022 which was greatly above the zero threshold, where they have been since 2019. This generalized fall in rates due to fall in Germany, reversed the cycle of interest rate rose in 2022, contrary to the rate in the US market, which represents the majority of the Fund's bond investments, positively impacted the Fund return. This development can be interpreted as a global gain for the fund's bond portfolio in 2023 as the fund's bond portfolio yielded 9.16%, cancelled out part of its losses recorded in 2022 (-7.09%) and in 2021 (-2.25%). Unlike the European market, Japanese market follows the path of bond market in the US, its long-term interest rate increased by 0.19 percentage point from 0.42% recorded at the end of 2022.

In terms of equity markets, the fund's equity benchmark (developed markets) accumulated gains in 2023. The gains in the equity portfolios were due to the increased trend in the US market and also due to upward trend in most global equity markets. The petroleum fund investments in equities recorded a gain of 23.67% in 2023, reversing the substantial loss of -16.84% recorded in 2022 and added to the substantial gains of 22.72% it recorded in 2021. In terms of foreign exchange impacts, the petroleum fund was also affected positively by the depreciation of the USD against the investment in other currencies.

The fund investments in shares have again benefited from the robust performance of practically all global equity markets, led by the US market.

In short, the PF currently holds a portfolio of a vast and diverse set of securities and is invested in major global stock and bond markets, that efficiently optimizes its return profile, and at the same time minimized its associated risks.

However, given its substantial investments in global bonds and equities, the future financial value of the petroleum fund and its returns trajectory continue to depend on price developments for these financial assets, which are naturally also affected by the development of the dollar against the respective investment currencies.

The value of petroleum fund and returns continues to depend on the price developments of the global financial assets.

For a longer term, a need to consider the risk of a global stock or bond market correction is important, given the current and simultaneous high stock market valuations and the still high levels of global bond interest rates, despite the rates recorded in 2022. The trends evidenced in 2023 have further reinforced this historical high valuation of securities in both investment markets. With inflation pressures decline, market expects that future policy rates will decline which further contributes to decline in long-term interest rates and rising equity markets. Additionally, central banks' policy rate decisions are becoming increasingly asynchronous, some already easing their policy rates and some are not yet pushing for further risk consideration.

However, the long-time investment of the Fund and its institutional framework was designed to deal with the market fluctuation in a rational way to benefit from the occasional episodes of price fluctuation that regularly occur across markets, by implementing the investment fund discipline rigorously and a targeted asset allocation.

On the contrary, the complete cease of production from Bayu-Undan at the end of 2023 and the lack of significant future oil revenue due to uncertain greater Sunrise exploration development and the waiting of technical and economical proven of petroleum exploration in the dry land, together with continued maintenance of a level of public expenditure that requires reduction of the Fund's capital is now present significant risks to the success of the strategy and respective investment horizon of the Fund. Therefore, the fund objectives and its implementation strategies need to reassess in line with this current development.

CHAPTER 01