Revitalizing the National Economy through **Innovations and Synergies**

Annual Report 2021

Table of contents



Introduction

The annual report of the Banco Central de Timor-Leste (BCTL) summarizes and presents the main national and international economic developments in 2021, as well as the activities carried out by the BCTL throughout the year. The Organic Law of the Central Bank establishes and provides the duties and framework for the Bank's annual reporting to the President of the Republic, the National Parliament, the Prime Minister and the Minister of Finance. The report includes two major sections, specifically, the assessment of relevant domestic and international economic developments, including also near term projection scenarios and the presentation of the Bank's activity report, which encompasses as well the relevant financial information.

2021 was marked by the remarkable recovery of the world economy, after the pandemic crisis and the respective global recession of 2020. The world economy grew 5.9% in 2021, after having retreated -3.1% in 2020. Analogous to the 2020 crisis, the economic recovery was transversal and synchronized across practically all geographies. According to the IMF, developed countries' aggregate GDP has already reached its pre-pandemic levels in 2021, but developing countries' GDP level in 2021 is already 4% above that of 2019.

In terms of prospects for 2022 and 2023, the IMF expects the world economic recovery to continue. The IMF specifically forecasts that the world economy will grow 4.9% in 2022 and 3.6% in 2023. This optimism is based on the perpetuation of the success of vaccination programs and containment of the degree of severity of the virus, as well as the gradual reduction of restrictions on economic and social activity over the next two years. This assumption, together with the ongoing robust economic recovery, supported by ample economic policy stimulus programs, justify the optimistic perspectives of the IMF. Even so, the Fund and most international institutions have repeatedly warned that the world economy continues to face substantial downside risks, highlighting the resurgence of global inflationary pressures to the highest levels of the last 30 years and the difficulty of properly adapting and withdrawing the monetary and budgetary stimulus programs implemented over the last two years. Additionally, despite the fact that the risk of the virus has already been partially mitigated with vaccination programs, the evolution of the virus and its variants continues to represent a material risk to expected extension of the global recovery.

Global inflationary pressures increased notably in 2021, visible in the USA, Euro-Zone and ASEAN economies, to record levels in recent decades. In these 3 blocs, annual inflation reached values well above 2%, which tend to be the benchmark for most central banks, with average inflation in the US and Eurozone standing at 4.3% and 2.2% in 2021 However, the IMF foresees a gradual convergence of average inflation rates in 2022 and 2023 towards 2%, in practically all world economies, 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 temporary productive and logistical constraints and that the economic policy authorities worldwide will be able to successfully reverse their stimulus programs in 2022 and 2023, moderating and adapting aggregate demand growth to the productive capacity of the respective economies.

In the money and bond markets, there was a general rise in interest rates in practically all geographies and maturities, especially in the USA, due to higher inflationary pressures and the economic recovery’s strength. In the foreign exchange markets, the dollar ended up registering a slight appreciation against the main international currencies in 2021, driven by the rise in the dollar interest rate differential.

The performance of the Petroleum Fund’s investments continued to benefit from the renewed elevation of world equity prices, but was penalized by the rise in interest rates in 2021, which resulted in losses for the Fund’s bond portfolio. However, the materialization and reinforcement of a scenario of historically high valuations, especially for equity markets in 2021, should naturally limit the future performance of the Fund in the coming years.

Asian economies once again performed above average in 2021, which was due to the general success in containing the virus and the rapid and synchronized recovery of production processes and economic activity in the region’s countries. In line with global optimism, the IMF expects the continued substantial and widespread recovery of economic activity in the region in 2022 and 2023, predicting that the bloc will continue to lead the world in terms of economic growth.

In the national context, Timor-Leste's economy returned to growth in 2021, but only recovered partially from the recession recorded in 2020 (fall of -8.6% of GDP). The recovery 2021 was mainly due to the stabilizing effect arising from the significant increase in public expenditure throughout the year, amounting to $306 million, and the expected recovery in private demand. However, despite the substantial increase in public spending, our estimates also consider the negative impacts arising from the extension of the pandemic mitigation measures, the massive floods of April 2021 and their respective damages, as well as the increase in inflationary pressures and the corresponding reduction in consumers' purchasing power.

For 2022, BCTL predicts the economic recovery to continue and economic growth to accelerate in Timor-Leste. This expectation is based, above all, on the continued growth of public demand in the coming year and on the acceleration of the growth in private demand, while higher net imports will once again cancel out part of the improvement in domestic demand.

In terms of budgetary policy, 2021 was marked by a significant increase in expenditure (+$306 million) and in the public deficit, practically due to the increase in current expenditure (+$326 million), in line with the increase in the respective budget. However, public investment continued to fall in 2021 (-$20 million), due to the weak execution rate of the respective budget. For 2022, BCTL expects a further increase in public expenditure and public budget deficit, mostly explained by the recovery in public investment in infrastructure and buildings, so that budgetary policy stimulus will continue to support the economic recovery from the 2020 pandemic crisis.

In line with the global trend, there was a notable increase in domestic inflationary pressures in 2021, with the average inflation rate standing at 3.8%, up from 0.5% and 0.9% in 2020 and 2019, respectively. The rise in inflation was mainly due to rising external inflationary pressures, explained by the strength of global demand recovery and the persistence of global production and logistical constraints in 2021.

Timor-Leste continued to record an external current account deficit, which increased in 2021, mostly driven by higher imports of goods and services. Despite the fact that oil revenues have registered a significant decline over the last years, these still remain an important factor in mitigating the impact of the substantial trade deficit on our country's current account balance.

Despite the challenging macroeconomic context, **the financial sector continued to remain robust and to record high dynamism** in terms of growth of its activity level, assets and funding resources. It is illustrative to note that bank credit continued to grow in 2021, as well as deposits and funds received by banks operating in the country.

It should also be noted that during 2021, BCTL developed several **relevant initiatives within the scope of monitoring the economic situation** and mitigating the economic impact of the pandemic crisis and the 2021's floods. In this context, we highlight particularly the continued implementation of the credit moratorium and loan subsidization program for households and companies, as well as the undertaking of households surveys in order to assess their degree of financial inclusion and socio-economic conditions.

In terms of activities, the Bank remains actively committed to promoting monetary and financial stability and the respective financial inclusion, having developed initiatives that are particularly relevant in this context. One of the main activities developed by BCTL was the "Campo Digital" program, which aims to promote knowledge and widespread use of new technological tools - mobile phones, electronic money wallets, ATMs and PoS - in the financial activities of our population. Also in 2021, the BCTL continued to operationalize its partnership with the Ministry of Education, Youth and Sports to continue to improve the teaching, monitoring and evaluation of the Financial Literacy program in schools across the country, taught to students from 1st to 6th grade. The celebration of the 7th anniversary of the National Savings Day, on 29 November 2021, took place at the administrative post of Maubisse, in the municipality of Ainaro and was attended by local authorities, representatives of commercial banks, fintech companies and their respective agencies, financial service users, students and the Maubisse community.

In the context of the **national payment system,** the Central Bank continued to make every effort to maintain sufficient liquidity reserves at all times to meet the needs for cash payments and to ensure the modernization and full functioning of the national payment and interbank settlement system, the R-Timor. The main developments registered in 2021 in this area consisted in the implementation of additional functionalities in the R-TiMOR system to serve the needs of the Ministry of Finance and its sub-accounts, now allowing national taxpayers to pay their taxes from the bank's ATM network or from their electronic money wallets. The implementation of the "B2W2B" functionality, in addition to making it possible to pay taxes, now allows any holder of a P24 bank card to transfer money from a bank account to an "e-wallet" account and vice versa. Additionally, the project to interconnect the P24 network with an Indonesian payments network under the responsibility of BCTL continued to be implemented, which will allow holders of domestic bank cards to use these in banks in Indonesia.

The BCTL continued to work closely with the Ministry of Finance as well as with the Petroleum Fund's Investment Advisory Committee to maintain an active and informed position within the ongoing discussions on the investment strategy of the Petroleum Fund and its rigorous implementation.

The Bank continues to maintain its focus on further advancing staff capacities, allocating significant financial resources for this purpose. This investment has been reflected positively on the institution's work quality, which continues to be recognized as one of the best in the country.

Finally, as has been usual and as BCTL's Governor, I would like to thank all the employees of the Central Bank, as well as our partners and interlocutors at various times, which continued to actively contribute to the consolidation of the Central Bank and the economic development of our country.

Abraão de Vasconselos | *Governor* | Dili, April 28th 2022

International Economic Developments

Chapter 1

This chapter describes and assesses the major global economic developments in 2021, covering also the economies of Timor-Leste's main trading partners, together with the more relevant international trends in global financial markets for our economy.

Based on this assessment, the chapter further looks into external developments' spillovers to our domestic economy, detailing the influences observed in 2021 and the prospects expected from 2022 to 2023. This analysis is based mainly on the most recent IMF's estimates and perspectives, presented in its "World Economic Outlook Updates", released in January of 2022 and October of 2021.

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

- 2021 was marked by the remarkable recovery of the world economy, after the pandemic crisis and the respective global recession of 2020. The world economy's GDP grew 5.9% in 2021, after having retreated -3.1% in 2020. Similar to the crisis, the economic recovery was transversal and synchronized across practically all geographies.

- According to the IMF, GDP in developed countries has already reached pre-pandemic levels in 2021, but developing countries' aggregate GDP's 2021 is already 4% above 2019's pre-pandemic level.

- In terms of projections for 2022 and 2023, the IMF expects a continued recovery of the world economy and across practically all regional and national economies. The IMF specifically forecasts that the world economy will grow 4.9% in 2022 and 3.6% in 2023. This optimism is based on the perpetuation of the success of vaccination programs and containment of the degree of severity of the virus, as well as the gradual elimination of restrictions on economic and social activity over the next years. This assumption, together with the robustness of the economic recovery recorded in 2021, supported by ample economic policy stimulus programs, underpin the IMF's optimistic perspectives.

- Even so, the Fund and most international institutions have repeatedly warned that the world's economy continues to face substantial downside risks, having highlighted the resurgence of global inflationary pressures to their highest levels of the last 30 years and the difficulty of adjusting and withdrawing the extraordinary monetary and fiscal stimulus programs implemented over the last two years. Additionally, despite the fact that the pandemic risks have already been partially mitigated by the vaccination programs, the future mutation of the virus and its variants continues to represent a material risk to the envisioned global economic recovery.

- Inflationary pressures registered a notable increase in 2021, especially evident in the US, Euro-Zone and ASEAN economies, to record levels in recent decades. In these 3 blocs, annual inflation reached values well above 2%, which tends to be the benchmark for most central banks, with average inflation in the US and Eurozone standing at 4.3% and 2.2% in 2021 .

- However, the IMF foresees a gradual convergence of average inflation rates in 2022 and 2023 towards 2%, in practically all world economies, 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 successfully reverse the respective stimulus programs in 2022 and 2023, moderating and adapting the expansion of aggregate demand to the productive capacity of the various economies.

- Asian economies once again performed above average in 2021, which was due to the general success in containing the virus and the rapid and synchronized recovery of production processes and economic activity 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 2022 and 2023, predicting that the bloc will continue to lead the world in terms of economic growth.

- In the monetary and bond markets, 2021 was marked by the general rise in interest rates in practically all geographies and maturities, especially in the USA, in line with the worsening of inflationary pressures and the strength of the economic recovery.

- In the foreign exchange markets, the dollar ended up registering a slight appreciation against the main international currencies in 2021, driven by the upward trend in the dollar interest differential. However, in the Asian context, there was a general appreciation of Asian currencies against the dollar, within a background of regional exchange market stability.

- Global equity and commodity markets ended up accumulating substantial gains again in 2021, benefiting from the strength of the economic recovery, supported by the success of macroeconomic stabilization policies, the substantial reduction in investor pessimism and the success of global vaccination programs.

- The performance of the Petroleum Fund's equity investments continued to benefit from the renewed rise in world share prices, but was penalized by the rise in interest rates in 2021, which yielded a global loss for the Fund's bond investment portfolio. However, the materialization and reinforcement of a scenario of historically high valuations, especially in the global equity markets in 2021, will naturally limit the upward future returns of the Fund over the coming years.

1.1 Major World Economies

1.1.1. Economic Growth in Major World Economies

2021 was marked by a notable recovery from the global recession recorded in 2020, following the pandemic and its respective economic and social impacts.

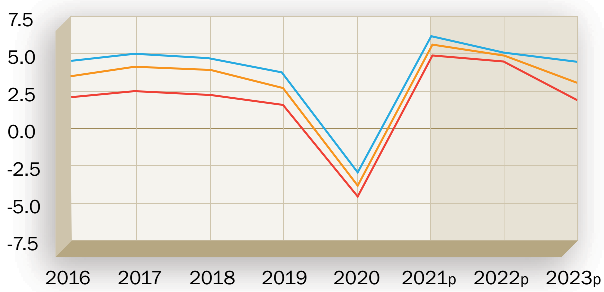
The world economy recorded a strong recovery in 2021, after the 2020 pandemic crisis.

Due to the increasing normalization of production processes and the success of global vaccination programs, supported by substantial budgetary and monetary stimulus programs implemented in practically all geographies, the world economy grew by 5.9% in 2021. Consequently, the global level of gross domestic product (GDP) has already exceeded the value recorded in 2019, which confirms that the -3.1% drop in output in 2020, the most pronounced annual fall in the last 30 years, was completely recovered.

Despite the substantial increase in inflationary pressures in 2021, which have already led to the reversal of part of the extraordinary monetary stimulus programs by many of the world's central banks, the economic outlook for 2022 and 2023 remains quite optimistic. Despite a slight natural slowdown compared to the growth experienced in 2021, the world economy, including the bloc of developed and emerging countries, is expected to continue to grow at very robust rates in 2022 and 2023, slightly above the trend recorded until 2019.

Chart 1.1

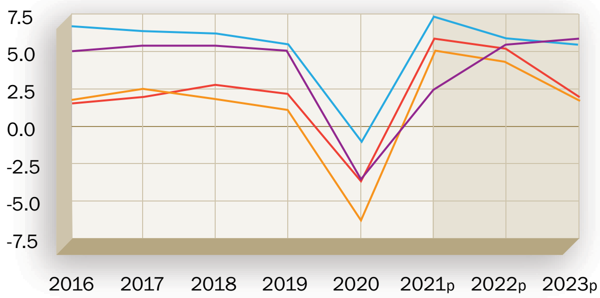
GDP Growth - 3 Major Blocs



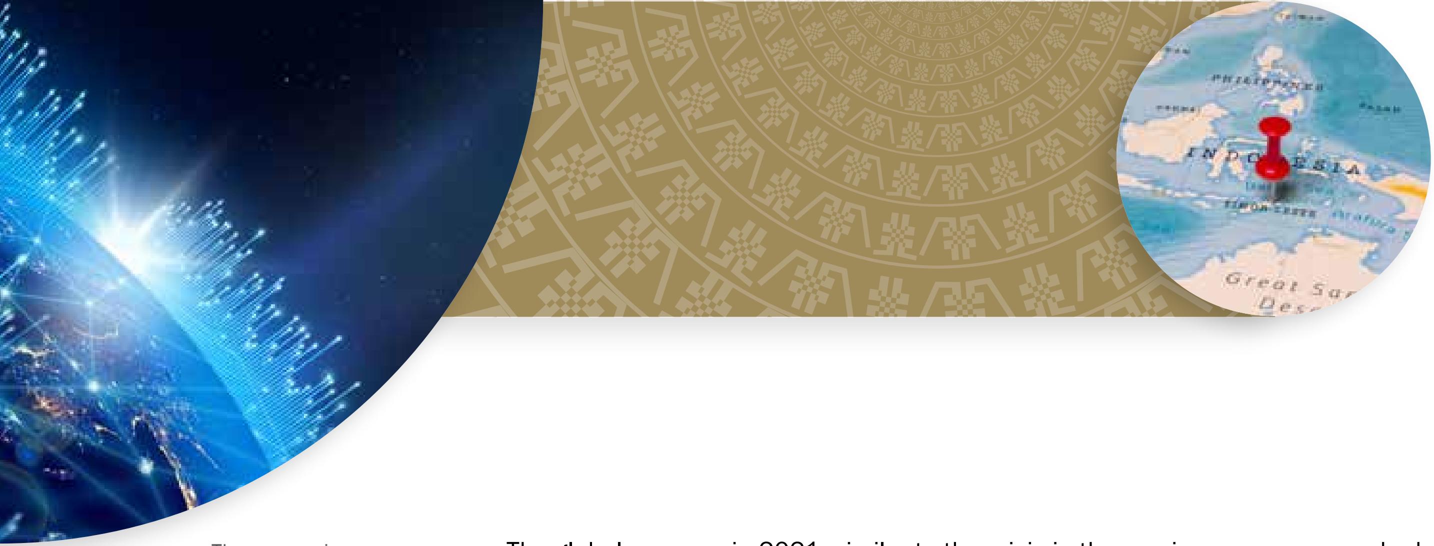
Source: FMI WEO

Chart 1.2

GDP Growth - Selected Regions



Source: FMI WEO



The economic recovery was transversal and synchronized, with many world economies recovering in 2021 the levels of activity of 2019.

The global recovery in 2021, similar to the crisis in the previous year, was marked by great synchronism in practically all the world economic blocs. According to the IMF projections, developed countries grew 5.2% in the aggregate in 2021, while emerging economies grew 6.4%. It is interesting to note that the developed countries expansion was very close to the growth pace in developing countries, which was also due to the fact that the 2020 crisis was more salient in developed economies, with the bloc's GDP falling -4.5 %, compared to the -2.1% drop recorded in emerging economies.

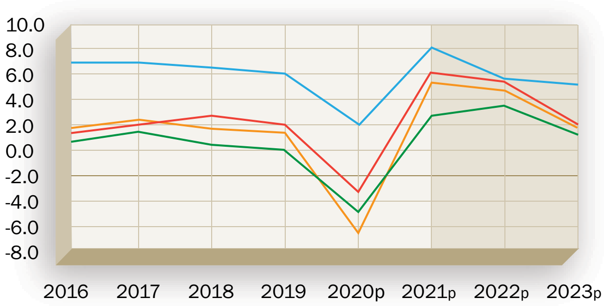
According to IMF forecasts, the developed bloc's aggregate GDP has already managed to reach pre-pandemic levels in 2021, but developing countries GDP in 2021 was already 4% above its pre-pandemic level of 2019.

In regional terms, it is also worth mentioning the noticeable economic performance of the Asia-Pacific economies, relative to global peers. The GDP of Emerging Asia and the 5 largest ASEAN economies grew 7.2% and 2.9% in 2021, after having demonstrated great resilience in 2020. With regard to the developed world, it should also be noted that the US economy has performed more robustly than the Euro-Zone, growing 2% since 2019, while the economy of the largest European bloc is still -2% below its 2019's level.

Charts 1.3.1 and 1.3.2 depict the comparative economic performance of the 4 largest world economies, which allows us to confirm the above-average performance of the Chinese and US economy during the pandemic and the decline and subsequent less expressive recovery in Japan. and the Euro-Zone.

Chart **1.3.1**

GDP Growth - 4 Major Economies



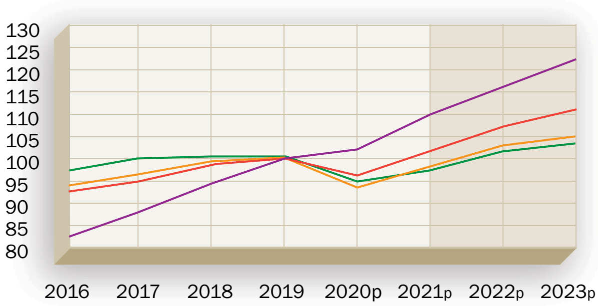
% annual change

US | E.U | Japan | China

Source: FMI WEO

Chart **1.3.2**

GDP Levels - 4 Major Economiess



2019 = 100

US | Japan | E.U | China

Source: FMI WEO

In terms of growth prospects for 2022 and 2023, the IMF generally expects the continued recovery of the world economy and across virtually all regional and national economies. The IMF specifically forecasts that the world economy will grow by 4.9% in 2022 and 3.6% in 2023, values which are slightly higher compared to the average growth recorded from 2012 to 2019.

The IMF's global outlook for 2022 and 2023 remains quite optimistic for almost all World economies.

This optimism is naturally based on the perpetuation of the success of vaccination programs and containment of the degree of severity of the virus, as well as the gradual elimination of restrictions on economic and social activity over the next years. This assumption, together with the robustness of the economic recovery seen in 2021, based on the ample economic policy stimulus programs, underpin the IMF's optimistic perspectives for the coming years.

Even so, the Fund and most international institutions have repeatedly warned that the world economy continues to face substantial downside risks, having highlighted, above all, the resurgence of global inflationary pressures to their record levels of the last 30 years and the difficulty in adapting and properly withdrawing the monetary and budget stimulus programs implemented over the past 2 years. Additionally, despite the fact that the virus risks have already been partially mitigated by the vaccination programs, the evolution of the virus and its variants continues to represent a material risk to the expected extension of the global economic recovery.

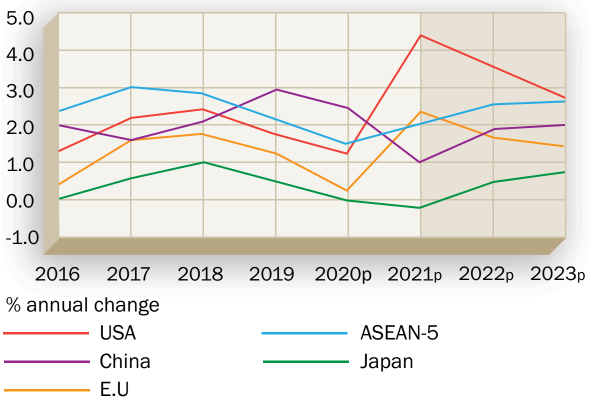
These optimistic growth prospects face substantial risks, such as the possible worsening of inflationary pressures, reduced economic policy support and the future evolution of the virus.

1.1.2. Inflation in Major World Economies

The following graphs show the evolution of average inflation rates and price levels in 5 of the main world economies.

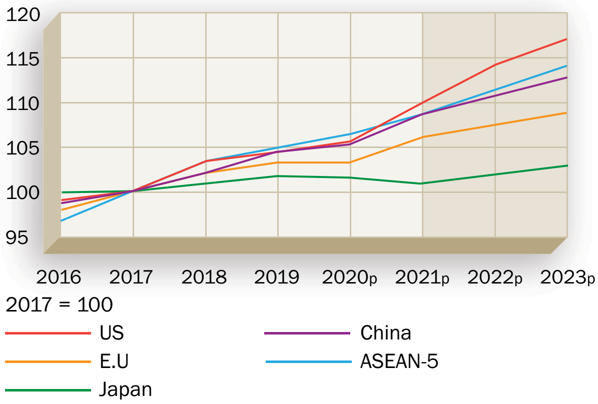
Global inflationary pressures rose substantially in 2021….

Chart **1.4.1**
Inflation Rates - 5 Selected Economies



Source: FMI WEO

Chart **1.4.2**
Price Levels - 5 Selected Economies

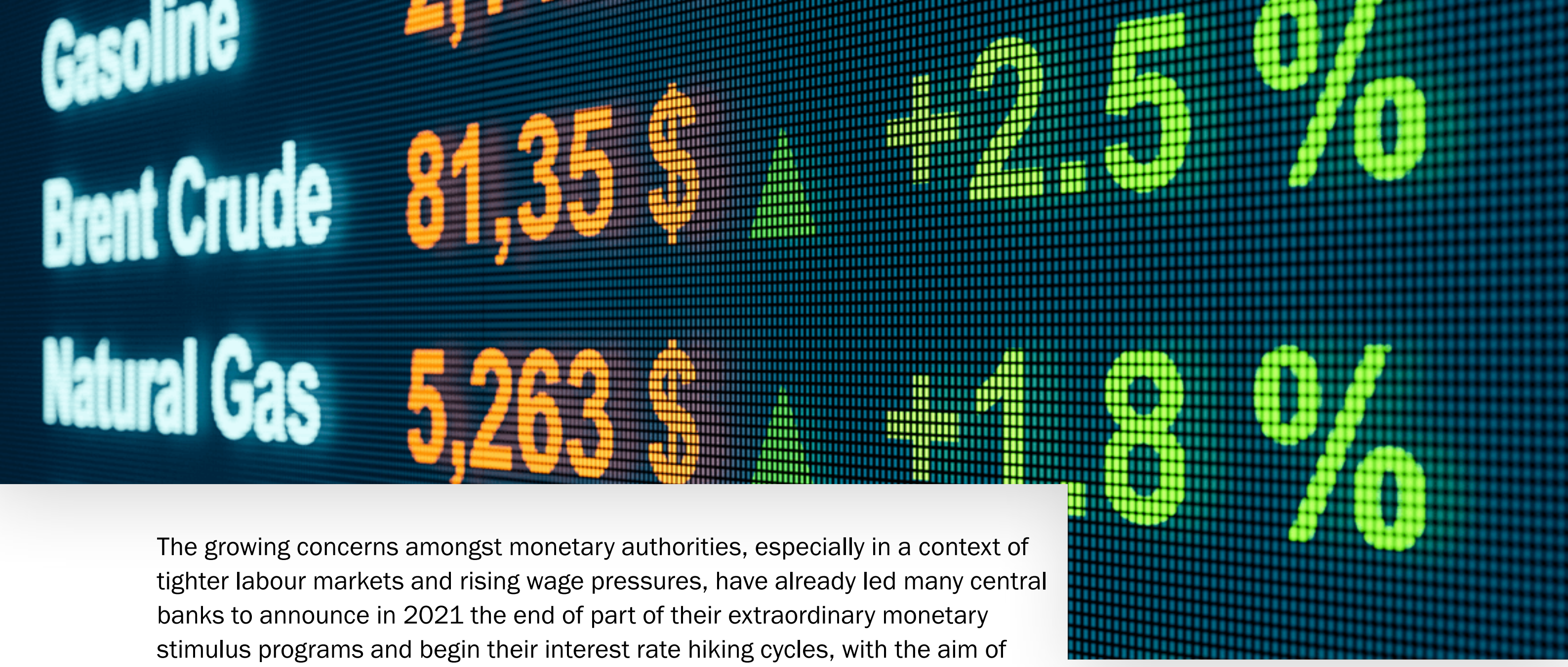


Source: FMI WEO

As can be seen, inflationary pressures registered a notable increase in 2021, especially evident in the US, Euro-Zone and ASEAN economies. In these 3 economies, annual inflation reached values well above 2%, which tend to be the benchmark for most central banks' monetary policy, with average inflation in the US and Eurozone standing at 4.3% and 2.2 % in 2021. However, it should be noted that these high average rates still obscure the sustained and worrying growth of inflationary pressures observed throughout 2021, with the year-on-year inflation rate in December 2021 being already above 7%. This value, which has not been observed since the 1980s, reveals the scale and dimension of the current inflationary episode. However, it should be noted that inflation levels in the Japanese and Chinese economies have been kept relatively low compared to their global peers, with their 2021's average inflation being -0.2% and 1.1%, respectively.

.... due to the strength of the economic recovery, the maintenance of highly stimulating policies and the perpetuation of productive and logistical constraints worldwide.

Naturally, the worsening of global inflationary pressures in 2021 resulted from the robustness of the global economic recovery and the highly stimulating degree of the implemented monetary and fiscal stimulus policies, particularly in the major developed economies. Alongside the material recovery in global demand, the persistence of social and economic restrictions, together with the worsening of constraints and failures in global logistics and production chains, also contributed to aggravate inflationary risks in most economies.



The growing concerns amongst monetary authorities, especially in a context of tighter labour markets and rising wage pressures, have already led many central banks to announce in 2021 the end of part of their extraordinary monetary stimulus programs and begin their interest rate hiking cycles, with the aim of moderating the demand expansion and curbing inflationary pressures.

In terms of perspectives, the IMF foresees a gradual convergence of average inflation rates in 2022 and 2023 towards 2% in practically all world economies, which constitutes the policy reference of many central banks. This means that 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 3.5% and 1.7% in 2022 and to 2.7% and 1.4% in 2023. On the contrary, inflationary projections in the Chinese and Japanese economy admit a slight acceleration in annual inflation to 1.8% and 0.5% in 2022 and 1.9% and 0.7% in 2023.

However, the IMF anticipates that inflationary pressures should gradually ease in 2022/2023, along with the adjustment of economic policies and the resolution of productive and logistical constraints.

This scenario is therefore based on the understanding that the current inflationary pressures result, above all, from the productive and logistical constraints that are still evident and that the economic policy authorities worldwide will be able to successfully reverse the respective stimulus programs in 2022 and 2023, moderating and adjusting the expansion of aggregate demand to the productive capacity of the various economies.

It should also be noted that the IMF continues to expect that the Euro-Zone and Japanese economies will continue to register inflation rates below those of the US in the next biennium, which should continue to register average inflation rates below the mentioned 2% reference..

1.1.3. Global Commodity Markets

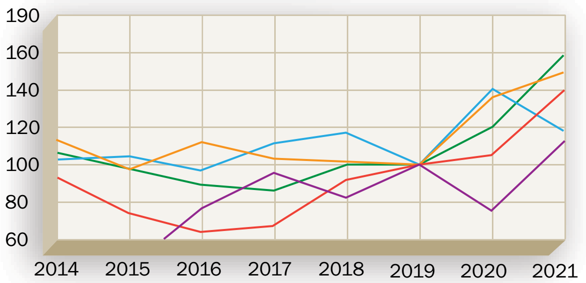
With a few exceptions, the year 2021 was marked by the general rise in market prices of the main traded commodities.

Commodity prices recorded broad-based gains in 2021.

This price rise occurred naturally in the global context of a substantial pickup in inflationary pressures, as mentioned in the previous point. The upward trend in raw material prices, in line with what had already happened in 2020, especially from April 2020 onwards, thus resulted in the extension of the recovery observed since the prices of most of these items recorded their lowest values, in 2015 /2016. For economies exporting these goods, typically developing countries, the continued rise of international prices represented a positive development.

Chart **1.5.1**

Major Commodities Prices - levels



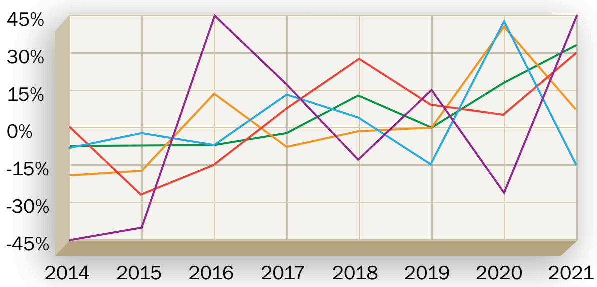
2019 = 100

Corn
Soybean
Wheat
Rice Viet.
Oil

Source: World Bank

Chart **1.5.2**

Major Commodities Prices - % change



% annual change

Corn
Soybean
Wheat
Rice Viet.
Oil

Source: World Bank

The oil price staged a remarkable recovery in 2021 (49%), in line with the strong recovery in world economic activity, after being one of the few commodities that recorded a price fall in 2020 (-24%). With this advance, oil price has already risen to its highest level since 2016.

The recovery in oil prices was due to the recovery in global demand in 2021, but also to the indirect impact of the global energy transition.

It should also be noted that the recovery in oil prices over the last few years and, in particular in 2021, has clearly highlighted the structural difficulties in the transition of the world's energic model. In fact, the recent reinforcement of the measures adopted towards the development of renewable energy sources and the reduction of CO2 emission levels, as well as the growing difficulty in financing companies and projects that invest in fossil energy sources, has 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, which was particularly evident in 2021 is also 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

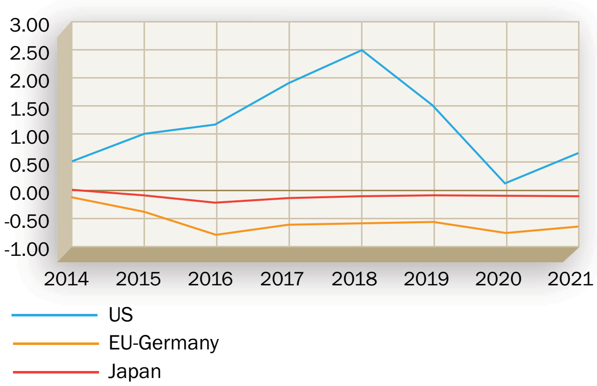
In terms of financial markets, we begin by analysing trends across major bond markets, particularly those for Treasury bonds, which allows us to assess trends and changes, as well as expectations, of monetary policies, economic growth and inflationary pressures of the various world economies.

In 2021, there was an increase in 2-year and 10-year interest rates, especially in the US market, as a result of growing inflationary pressures and the strengthening of expectations of a reversal of the monetary policy cycle in the major economies. This trend counteracted the widespread and broad fall in interest rates recorded in 2020, following the implementation of highly stimulating monetary programs to stabilize the world's economies.

Naturally, 2-year interest rates, which are more sensitive to changes in monetary policy, rose in 2021, especially in the case of the US. In economies where the level of short-term interest rates was below the zero threshold (0%), this rise was not yet so evident, with the respective central banks preferring to maintain their accommodative position for longer.

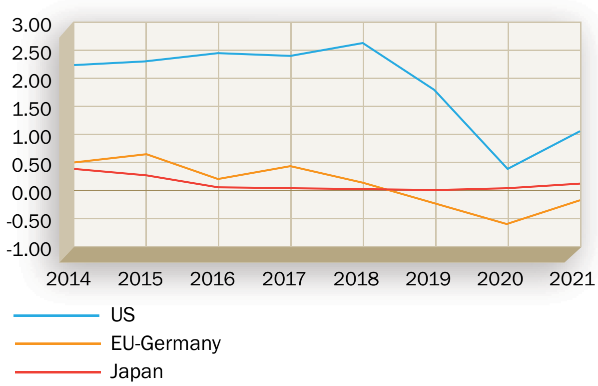
Two-year interest rates rose in the US, in line with worsening inflationary pressures and the strength of the economic recovery....

Chart 1.6
2-Years Interest Rates %



Source: Bloomberg

Chart 1.7
10-Years Interest Rates %



Source: Bloomberg

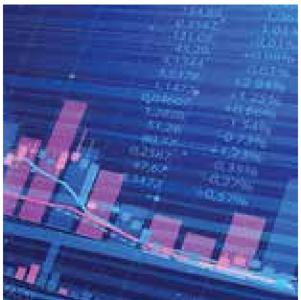
In the case of the US, the rise in 2-year interest rates was substantial, having increased from 0.12% at the end of 2020 to 0.73% at the end of 2021. Despite this recovery, 2-year interest rates in the US are still well below their pre-pandemic levels, which were 1.57% at the end of 2019. This development, especially considering that the rates of 2021 are still well below those of 2019, clearly shows that the monetary stimulus program of the FED (Federal Reserve Bank), including its key rates, is still at very stimulating levels for the US economy. Given the high level of inflationary pressures in the US at the end of 2021, the Fed should be forced to implement a continued and notable reduction in monetary stimulus throughout 2022, in order to stabilize inflationary expectations without compromising the respective economic recovery.

.... as well as longer interest rates, which also partially offset the declines recorded in 2020.

In the case of 10-year interest rates, there was also an increase in 2021 compared to 2020, thus reversing part of the fall recorded in the previous year. Even so, like the 2-year rates, the 10-year interest rates in the US market, valued at 1.52% at the end of 2021, are still well below 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 remained at negative levels at the end of 2021 (-0.17%), but recovered substantially, compared to -0.57% in 2020. However, the 10-year interest rate in Germany was already, at the end of 2021, slightly above its pre-pandemic level of 2019 (-0.19%).

In both 2 and 10 years, interest rates in the US remained at levels well above those observed for the Euro-Zone and Japan, similarly to what has happened since 2013, which seems to result from the perpetuation of the perspective that the US economy should continue to register a better relative performance over the next few years.

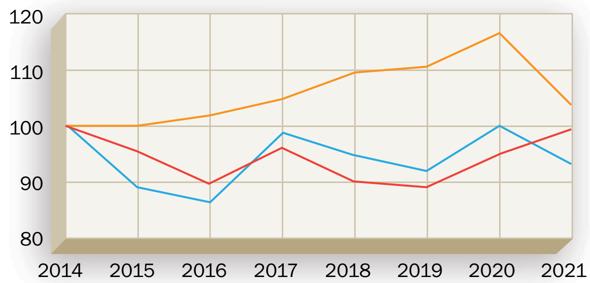
Naturally, bond markets developments, together with the economic developments already analysed, also determined a large part of the changes registered in the main foreign exchange and equity markets worldwide.



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

Chart **1.8**

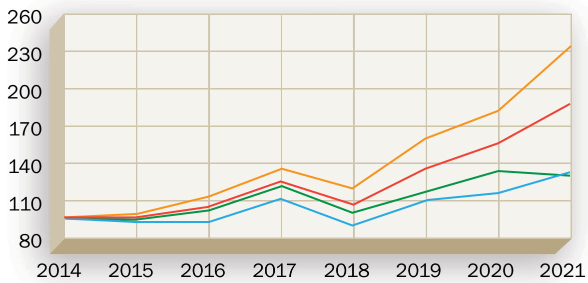
Major Currencies vs USD: 2014=100;
Decline corresponds to depreciation



Source: Google Finance

Chart **1.9**

Stock Markets Benchmarks, USD prices
2014=100



Source: Google Finance

In the foreign exchange markets, the dollar appreciated against the euro and the yen, but lost value against the Chinese yuan, contrary to the generalized depreciation seen in 2020. This change resulted, above all, from the growing inflationary pressures and FED's concerns, together with rising expectations of the immediate end of the monetary stimulus cycle in the North American economy. 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 currently offer higher rates of return than most debts from other developed countries. Additionally, Euro-Zone and Japanese central banks have shown less concern with their economies' inflationary pressures, having indicated that will extend their respective monetary stimulus programs.

In equity markets, most world markets continued to record a strong performance, thus extending the huge recovery seen since April 2020. As shown in chart 1.9 above, the main world equity markets accumulated gains in 2021, with the US market once again outperforming its global peers.

The major world equity markets recorded remarkable gains again in 2021, extending the upward trend observed since 2009.

The US equity market - represented here by the ETF (Exchange Traded Fund) that replicates the “S&P 500” index - recorded gains of 27% in 2021, after having risen 16% in 2020. These returns have been supported by the optimism regarding IT sectors and revolutionary technologies, which represents a growing and more significant portion of this market, when compared to other world’s equity markets. Additionally, the role of the expansionary fiscal policy and the extraordinary liquidity injections in the US and worldwide should not be overlooked as a driving factor of the equity markets’ robust performance in 2021 and 2020.

The dynamism of the equity markets in 2021 and 2020 thus again extended the long rising trend recorded since 2009, only partially interrupted in 2018, resulting in a generalized increase in the valuation ratio of shares’ prices relative to corporate earnings, to historically record levels.

In addition to the US, the global equity market recorded gains of 17% in 2021 (14% in 2020), with the Asian market – including developed countries only – falling -1%. The European market, as has been the habit in recent years, recorded gains below its global peers, having risen only 13% in the year.

In summary, the US stock market thus continued to far outperform the other world markets in the last 12 years, having continued to benefit from the greater dynamism of its economy, despite the global pandemic and recent confusing and disturbing political episodes.

Many equity markets, and specifically the US, are now considered to be broadly overvalued, when considering the ratio of stock prices to corporate earnings.

Taking into account the remarkable performance of this market in the last 12 years, which resulted in the substantial appreciation of stock prices in relation to corporate earnings, it should be noted that the downside risks to the substantial recovery of the American economy in 2022/2023, or to the record corporate profits today, more than ever, represents a significant risk to the future performance of this stock market.

1.2 Asian Economic Developments

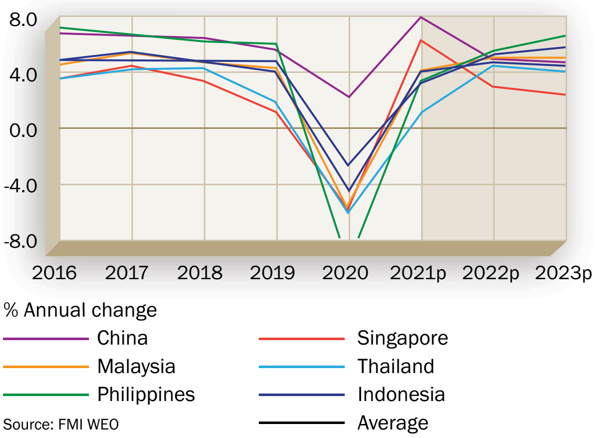
After summarizing the broad global macroeconomic background in 2021, it is important to detail the assessment of developments across the Asian space, in particular ASEAN, as the main economic partners of Timor-Leste are located in this region.

Our analysis focuses on ASEAN's five major economies and China, whose economy has increasingly taken a more global and regional relevance and clout. In turn, from these six economies, Indonesia continues to be Timor-Leste's main commercial partner, which justifies some further specific comments on its economic developments.

In terms of relevant developments for these economies, the 6 countries' GDP registered a generalized recovery, with average economic growth estimated at 4.2% in 2021, compared to a -4.4% fall in 2020.

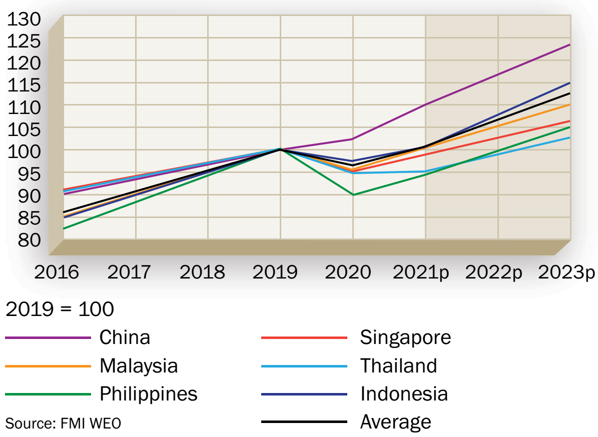
The largest Asian economies staged a remarkable economic recovery in 2021, after the pandemic crisis and its impacts in 2020.

Chart 1.10a
GDP Growth rates



Source: FMI WEO

Chart 1.10b
GDP Levels



Source: FMI WEO

The Asian economies thus continued to record a relatively robust performance in 2021, when compared to the other world economies, which was due to the general success in containing the virus and the rapid and synchronized recovery of production processes and economic activity in the region and its countries.

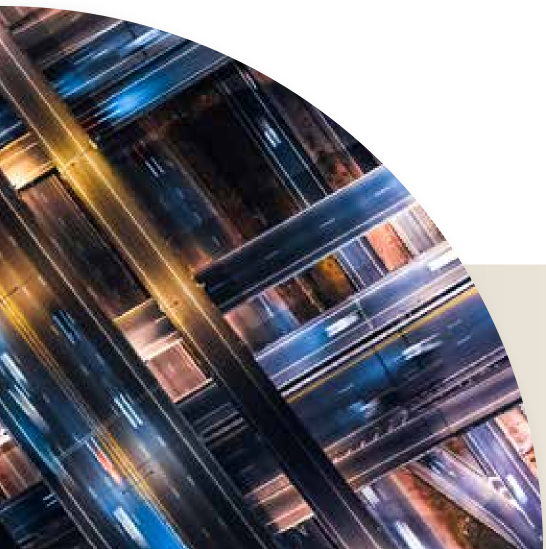
Of this group of countries, in 2021, only 3 - Philippines, Thailand and Malaysia - had an annual GDP level lower than that of 2019 (pre-pandemic), with Indonesia, China and Singapore having already recovered their pre-pandemic levels in 2021, with special emphasis on China, whose GDP in 2021 is already 11% above that of 2019.

The prospects for economic growth in the region remain very optimistic for 2022 and 2023.

In terms of prospects, in line with its global optimism, the IMF expects the continued substantial and broad-based recovery of economic activity in the region in 2022 and 2023, predicting that the region will continue to lead the world in terms of economic growth. It should be noted in this regard that the IMF now expects that all the 6 economies will regain their 2019's GDP levels in 2022, predicting an average growth rate in the 6 economies of 5.3% in 2022 and 5.2% in 2023.

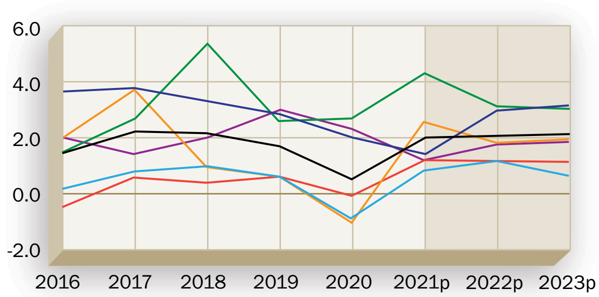
According to the same forecasts, at the end of 2023, the IMF expects China and Indonesia's GDP to be 23% and 14% above the value of 2019, which are the economies with the highest growth rates. On the contrary, Thailand and the Philippines are expected to be the lowest growth economies by 2023 in the region, as their output will only be 3% and 6% above their respective 2019 level.

Also in line with the global trend, inflation accelerated in 2021 in the region, contradicting the slowdown seen in 2020. The average inflation rate of the 6 Asian countries rose to 2% in 2021, compared to 0.8% in 2020 and 1.7% 2019. It is also worth noting that only 2 economies – the Philippines and Malaysia – recorded above-average inflation rates, valued at 4.3% and 2.5%, respectively.



Inflation in the region also accelerated in 2021, in line with the global trend.

Chart **1.11a**
Inflation Rates

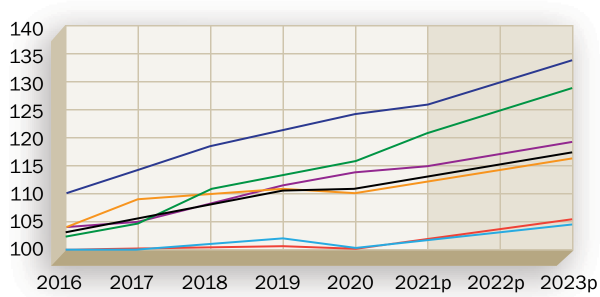


% Annual Change

China
Malaysia
Philippines
Singapore
Thailand
Indonesia
Average

Source: FMI WEO

Chart **1.11b**
Price Levels



2014 = 100

China
Malaysia
Philippines
Singapore
Thailand
Indonesia
Average

Source: FMI WEO

The IMF's outlook for 2022 and 2023 expects the materialization of a scenario of general inflation stability in the region, with average annual inflation remaining close to 2%, annually. Despite the expected extension of a robust economic recovery and growth in the region and rising global inflationary pressures, the Fund believes that Asian economies and their monetary authorities will be able to ensure that price stability is maintained and inflation remains close to policy-reference levels, during the next 2 years.

The rise in inflation rates in the various economies and the average depreciation of the dollar against the 6 Asian currencies, amounting to -3% in 2021 (appreciation of 0.4% in 2020) explained, in turn, the increase in regional inflationary pressures, when measured in US dollar terms.

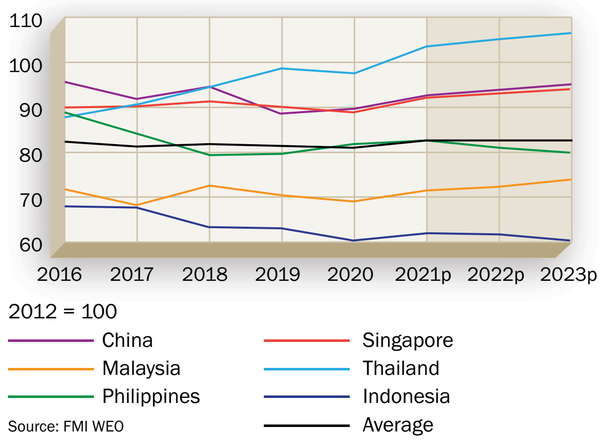
These relevant developments of terms of the main macroeconomic indicators - economic activity and inflation - help to explain, as are also explained, by the developments registered in the 2 main financial markets, the regional foreign exchange and bond markets.

In exchange markets, despite the high volatility recorded throughout the year, 2021 ended up being marked by the 3% average appreciation of regional currencies against the dollar, with the Philippines and Indonesia currencies being the only with annual appreciation rates below 3%, at 0.6% and 1.8%, respectively.

Regional currencies appreciated, on average, against the dollar in 2021....

Chart **1.12**

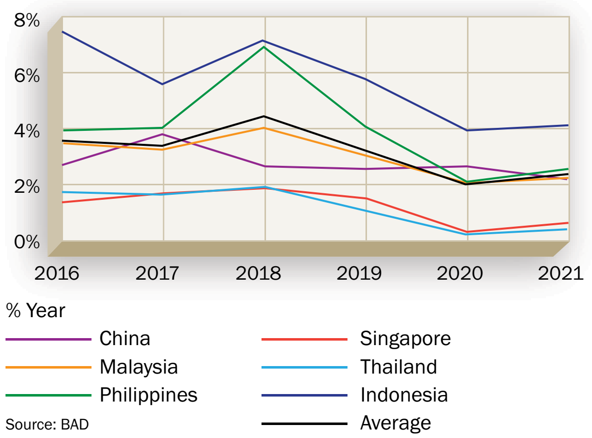
Exchange Rates vs USD



Source: FMI WEO

Chart **1.13**

2-Years Interest Rates



Source: BAD

The IMF expects that most regional currencies will remain relatively stable against the dollar between 2022 and 2023, which, if this scenario materializes, will contribute to stabilizing inflationary pressures in the region and, above all, to stabilizing the prices of goods imported by Timor-Leste. It should be noted, however, that this scenario of exchange rate stability may be materially affected by the risks related to the economic recovery, the evolution of the pandemic and inflationary pressures worldwide.

.... with 2-year interest rates rising, in line with the change recorded in the dollar market.

Bond market interest rates, represented here by 2-year bonds, registered a general increase in 2021, in line with world markets, thus cancelling out part of the decline recorded in 2020.

The average 2-year interest rate of the 6 economies rose from 1.8% in 2020 to 2.2% at the end of 2021, but continued to trade below the level observed at end of 2019 (3%). The rise in 2-year interest rates in the various economies resulted from the rise in reference rates by some central banks and also from their economic performance and prospects. Despite having followed the dollar market changes, interest rates in the region are still above the rates observed in most developed markets, which reflects their better relative economic performance of the region, but also the lesser room for manoeuvre in terms of monetary and exchange rate policy.

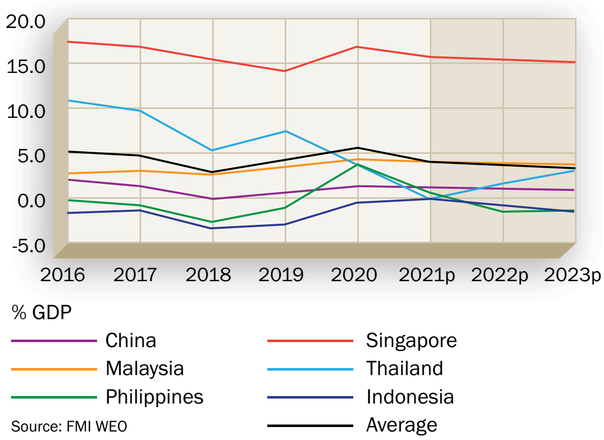
Regarding their external accounts balances, we can conclude that most partners continued to maintain substantial external surpluses in 2021, with the exception of Indonesia and Thailand, which recorded a current external account deficit of -0.3% and -0.4 % of GDP in 2021. It should also be noted that, although there was a reduction in the region's average external surplus in 2021, compared to 2020, the various economies managed to maintain positive external balances, despite the strong disruptions to economic activity and trade worldwide.

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

For 2022 and 2023, the IMF continues to predict stability in net external balances in the region, although it is also worth noting that the Philippines and Indonesian economies should continue to record increasing external deficits in this next biennium.

Chart **1.14**

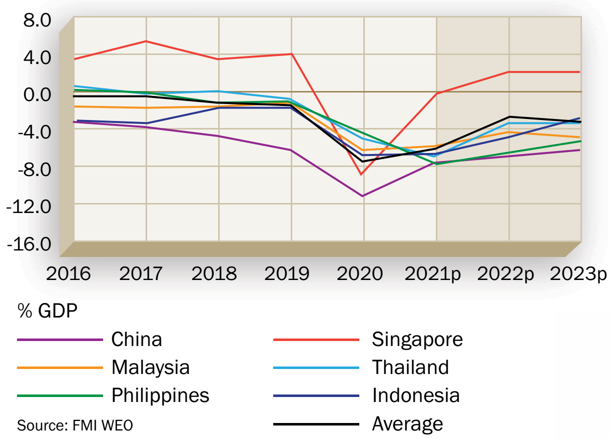
External Current Account Balances



Source: FMI WEO

Chart **1.15**

Fiscal Balances



Source: FMI WEO

In terms of budgetary balances, 2021 was marked by a slight reduction in public deficits in the region, with the average deficit falling from -6.9% in 2020 to -5.7% of GDP in 2021. This slight improvement in fiscal deficits cancelled out only part of the substantial deterioration of the public deficits of the various Asian economies in 2020, due to the drops in economic activity and the mobilization of substantial amounts to support the respective populations and economic sectors affected by the pandemic. Consequently, at the end of 2021, public deficits materially exceeded the respective average value of -1.6% of GDP, recorded in 2019. It should also be noted that Singapore recorded the largest deficit reduction in 2021, which fell from -8.9% in 2020 to -0.2% of GDP in 2021, which reveals the end of many public health support programs and economic activity in the country.

In 2021, public sector deficits continued to remain high in the region, which only partially offset the fiscal deterioration seen in 2020.

For 2022 and 2023, the IMF expects a gradual reduction in budget deficits in the region, anticipating an average deficit of -3.9% and -3.2% of GDP in 2022 and 2023. As a result, most economies should maintain a stimulative fiscal policy stance over the next 2 years, which will certainly help to explain the strength of economic growth in the next biennium. With the exception of Singapore, which should register a budget surplus as early as 2022 (+2% of GDP), the remaining 5 economies should continue to record deficits above -3% of GDP over the next few years. It should also be noted that the fiscal policies in China and the Philippines will continue to be the most accommodative in the region, with their respective public deficits amounting to -6.8% and -6.2% of GDP in 2022.

In short, in line with the global trends, there was a notable improvement in the macroeconomic background across the Asian region in 2021, which made it possible to recover completely the 2020's fall in economic activity and cancel part of the deterioration of macroeconomic fundamentals in the various economies.

It is also worth noting 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.

Note, however, that this general background does not fully apply to the Indonesian economy, Timor-Leste's largest trading partner. On the one hand, we highlight the vigorous recovery of its economy, which has already managed to recover in 2021 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 high deficit in public accounts (-6.1% in 2021) and a slight external deficit of -0.3% of GDP.

In terms of outlook, the Fund continues to expect a strong performance for the Indonesian economy over the next 2 years, with an average annual growth rate of 5.2%, as well as the central bank's success in maintaining a stable and moderate inflation rate (3% year) and stabilizing the rupiah's external value (annual depreciation of -0.7%). Although public and external deficits are expected to continue, the IMF forecasts clearly assume that the country will manage to avoid the macroeconomic volatility registered until 2018, visible above all in the depreciation of the rupiah, the increase in inflationary pressures and the fall in external revenues, resulting from the tumble in international prices of many commodities exported by the country.

Naturally, the pluriannual recovery in the price of these raw materials, particularly visible in 2020 and 2021, has also supported, and is expected to continue to underpin, the recovery of economic activity and the country's export earnings. 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 evolution of the global "commodity" markets and the world economy.

The importance of this partner for our country and economy implies the maintenance of adequate monitoring of 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 above review of major international economic and financial developments as well as of Asian economic developments, which are much more relevant for Timor-Leste, would not be complete without understanding the respective repercussions on our economy.

This point tries to identify the main channels of transmission of the international developments to our economy. At present, it is reasonable to accept that these effects are still small and limited to certain sectorial aspects of our economy. This chapter seeks to illustrate 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 allow us to analyse this relationship properly.

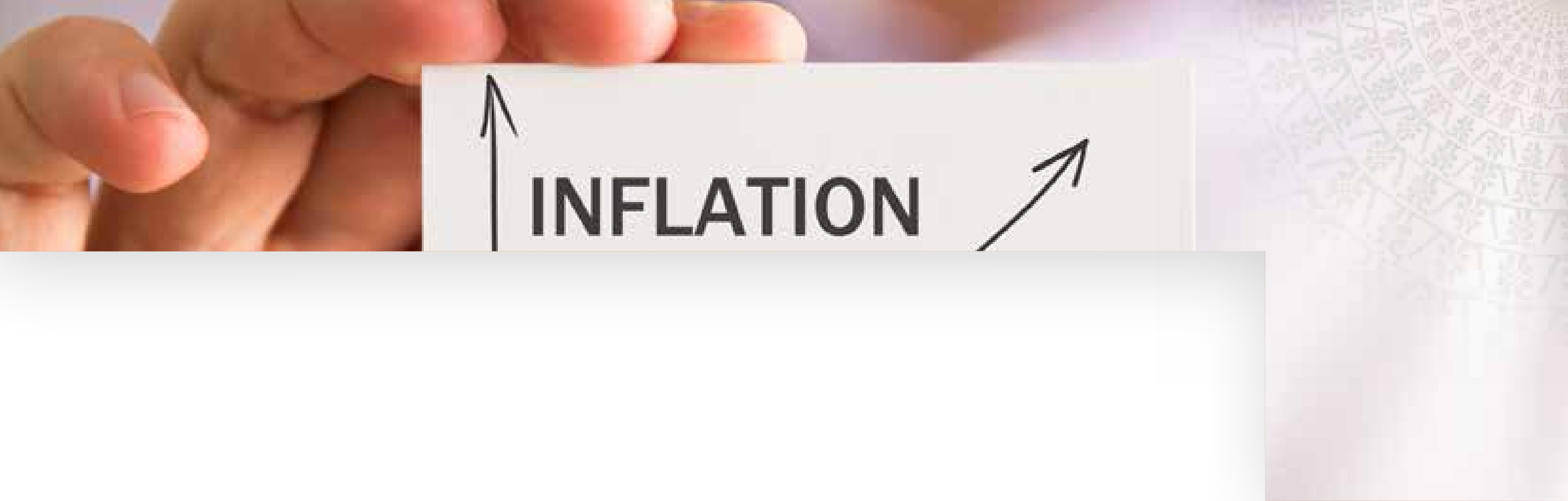
Naturally, as our economy develops and effectively deepens interdependence relations with its regional economic partners, we expect that external developments will increasingly shape developments in our domestic economy, expanding the number and influence of the various transmission channels.

1.3.1. Imported Inflation

One of the main transmission channels for our economy is in fact the impact of international prices on domestic inflation developments and respective expectations. Since Timor-Leste is an economy with great import intensity - imports of goods and services accounted for 47% of non-oil GDP in 2020 - it is natural to expect that international prices of imported goods and services will continue to substantially influence domestic inflation developments.

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

BCTL's empirical research and economic modelling has confirmed the importance of this channel. One of the main issues of our work in this context stems from the difficulty in defining an appropriate variable to measure the level of "external inflation" for Timor-Leste, given the large variability of our import basket and of the geographical structure of our imports. After experimenting with several functional forms for this variable, we concluded that the most appropriate



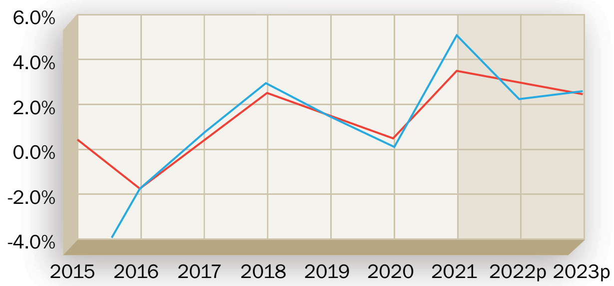
empirical variable seems to be an average of the inflation rates of the 5 largest economies of ASEAN and China converted into dollars. In practice, this measure corresponds to an average of the regional inflation rate measured in dollar terms, which at the same time captures the impact of regional exchange rate variations against the dollar and local currency inflation rates.

As can be seen below on the chart on the left, domestic inflation tends to reasonably track the movements of foreign inflation rates, albeit with lower volatility. To the extent that the external inflation rate is the average of six economies already mentioned, BCTL's inflation forecasting models use this variable and respective expectations to construct inflation forecasts.

Foreign inflation tends to drive Timor-Leste's inflation trajectory ....

Chart **1.16**

Domestic vs External Inflation



% annual change

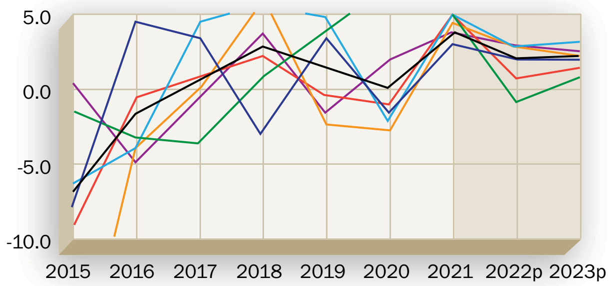
Domestic Inflation

External Inflation

Source: DGE and BCTL Estimates

Chart **1.17**

Regional Inflation in USD terms



% average annual change

China | Singapore

Malaysia | Thailand

Philippines | Indonesia

Average

Source: FMI WEO

Additionally, as can be concluded from the 2 charts, the rise in the inflation rate in 2021, as well as in 2017 and 2018, was positively influenced by the rise in external inflation rates. Naturally, the relationship is not perfect, as Timor-Leste's non-oil economic developments, especially over the last few years, also strongly affect the domestic inflation rate trajectory.

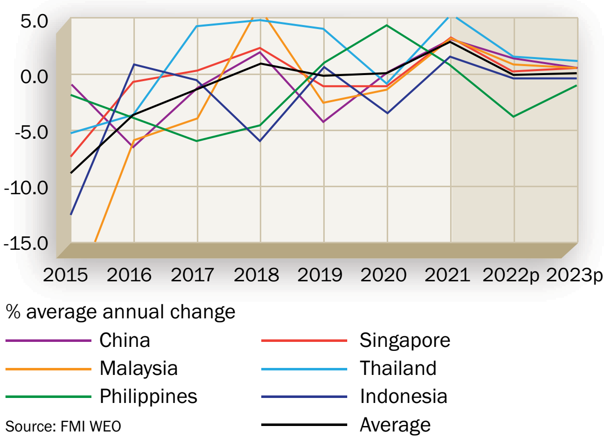
... so the acceleration of external inflation in 2021 supported the rise in inflation in Timor Leste.

In terms of trajectory, 2021 was naturally marked by the intensification of external inflationary pressures, which exerted upward pressures over domestic inflation, thus reversing the trend recorded in 2019 and 2020 towards lower inflationary pressures. In 2021, our external inflation metric ascended to 5%, which results from the combination of a 2% external inflation rate in local currency terms and a 3% average appreciation rate of regional currencies against the dollar in 2021.

As external inflation rates in local currency terms are relatively stable over time, it can be concluded that the movements of partners' currencies against the dollar are, in turn, a very important factor in determining domestic inflation.

Chart **1.18**

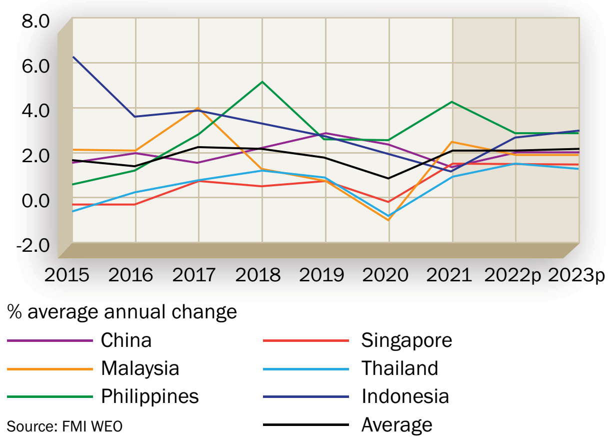
Asian Currencies vs USD



Source: FMI WEO

Chart **1.19**

Local Currency Inflation Rates



Source: FMI WEO

Bearing in mind the importance of this transmission channel, the future trajectory of external inflation, strongly driven 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 2022 and 2023 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 2022 and 2023 (appreciation of 0.2% per year), which, together with the maintenance of moderate trading-partners' inflation rates, around 2.1% per year, leads us to expect that imported inflation will remain stable over the same time horizon (2.3% year), helping to stabilize inflationary pressures in Timor-Leste in both 2022 and 2023. Therefore, BCTL expects that the average domestic inflation rate will slow down over the next 2 years, gradually decelerating from 3.4% in 2021 to 2.5% in 2023.

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

1.3.2. Energy Markets and Oil Revenues

Oil, natural gas and other energy resources' prices are highly volatile, having typically fluctuated widely between periods and regimes of high and low-price levels. The charts below depict these fluctuations and allow us to place the recent developments in energy prices on a longer time-frame perspective. It should be noted that it is not uncommon for energy prices to fall by 50% and rise by more than 50% within 1 year, as the 2020's pandemic crisis illustrates. In terms of levels, the sharp decline in oil prices from the end of 2014 cancelled all nominal price gains recorded since 2009.

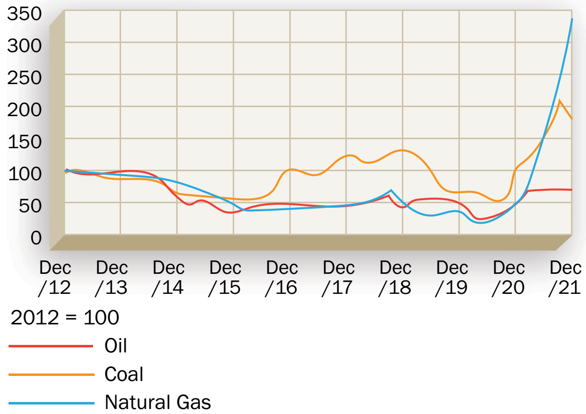
In 2021, there was a remarkable recovery of practically all energy resources, with particular emphasis on natural gas. Of the energy commodities considered in the charts below, gas and coal prices are now at their record highs of the last 10 years, which clearly confirms the difficulties of energy supply in adjusting and satisfying the global demand's recovery in 2021.

Oil and most commodities' prices recorded a notable recovery in 2021, after the sharp falls observed in 2020.

Oil price - brent reference - rose 49% in 2021, fully cancelling the pronounced fall in 2020, caused by the pandemic and rising to its highest level of the last 4 years. Even so, oil continues to be traded at lower prices than in 2014, having only partially recovered from the drop recorded in 2015.

Chart **1.20**

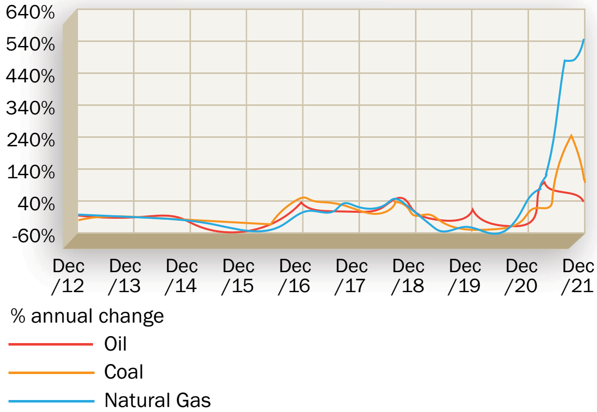
Energy Prices - spot levels



Source: World Bank

Chart **1.21**

Energy Prices - % change



Source: World Bank

However, it should be noted that the upward movement in the oil price in 2021 occurred in a context of relative stability throughout the year, after the significant volatility recorded in 2020, due to the disturbances caused by the pandemic crisis and its developments.

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 rise in oil prices in 2021, after the substantial fall in 2020's first half, whose speed and magnitude were in no way predicted by most market participants and analysts.

Timor Leste's future oil revenues are now practically marginal when compared to the revenues obtained in 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 future oil revenues, taking into account the fields in current exploration, are currently very small compared to what has already been extracted from the reserves of the Timor Sea, with the prospect that existing fields will cease to produce completely by 2023. Expected future revenues from 2022 to 2023 now amount to only around $150 million, which represents a renewed decrease from the 2020's expected value of $200 million.

Taking into account the now low estimates of expected future oil revenues from the Timor Sea, we do not detail in this report, as we did in previous years, the sensitivity analysis of domestic oil revenues in terms of oil prices' various projection scenarios.

1.3.3. Financial Markets and the Petroleum Fund

Finally, we consider another transmission channel of international developments to our economy, which relates to the Petroleum Fund (PF), established to efficiently manage the country's oil wealth. 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 Petroleum Fund and, in turn, the Fund's 'Estimated Sustainable Income' (ESI). 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 pace and scale of spending and public investment policies.

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

The PF concluded 2021 recording total net financial assets of $19,651 million, which represents a renewed increase of $660 million versus 2020's closing balance ($18,991 million). The Fund is mainly invested (69.43%) in developed countries' treasury bonds and in shares (30.57%) of thousands of developed markets' companies.

Presently, FP invests 69.4% of its value in bonds and 30.6% in equities...

In 2021, the Fund again recorded an overall (after fees and taxes) net profit of $1,104 million, which was below the $1,859 million and $2,100 million return achieved in 2020 and 2019. This continued and substantial performance was practically due to the renewed rise in equities investments, as the bond portfolio recorded a global loss in 2021, while exchange rate changes had only a marginal impact over the Fund's valuations.

Since its inception, the PF has been expanding its investment universe, starting, first, by only investing in US Treasury securities, then gradually investing in shares and, finally, extending investments to bonds issued by several global Treasuries. The gradual extension of its investment mandate was driven by the growing demand for a higher expected return for the Fund and search for greater diversification of its investments and relevant markets.

PF's performance is now crucially driven by price trends in global bonds and equities 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, allow a more solid portfolio to be built and whose risk-return profile is more efficient. At present, 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, by investing in bonds and stocks, the Fund benefits from increases in market values of these securities or, on the contrary, 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.

.... but foreign exchange fluctuations also affect the PF, which has invested in currencies beyond the USD.

In addition, since the PF invests in several jurisdictions and markets, denominated in currencies other than the US dollar, the Fund is also exposed to exchange rate risks, understood as the possibility and impact arising from the depreciation of the various investment currencies against the dollar.

In short, the PF's financial risk includes 3 types of market risk: 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 consists in the risk of depreciation of the investment currencies against the US dollar.

The price changes of PF's assets and the various investment currencies thus constitutes the true channel of transmission between international markets, the value of PF and its ESI and our country's economy.

In 2021, the Fund recorded another positive performance, practically due to the gains of its equities portfolio.

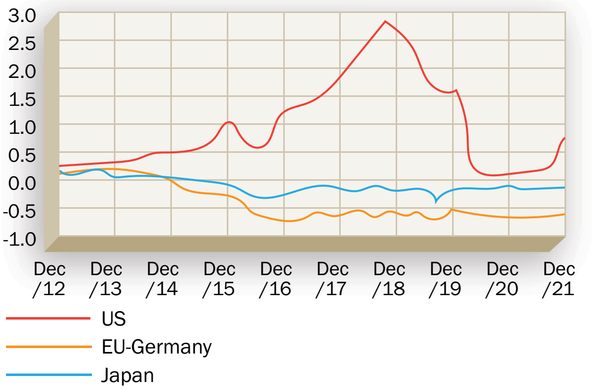
As noted, in terms of returns, 2021 was also very positive for the FP, which returned +5.7% in terms of its 2020's closing value, compounding the gains already recorded in 2020 (10.67%) and in 2019 (13.25%). However, in 2021, the loss in the Fund's bond portfolio cancelled part of the exceptional gains for its equity investments.

Bond investments recorded a net loss in 2021, cancelling part of the gains accumulated in 2020 and 2019. This loss was due to the generalized increase in interest rates during the year.

As previously mentioned, in 2021, global bonds and treasuries markets were impacted by a widespread increase in interest rates, especially in the US market, more marked in the case of 2-year maturities than in the 10-years. It should also be noted that these increases only partially cancelled out the interest rate falls recorded in 2019 and 2020.

Chart **1.22**

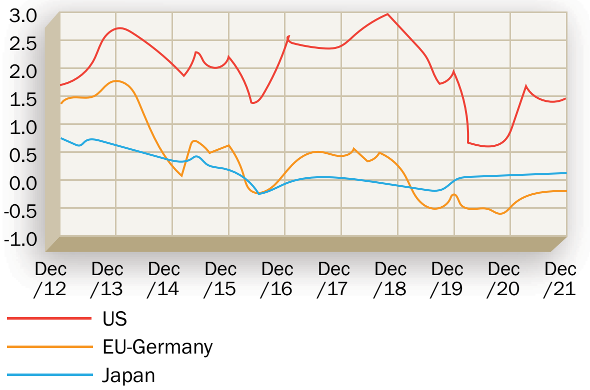
2 Year Interest Rates - % year



Source: Bloomberg

Chart **1.23**

10 Year Interest Rates - % year



Source: Bloomberg

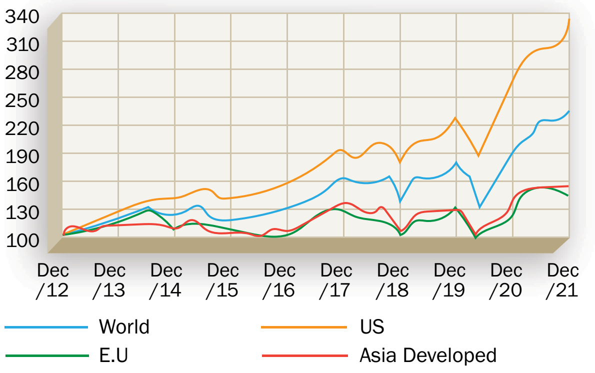
In the European and Japanese markets, long-term interest rates also rose slightly, but remained in negative territory, or close to the zero threshold, where they have been since 2019. This generalized rise in rates, which reversed the cycle of interest rate falls of 2019 and 2020, particularly in the US market, which represents the majority of the Fund's bond investments, negatively impacted the PF's return, despite the coupon income received from bonds. This development yielded a global loss for the Fund's bond portfolio of -2.25% in 2021, which cancelled part of its gains recorded in 2020 (5.04%) and in 2019 (5.16%).

In terms of equity markets, the Fund's equity benchmark (the black line in the chart below – "World") accumulated new gains in 2021. The gains in the FP's equity portfolio were due to the upward trend in the US market, but also in most global equity markets. PF's investments in equities recorded an exceptional gain of +22.71% in 2021, thus adding up to the substantial gains of 2020 (14.03%) and 2019 (27.67%). In terms of foreign exchange impacts, the PF was only marginally affected by a very slight appreciation of the USD against investment currencies.

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

Chart **1.24**

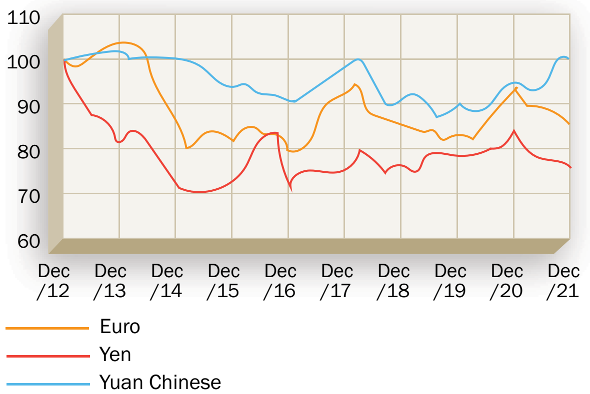
Equity Markets in USD – 2012 = 100



Source: Google Finance

Chart **1.25**

Currencies vs USD – 2012 = 100



Source: Google Finance

In short, the Petroleum Fund 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 risk-return profile.

The PF's value and returns trajectory continues to largely depend on the price developments for these global financial assets, measured in USD terms.

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

In a longer time horizon, we do think that the risk of a global stock or bond market correction is now significant, given the current and simultaneous high stock market valuations and the still historically low levels of global bond interest rates, despite the rate rises recorded in 2021. The trends evidenced in 2021 have further reinforced this historical overvaluation of securities in both investment markets, particularly for equity markets.

In this regard, it should be noted that the top US stock market index, the S&P 500, after its renewed ascent in 2021, reached a new peak price level that corresponds to more than three times its level of December 2009 and today registers historically record valuations, visible for example in its extraordinary ratio of price to companies historical earnings.

However, the long investment horizon of the Fund and its institutional framework should allow us to deal with the markets' short-term swings in a rational way and even to benefit from the occasional episodes of price declines across markets, by a rigorous implementation of the Fund's investment discipline and targeted asset allocation.

On the contrary, the absence of significant future oil revenues from ongoing exploration projects, together with the continued maintenance of a level of public expenditure that results in an active reduction of the Fund's capital, today represent significant risks to this strategy's success and respective temporal investment horizon. These risks, if not mitigated adequately over the coming years, should require a due reassessment of respective PF's objectives to ensure consistency and coordination with its investment strategy implementation.

Economy Domestic – Recent Developments and Projections

Chapter 2

This chapter describes major developments in Timor Leste's non-oil economy in 2021 and relevant perspectives for 2022 and 2023, also discussing important changes regarding the public, financial and external sectors.

As is further detailed below, the main national economic developments in 2021 were:

- Timor-Leste's economy activity recovered in 2021, but only offset part of the steep tumble recorded in 2020, when GDP fell -8.6%. The recovery in economic growth in 2021 to 2.9% is mainly due to the stabilizing effect of a significant increase in public expenditure throughout the year, amounting to $306 million (+27%) and the expected recovery in private demand. However, despite the substantial increase in public spending, our forecasts also consider the negative impacts arising from the extension of the pandemic mitigation measures, the massive floods of April of 2021 and their respective damages, as well as the increase in inflationary pressures and the reduction in consumers' purchasing power.

- For 2022, BCTL expects the economic recovery to continue and strengthen, projecting that economic growth will accelerate to 5.8%. This expectation is based, above all, on the continued growth of public demand in the coming year (+10.4%) and on the acceleration of private demand growth (+2%), while higher net imports (+6.5 %) will once again offset part of the recovery in domestic demand. Unlike 2021, we expect public investment (+75%) to be the main driver of public demand growth in 2022.

- In terms of fiscal policy, 2021 was marked by a significant surge in public spending (+$306 million) and the public deficit, which was practically due to the increase in current expenditure (+$326 million), in line with higher budgeted spending. We also highlight the continued fall in public investment in 2021 (-$20 million), mostly due to weak budgetary execution rates. For 2022, BCTL expects a further increase in spending and a wider public budget deficit, mostly explained by the recovery of the capacity to execute the budgeted investments in infrastructure and buildings, expecting that budgetary policy will continue to be broadly supportive of the economic recovery from the 2020 pandemic crisis.

- In line with global trends, there was a notable increase in domestic inflationary pressures in 2021, with the average annual inflation rate standing at 3.8%, above the 0.5% and 0.9% of 2020 and 2019, respectively. The rise in inflation was mainly due to the worsening of external inflationary pressures, explained by the strength of the recovery in world demand and the persistence of global production and logistical constraints in 2021. The BCTL further anticipates an acceleration of inflationary pressures over the first few months of 2022, followed by a gradual slowdown throughout 2022 and 2023. Specifically, we expect average inflation rate in 2022 to remain at levels similar to those of 2021, above 3%, but then converge down to 2% in 2023.

- Timor-Leste continued to record an external current account deficit, which increased again in 2021, mostly due to the rise in goods and services imports. Although oil revenues have decreased substantially over the last years, they continue to be a relevant factor to mitigate the vast trade deficit's impact on the current account balance.

- Notwithstanding the challenging macroeconomic context, the financial sector continued to remain robust and highly dynamic, recording continued growth of its activity, assets and funds. It is illustrative to note that bank credit continued to grow in 2021, as well as deposits and funds raised by banks operating in the country.

- In 2021, the BCTL continued to implement several relevant initiatives regarding national economic monitoring and the pandemic crisis and 2021's mass-floods impact mitigation. The most relevant initiatives in this context were the continued implementation of the credit moratorium and loan subsidization program for households and companies and the undertaking of household and informal businesses surveys, with the objective of evaluating financial inclusion trends and assessing socioeconomic conditions.

2.1 Economic Activity and Inflation

2.1.1. Recent Economic Developments and Perspectives

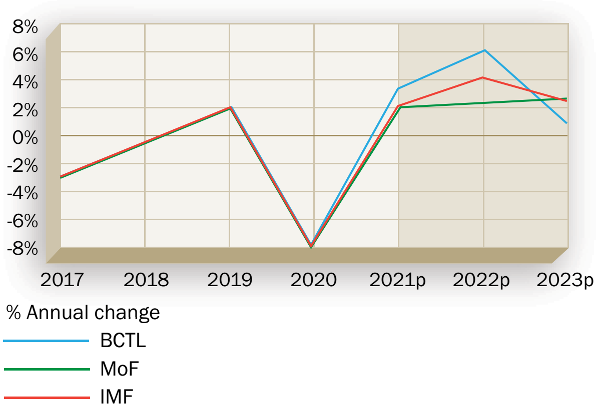
According to BCTL projections – at the time of this report, the official national accounts data was only available until 2020 – the domestic economy should have recorded an economic recovery in 2021, but managed to recover only a part of the steep 2020's GDP recession (-8.6% fall in GDP).

In 2021, the domestic GDP rose 2.9%, but only managed to offset part of the abrupt drop in 2020's GDP.

Economic growth in 2021 (+2.9%) should be mainly due to the stabilizing effect of a significant annual increase in public expenditure, amounting to $306 million (+27%) and an expected recovery in private demand. However, despite the substantial increase in public spending, our forecasts also consider the negative impacts arising from the extension of the pandemic mitigation measures, the massive floods of April 2021 and their respective damages, as well as the increase in inflationary pressures and the reduction in consumers' purchasing power.

Chart 2.1a

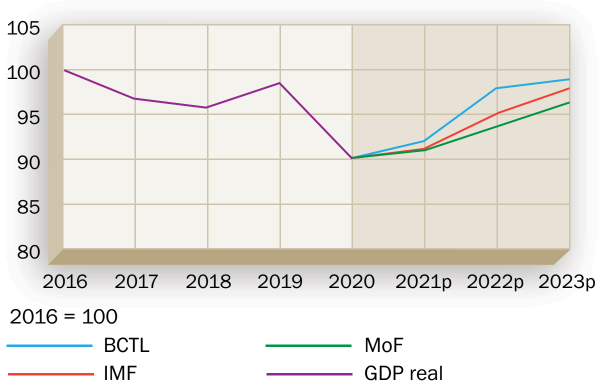
GDP Real Growth



Source: BCTL, 2022 OGE Proposal and IMF

Chart 2.1b

GDP Real



Source: BCTL, 2022 OGE Proposal and IMF

The resumption of growth in 2021 was due to the expansion of public demand and, to a lesser extent, to the recovery of private demand.

As already mentioned, the recovery in growth in 2021 was mainly due to the expansion of public demand - which is expected to have risen 2.7%, in real terms, in 2021 - and of private demand, which should have increased by 1.8% in the year. However, as has been normal in the past, the domestic demand expansion led to an increase in net imports, which grew 2.8%, thus cancelling part of the effect of the recovery in domestic demand.

At a more disaggregated level, the recovery in public demand in 2021 was mainly due to the increase in public consumption (+8.2%) – led by the increase in public expenditure on wages and on goods and services – as public investment continued to decline in 2021 (-15.7%), due to the extraordinary reduction in the capacity to execute the capital expenditure budget in 2021, as described below in the section regarding the State budget. This rise thus recovers only part of the drop in public demand seen in 2020 (-11.4%) due to the abrupt drop in public investment in that year (-50%) – explained by the pandemic and the substantial delay in the approval of the 2020's budget - which had been mitigated by the expansion of public consumption (+6.2%).

In terms of the recovery in private demand in 2021 (+1.8%), we estimate that the recovery is due to the recovery of household investment in housing (+35%) and corporate investment (+21%) and, to a lesser extent, to the slight recovery in household consumption (+0.5%). It is therefore important to note that our projected recovery of private investment in 2021 is mainly due to the efforts and expenses in the rebuilding of infrastructure and houses destroyed in the April floods, which is easily observable in the expressive increase in the imports of construction materials (+89%) and industrial inputs (+16%) in 2021. In terms of private consumption, we highlight that some indicators suggest a recovery throughout the year, but that the increase in inflationary pressures in 2021, together with the extension of pandemic restrictions, should have limited the recovery in households' consumption to 0.5% in 2021. The pickup in private demand in 2021 thus only managed to reverse part of the fall recorded in 2020 (-3.3%) due to pandemic situation, which led to extraordinary decreases in private consumption (-2.4%), households' investment (-4.6%) and private companies' investment (-25%), in that year.

BCTL expects the recovery to continue and to strengthen in 2022, projecting that the GDP will grow 5.8% in the coming year.

The BCTL further expects the economic recovery to continue and strengthen in 2022, projecting that GDP growth will accelerate to 5.8% in 2022. This expectation is based, above all, on the continued growth of public demand in the coming year (+10.4%) and on the strengthening of private demand growth (+2%), while the expected expansion in net imports (+6.5%) will once again subtract from the recovery in domestic demand of GDP.

Unlike 2021, we expect public investment (+75%) to be the main driver of public demand growth in 2022, despite our conservative expectation regarding the ability to execute the public capital expenditure budget next year. On the contrary, also based on the already approved Budget for 2022, we estimate that public consumption will register a slight decrease (-0.5%) in 2022.

In terms of private demand, household consumption growth is expected to accelerate to 2% in real terms in 2022. Additionally, we project that private investment will only rise 3% in 2022, as we believe that the extraordinary rise in private investment in 2021 will not be repeated in 2022.

In short, our optimistic projections for economic growth in 2022 are mainly due to the maintenance of a high level of public expenditure, an increase in the capacity to execute public investment and the continued recovery of private demand in our economy. Due to this trajectory, BCTL expects real GDP to reach at the end of 2022 its pre-pandemic 2019 level.

BCTL's economic growth prospects for 2021 are practically in line with those from the Ministry of Finance (1.6%). However, for 2022, our projections are more optimistic than Ministry of Finance's estimates, which only anticipates growth of 2.1% for next year. This may be due to the fact that the budget approved for 2022 is substantially higher than its initial proposal presented to the National Parliament.

For 2023, assuming that public expenditure level will be similar to 2022 and despite the projection's elevated uncertainty, we estimate a renewed slowdown in economic growth to 1%, since the continued recovery of private demand will not be able to offset the stagnation of public demand expansion in that year.

Beyond 2022, taking into account the growing public budgetary restrictions, we expect a further deceleration of economic growth, due to the need to contain the expansion of public expenditure.

Finally, it should be noted that this projection scenario for 2022 and 2023, similarly to what happened between 2017 and 2020, once again confirms the uninterrupted and excessive dependence of the domestic economy on public spending policies and programs, while the effective start of a developmental and investment process led by the private and productive sectors continues to be postponed.

We thus renew our emphasis on the need to effectively promote and quick-start growth across national productive sectors. This continues to be particularly necessary and important to meet the growing challenges in terms

of job creation for our young population and prepare the country for the coming need to implement a reduction in the level of spending and public investment, in view of the substantial reduction in future oil revenues and accumulated returns in the Petroleum Fund's capital.

2.1.2. GDP Developments – Spending and Production Components

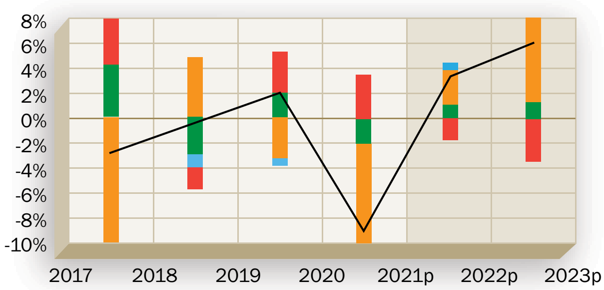
Although official estimates of Timor-Leste's national accounts only exist until 2020, BCTL has developed an internal model that allows it to estimate the trajectory of the most relevant components of domestic and external demand for more up-to-date periods. In this sense, the analysis that follows is based on official data up to 2020 and on BCTL estimates for 2021, seeking to assess the most relevant medium-term trends for our domestic economy.

Public demand will continue to be a relevant driver of domestic economic performance in 2022.

In terms of expenditure's macroeconomic aggregates, as already mentioned and according to the charts that follow, we again emphasize that the 2021 and 2022's economic recovery is mainly due to the significant increase in public demand, due to the material increase in public expenditure in these 2 years. The relevance of public demand for the trajectory of our economy has been, in fact, one of the main trends of our economy in the last decade.

Chart **2.2a**

GDP real growth - Spending Aggregates



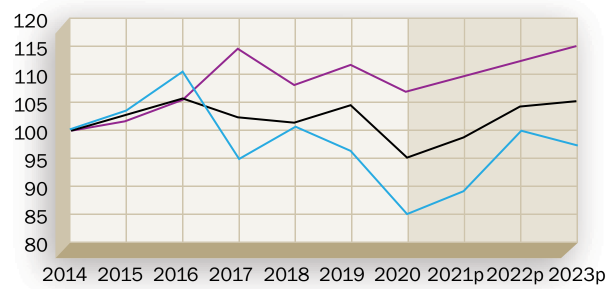
% annual changes and contributions

Net Exports
Public Partners
Public sectors
Private sectors
GDP

Source: DGE and BCTL

Chart **2.2b**

GDP real levels - Main Components



2014 = 100

Private demand
PIB
Public demand

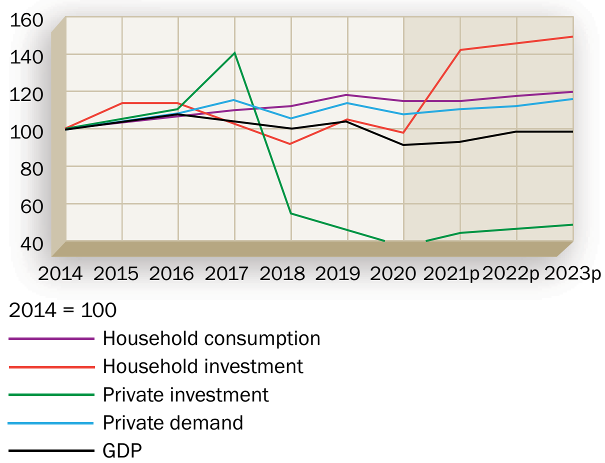
Source: DGE and BCTL

In the chart depicting the trajectories of real GDP and private and public demand since 2014, we can see that the downward trend in the level of activity (GDP) recorded from 2016 to 2020 was mainly due to the gradual reduction in public demand, while the increase in public expenditure between 2020 and 2022 drove the resumption of GDP growth after 2020. It should also be noted that private demand has registered moderate growth since 2016, but which was not enough to offset the impact of the fall in public expenditure on the GDP's downward trajectory.

In the graphs below, we present the evolution of the private and public demand subcomponents, compared to the GDP trajectory since 2014.

Chart **2.2c**

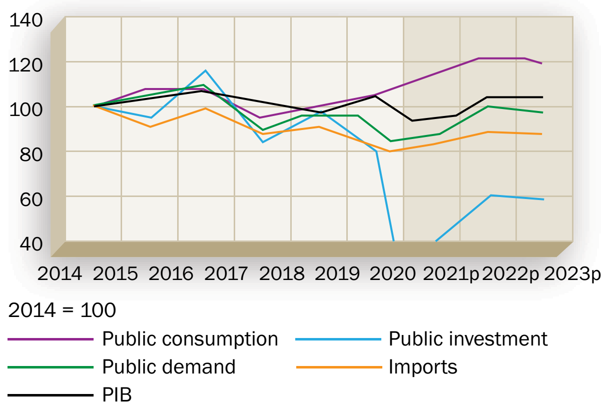
GDP real levels and Private Demand



Source: DGE and BCTL

Chart **2.2d**

GDP real levels, Public Demand and Imports



Source: DGE and BCTL

In terms of private demand, it should be noted that it has been more robust than GDP since 2016, supported by the continuous growth of households' private consumption. Private company investment was the worst-performing sub-component of private demand between 2017 and 2020, having dropped below 40% of its 2014's real level. This sharp drop in business investment, evident from 2018 onwards, represents a very negative development for our economy, since it translates into a disinvestment in equipment and capital goods necessary to increase the economy's productivity and reflects the anaemic performance of the national private sector.

Despite the sustained growth of private demand in recent years, we also highlight the negative impacts arising from the drop in corporate investment in the same period.

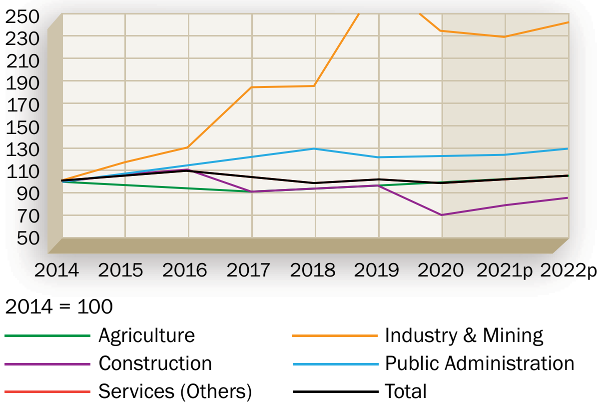
With regard to public demand, it should be noted that it has underperformed GDP since 2016, mainly due to the drop in public investment recorded since that date. It is also interesting to point out that the substantial drop in public investment until 2021 has been accompanied by a significant reduction in private investment in the same period, which once again demonstrates the importance of public expenditure on capital goods for the investment of private companies in our economy.

The construction, public administration and services sectors should be those that most contribute to the economic recovery in2021 and 2022.

In terms of the trajectory of the economy's productive structure, as shown in the following charts, the remarkable growth of the industrial and mining sector and, to a lesser extent, of the public administration, which have surpassed the trajectory of GDP since 2016, stands out. On the negative side, due to the aforementioned reduction in private and public investment, the civil construction sector was the one whose activity decreased the most since 2016.

Chart **2.3a**

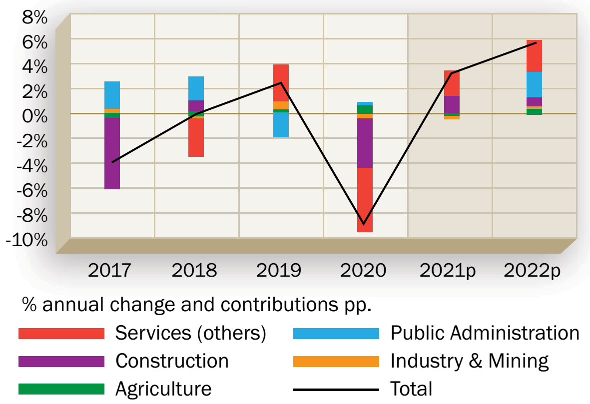
GDP real levels - Production Sectors



Source: DGE and BCTL

Chart **2.3b**

GDP real growth - Production Sectors



Source: DGE and BCTL

In terms of the outlook for 2021 and 2022, we emphasize that the recovery in GDP growth should be more driven, in 2021, by the growth of services and construction and, in 2022, by the growth of these sectors together with public administration's expansion. This trajectory also reflects the upward trend public expenditure in 2021 and 2022, since these sectors are among those that typically benefit the most from the respective budgetary stimulus.

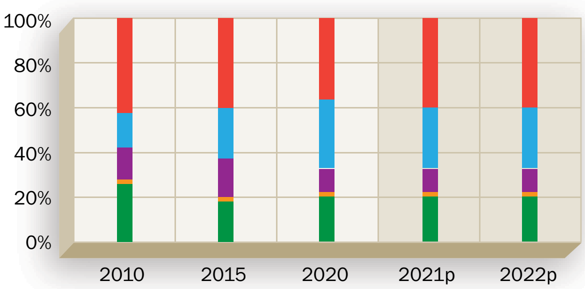
From 2010 to 2020, according to chart 2.3c, the main trend in the production structure consisted of significant drops in the shares of the agricultural/ primary sector (from 25% to 20% of GVA) and civil construction (from 16% to 10%) and the simultaneous increase in the weight of public administration, from 17% in 2010 to 30% in 2020. The services sector continued to maintain its dominant position in the economic structure, representing 38% of GVA in 2020, compared to 42% in 2010.

The services sector has maintained its dominant position in the domestic economy.

With regard to 2021 and 2022, BCTL expects this production structure to remain relatively stable, with the exception of a slight pickup in the importance of the construction sector, due to the expected recovery of private and public investment.

Chart **2.3c**

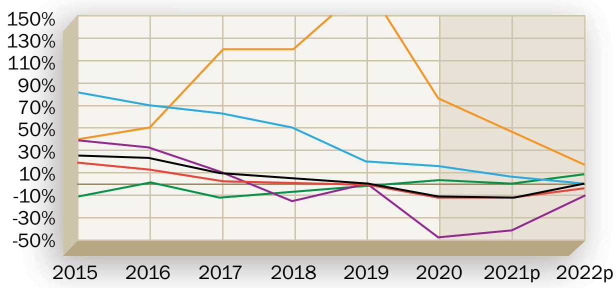
GDP Composition - Production Sectors



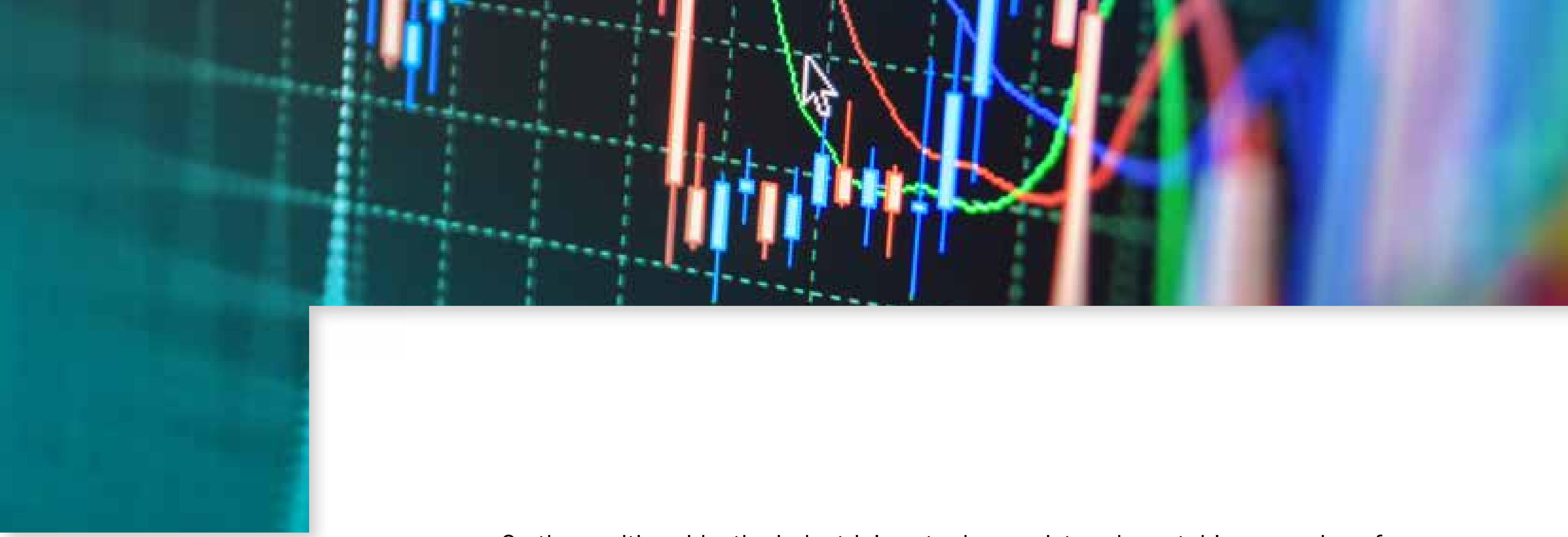
Source: DGE and BCTL

Chart **2.3d**

Sectors 5-Year Cumulative Real Growth Rates %



Source: DGE and BCTL



On the positive side, the industrial sector has registered a notable expansion of its activity, with its GVA growing 136% between 2014 and 2020. Even so, despite this robust expansion, this sector continues to represent a small part of the domestic economic production, amounting only to 2.2% of GDP.

The growth of sectors less dependent on budgetary policies continues to be limited, not yet allowing an effective diversification of our economy.

This productive structure demonstrates that the country's economy continues to largely depend on the public sector, since the sectors less dependent on the public budget - agriculture, fisheries, industry, hotels and restaurants - only represented 24% of GDP in 2020. However, there was a slight improvement in the relative importance of these productive sectors, as in 2015 their combined GVA amounted to 21% of GDP. This trajectory was due to the fact that the accumulated growth of these 3 sectors between 2015 and 2020 (7%) surpassed the accumulated fall in GDP of -7.1% in the same period.

Despite the clear progress of the industrial sector, the anaemic growth of the agricultural and fisheries sector - which is the largest of these sectors and which grew 6% - and the substantial fall in the restaurant/hotel sector of -25% between 2015 and 2020, limited the expansion in activity of the productive sectors less dependent on budgetary policies. Finally, it should be noted that public administration and logistics, more directly dependent on decisions and levels of public expenditure, grew 15% and 11% in the 5 years to 2020.

2.1.3. Prices and Inflation

At the end of 2021, the average inflation rate rose substantially to 3.8%, compared to 0.5% and 0.9% in 2020 and 2019.

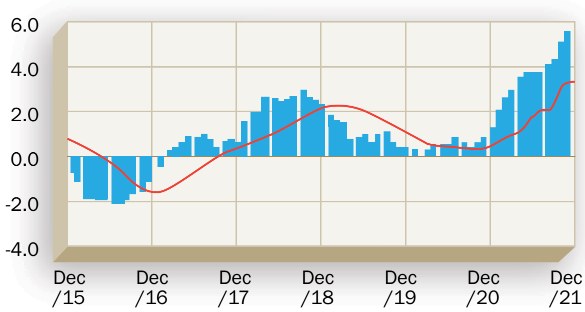
The average annual inflation rate in Timor-Leste, according to the DGE, was 3.8% in 2021, which represented a strong rise compared to the 0.5% and 0.9% recorded in 2020 and 2019, respectively. In year-on-year terms, inflation rate's rise is even more noticeable, having accelerated from 1.2% in December 2020 to 5.3% in December 2021.

As can be seen in the charts and tables that follow, in 2021 inflation rose to the record levels of the last decade. This trend, in line with what has been happening in the various world economies following the economic recovery from the 2020 pandemic, broke away from the relative price stability recorded between 2013 and 2020 in Timor.

We also note that the increase in inflationary pressures in 2021 was mainly due to the surge in food inflation in the CPI basket, as food inflation in 2021 accelerated to 7.3%, compared to 2.2% in 2020. On the other hand, non-food inflation – non-food items represent 46% of the consumption basket – increased to 3.1% in 2021, compared to -0.1% in 2020, which was itself mostly due to increasing alcoholic and tobacco inflation.

Chart **2.4**

TL Inflation Rate



% annual change in prices

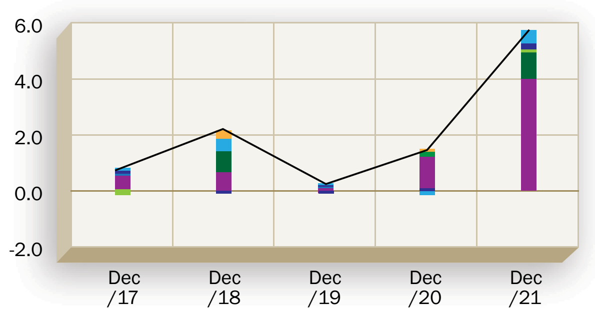
Inflation Annual

Inflation Average

Source: DGE

Chart **2.5**

Contribution to Inflation rate



% annual change and contribution

Education | Recreation | Communication
Transport | Health | Equip. of Housing
Housing | Clothes & Footwear | Alcohol & Tobacco
Food | Total

Source: DGE and BCTL analysis

Table 2.1 provides more detail in terms of inflationary trends, disaggregating annual inflation rates by large groups of goods/services:

Table **2.1**

CPI Basket Sub-Groups Inflation Rates - % annual average

	Dec-17	Dec-18	Dec-19	Dec-20	Dec-21
Food	0.8	1.5	0.2	2.2	7.3
Alcohol & tobacco	-0.3	11.0	0.8	-0.4	10.7
Clothing & Footwear	8.0	-0.1	0.1	2.2	-0.1
Housing	0.7	0.7	-0.2	0.0	1.4
Household equip.	1.7	-0.5	-0.7	-1.0	2.1
Health	0.0	0.0	0.0	0.0	0.7
Transport	-0.5	3.9	0.1	-2.5	6.6
Comunication	-0.9	0.4	-1.1	0.6	0.0
Recreation	-1.1	0.5	0.3	-0.1	1.0
Education	0.0	16.6	9.0	2.6	0.0
Total	**0.6**	**2.1**	**0.3**	**1.2**	**5.3**

Source: DGE and BCTL Analysis

The rise in inflation in 2021 was mainly due to the substantial acceleration in food inflation.

As can be seen, the high contribution of the acceleration of food inflation to the rise in general inflation resulted from both the acceleration of food prices - average of 6% in 2021 and year-on-year of 8.5% in December 2021 - and the elevated importance of food expenditure in the consumers' reference basket, representing 54% of the basket.

Despite the smaller contribution of non-food inflation to the rise in inflationary pressures in 2021, we highlight among these items, the acceleration of alcoholic beverages and tobacco (10.7%) and transport (6.6%) inflation.

We thus note that, despite the worsening of inflationary pressures in our economy in 2021, in line with what happened in most world economies, this trend does not seem to have affected all sectors and expenditure classes, which indicates that inflationary pressures were not yet widespread in our economy in 2021.

In terms of macroeconomic determinants, the rise in inflation in 2021 seems to be mostly due to the worsening of external inflationary pressures and a slight generalized depreciation of the dollar against the currencies of Asian countries, which continue to be our country's main trading partners. As already mentioned in the chapter regarding the international economic background, the worsening of international inflationary pressures was due to the robustness of the global economic recovery, supported by stimulative levels of monetary and budgetary policies, and to the perpetuation of logistical and productive bottlenecks in the world economy in 2021, resulting in a significant increase in the prices of many goods and services traded internationally.

Although the trajectory of aggregate demand and domestic GDP continues to be one of the determinants of the inflation trends in the country, the weakness of the apparent recovery of the national economy should have contributed to anchoring inflationary pressures in 2021. After the substantial fall in GDP in 2020, which compounded the anaemic economic performance recorded since 2016, and notwithstanding the economic recovery expected in 2021, BCTL anticipates that the current level of economic activity remains below its potential level, which has resulted in the underemployment of domestic economic resources and will continue to exert a negative pressure on the general level of prices in our economy.

In terms of future prospects for 2022 and 2023, BCTL anticipates an acceleration of inflationary pressures over the first few months of 2022, followed by a gradual slowdown throughout 2022 and 2023. Specifically, the BCTL expects that the average inflation rate in 2022 will remain close to that of 2021, above 3%, but then to converge down to 2% in 2023.

Inflation projections for 2022 and 2023 stand at 3.3% and 2.2%, which translates into a gradual reduction in inflationary pressures over the next 2 years.

These projections are naturally based on the assumption of exchange rate stability of the dollar against Asian currencies, on the gradual stabilization over the next few years of international inflationary pressures and stable inflation in the economies of our country's main partners and also on the fact that the domestic economy should continue to operate below its potential level.

Despite the expected economic recovery from 2021 to 2023, the anaemic performance of the last 5 years has resulted in the current underemployment of labour and capital resources. The BCTL therefore estimates that the current level of GDP is currently below its potential, or full employment, level. This fact, together with the expectation that the expected economic recovery will not be enough to close the domestic "product gap" by 2023 and that it is difficult to expect a sustained growth in the level of future public expenditure, given the lack of budgetary resources and the rising risks to the sustainability of public finances, leads us to believe that inflationary pressures due to the domestic economy performance, will remain practically non-existent over the next few years.

2.2 Public Finances

2.2.1. 2021 Public Budget Program

Public expenditure increased substantially in 2021 ($306 million), which was explained by the increase in the 2021's Budget, and particularly to much higher current expenditure.

In 2021, according to the data in table 2.2 below, public expenditure, on an effective cash basis, recorded a substantial increase of $306 million, which more than compensated for the -$94 million drop seen in 2020, due to the delay of the respective delay in the approval of the public budget for that year.

Therefore, the overall amount of expenditure incurred amounted to $1,442 million in 2021. The increase in public expenditure compared to 2020 was due to the increase in the 2021 budget, compared to the previous year, as the overall rate of expenditure execution decreased in 2021 to 71%, compared to 76% in 2020. It should be noted, therefore, that the 2021 Budget approved total expenditure amounting to $2,030 million, which translated into an increase of $533 million compared to the $1,497 budgeted for 2020.

The decrease in the overall expenditure execution rate was due to the reduction in the budget execution of public investment, since the current expenditure execution rate increased to 83%, compared to 76% in 2020. On the contrary, the public investment execution rate dropped from 50% in 2020 to an historically low level of 27% in 2021.

Table **2.2**

Public Budget – Allocations, Changes and Execution Rates

	Million of USD			% annual change		Execution rate		
	2019	2020	2021	2020	2021	2019	2020	2021
Total revenues, exc. Loans	**187**	**182**	**161**	**-3%**	**-12%**	**94%**	**111%**	**86%**
Fiscal revenues	123	119	119	-3%	0%	90%	103%	95%
Non-fiscal revenues	56	57	26	0%	-54%	102%	127%	46%
Revenue Retention of agenices	8	7	17	-13%	144%	116%	134%	266%
Total public expenditure	**1,221**	**1,136**	**1,442**	**-7%**	**27%**	**83%**	**76%**	**71%**
Recurrent expenditure	907	975	1,302	8%	33%	88%	76%	83%
Capital expenditure	264	130	125	-51%	-4%	72%	73%	31%
Loans	50	30	15	-40%	-51%	57%	50%	27%
Financing								
RSE	529	544	548	3%	1%	100%	100%	100%
Excess witdrawals from PF	440	420	600	-5%	43%	66%	100%	72%

Source: TL Transparency Portal and BCTL calculations

In annual terms, on a cash basis, the increase in total public expenditure of $306 million was explained by the substantial increase in current expenditure ($326 million), as capital expenditure decreased by -$20 million. The drop in investment and its execution rate are therefore particularly noticeable, given that the 2021 Budget forecast an increase of $256 million in 2021 compared to the previous year.

On the revenues side, the Government foresaw in its 2021 OGE total non-oil revenue of $187 million, excluding loans and grants, but actual revenue amounted only to $161 million, which resulted an overall execution rate of 86%.

This resulted in an annual reduction in revenue of $21 million compared to 2020, mainly due to the drop in non-tax revenues, largely due to the reclassification of EDTL as a public company, which led to its revenues no longer being accounted for as budgetary revenues. In terms of its composition, tax revenues continued to represent the most important category, amounting to $119 million in 2021, having remained practically unchanged compared to 2020. It should also be noted that revenues from autonomous State agencies recorded a notable increase from $10 million to $17 million in 2021.

Due to the substantial increase in public expenditure (+$306) and the simultaneous decline in non-oil revenue (-$21 million), the public sector deficit calculated on a cash basis, excluding oil revenues, increased in 2021 by $327 million, to $1,281 million.

The significant increase in expenditure, together with the decline in non-oil revenue, resulted in a deterioration of the budget deficit, in 2021.

2.2.2. Public Revenue

One of the main priorities of the Government continues to be in reducing the country's dependence in terms of Petroleum Fund's financing. Efforts in this direction remain fundamental in the Government's discussions and budget planning. In its 2021 OGE, for example, the Government continued to highlight its tax reform policy, in order to improve the country's fiscal framework and boost non-oil domestic revenues.

The overall amount of public revenues decreased in 2021, which was due, as mentioned, to the drop in non-tax revenues, due to the reclassification of EDTL as a public company, so its revenues are no longer accounted for as budget revenues.

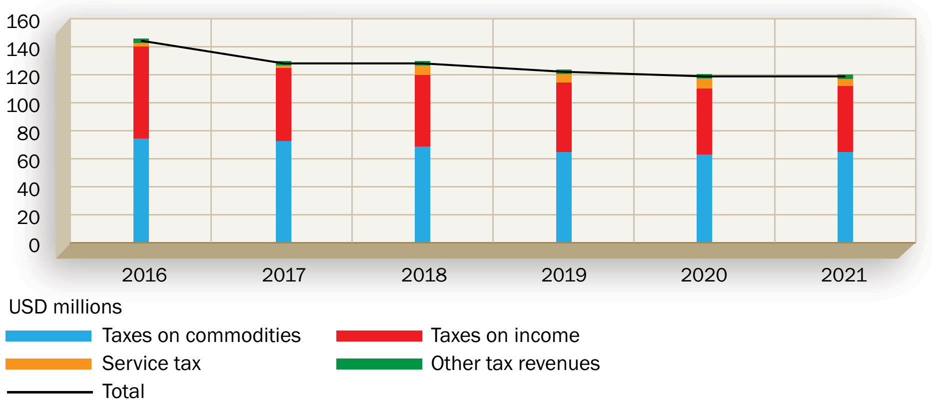
Public non-oil revenue declined -12% in 2021, to $161 million.

In 2021, on a cash basis, domestic non-oil revenues reached $161 million, down -12% from $182 million in the previous year. In terms of its components, tax revenue was broadly unchanged at $119 million, tax revenue decreased -54% to $26 million and autonomous agencies' revenue increased 144% to $17 million.

Chart 2.6 shows the changes in tax revenues and its main components over the last few years, namely, taxes levied on the income of individuals and companies and taxes levied on the import of goods. Despite the stability of overall tax revenues in 2021, it should be noted that the slight decrease in income taxes (-$2 million) to $47 million was fully offset by the increase in revenue obtained from taxes on imports (+$1 million, to $65 million) and on services (+$1 million, to $5 million).

Chart **2.6**

Fiscal Revenue - cash basis



Source: TL Transparency Portal and BCTL calculations

2.2.3. Public Expenditure

The overall public expenditure execution rate dropped again in 2021 to 71%, prolonging the execution rate's decline in 2020 (76%) and 2019 (83%), which thus remained well below the 91% and 88% recorded in 2018 and 2017.

Although the expenditure budgeted for 2021 was substantially higher than that for 2020 (+$533 million), the renewed reduction in the overall rate of execution ended up limiting the annual increase to $306 million, on a cash basis. This resulted in an annual 27% increase in effective public expenditure, more than offsetting the drop of -$94 million (-8%) recorded in 2020.

Public expenditure increased 27% to $1,442 million, as a result of the substantial increase in the expenditure on public transfers, goods and services, and wages.

As mentioned above, the increase in global expenditure was explained by the substantial increase in current expenditure, valued at $326 million, as capital expenditure declined by -$20 million in 2020. We also note that the reduction in public investment was exclusively due to the weak capacity to execute the investment programs, as the investment budgeted for 2021 would have resulted in an annual increase of $251 million. This rising trend in terms of current expenditure importance, to the detriment of capital expenditure, reinforced the trajectory already observed in 2020 and 2019.

2.2.3.1. Current Expenditure

In 2021, current expenditure increased 33%, adding to the rises already recorded in 2020 (+7%) and 2019 (+14%), which as a whole reversed the decline observed in 2017 and 2018. This type of expenditure, which amounted to $1,302 million in 2021, it is now at its highest level in historical terms, already well above the maximum values seen in 2015 and 2016, of $1,030 million.

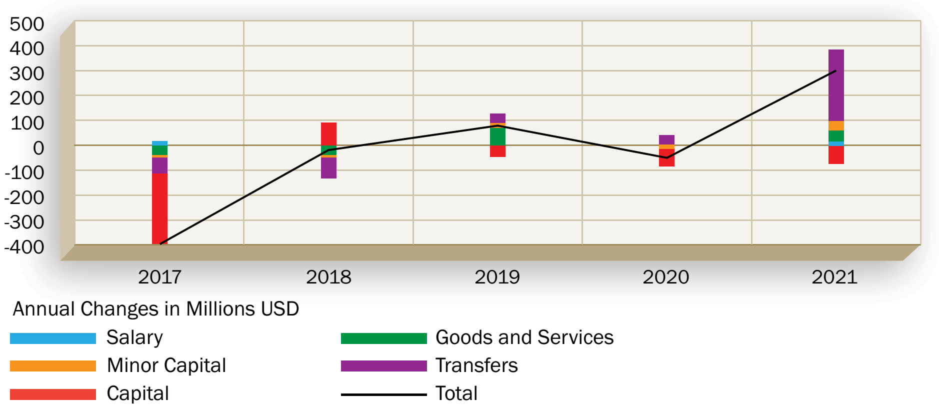
The significant surge in current public expenditure practically explained the increase in global public expenditure in 2021.

Current expenditure thus continued to be the main component of public spending, amounting to 90% of the total, which represented a continued rise compared to the 86% in 2020 and the 74% and 71% recorded in 2019 and 2018. It should be noted that the increase in current expenditure was due to the increase in budgeted amounts (+$289 million), but also to the increase in the rate of execution of this type of expenditure, which rose from 76% in 2020 to 83% in 2021.

Chart 2.7 presents the annual changes in the components of public expenditure for the last years, determined on an effective cash basis. As can be seen, in 2021 the increase in expenditure on transfers (+$273 million), on goods and services (+$37 million) and on salaries (+$25 million) explained the significant increase in current and total expenditure, taking into account the decrease in public investment of -$20 million.

Chart **2.7**

Public Expenditure Changes by Category - cash basis



Source: TL Transparency Portal and BCTL calculations

Due to these changes, expenditure on transfers represented in 2021 the largest category of total expenditure, with 46% of the total (34% and 27% in 2020 and 2019), followed by expenditure on goods and services with 29% (33% and 30% in 2020 and 2019) and public wages with 16% (18% and 16% in previous years).

2.2.3.2. Development Capital Expenditure

The Government budgeted for 2021 an overall capital expenditure, including the loans program, a total of $464 million, which represented a substantial increase of $244 million (+111%) compared to the $220 million allocated in 2020. This budget thus sought to offset the budgeted decrease in 2020 (-$218 million) and provide more budgetary support to the domestic economy.

Expenditure on capital goods was budgeted at $464 million, of which only $140 million was executed.

However, taking into account the poor execution capacity in terms of public investment in 2021, with the execution rate falling to 30%, from 73% in 2020, the effective value of public investment ended up falling - $20 million, to $140 million in 2021.

Despite the stated decrease in the execution rate, it should be noted that the 2020 execution rate of 73% resulted mainly from the late approval of the 2020 OGE, which meant that the budgeted amount was intentionally reduced and partially postponed to 2021, as it was impossible to properly execute a higher budget just in the last quarter of 2020. In this context, we consider that the execution of the public investment program continued to face substantial restraints in 2021, similar to those of 2020.

Table **2.3**

Public Investment Programs

	millions of USD			% annual Change		% Total	
	2019	2020	2021	2020	2021	2020	2021
Minor Capital	27	5	44	-81%	732%	3%	32%
Loans	50	30	15	-40%	-51%	19%	11%
Infrastructure Funds	225	108	58	-52%	-46%	67%	41%
Public Inv. ecl.Infr.Funds	12	17	23	44%	36%	11%	17%
Total	**314**	**160**	**140**	**-49%**	**-13%**	**100%**	**100%**

Source: TL Transparency Portal and BCTL calculations

The majority of capital and development expenditure was spent under the infrastructures program, including loans, whose weight amounted to 52%, whose weight fell versus the 86% in 2020. The Infrastructure Fund Program continues to assume the greatest relevance in terms of public investment, as its expenditure corresponds to 41% of the total for the category in 2021.

Investment in roads, including the loans program, continues to represent the top priority for public investment.

Table 2.4 further details information regarding the main components of the national public investments programme, identifying the highest priorities in terms of its infrastructure programmes.

Table **2.4**

Public Investment Composition

	Million of USD			% of Public Investment		
	2019	2020	2021	2019	2020	2021
Minor capital	27	5	44	9%	3%	32%
Buildings	1	2	4	0%	1%	3%
Total Infrastructures	286	153	91	91%	96%	65%
Public investment	**314**	**160**	**140**	**100%**	**100%**	**100%**

10 main investments in infrastructures

	Million of USD			% of Public Investment		
	2019	2020	2021	2019	2020	2021
Roads	232	118	60	74%	74%	43%
Institutional development	9	12	9	3%	7%	6%
ZEESM	0	0	5	0%	0%	4%
Planning	5	3	4	2%	2%	3%
COVID	0	1	3	0%	0%	2%
PDIM	3	5	2	1%	3%	2%
Health	0	0	2	0%	0%	1%
Agriculture	1	1	2	0%	1%	1%
Education	1	0	2	0%	0%	1%
Defense and security	3	1	1	1%	1%	1%
Other Infrastructures	32	12	3	10%	7%	2%
Total infrastructures	**286**	**153**	**91**	**91%**	**96%**	**65%**

Source: TL Transparency Portal and BCTL calculations

As can be seen, investment in minor capital – capital goods – increased considerably in 2021 to $44 million, which translated into an increase in its importance to 32%, compared to 3% in 2020. This substantial increase thus cancelled part of the substantial drop in investment in infrastructure (-$62 million), and was reinforced by the pick-up in buildings investment amounting to $2 million.

In terms of sector priorities for public investment in infrastructure, investment in roads and bridges continued to be the main programme, with an annual expenditure of $60 million in 2021. However, the relative weight of this priority in overall public investment declined to 43% of the total, compared to 74% in 2020 and 2019.

In terms of the remaining items, investment in institutional development, ZEESM, infrastructure planning and design, investment in infrastructure necessary to implement the Covid mitigation program and PDIM represented the most relevant investment categories, in addition to roads and bridges.

2.2.4. Public Funding Sources

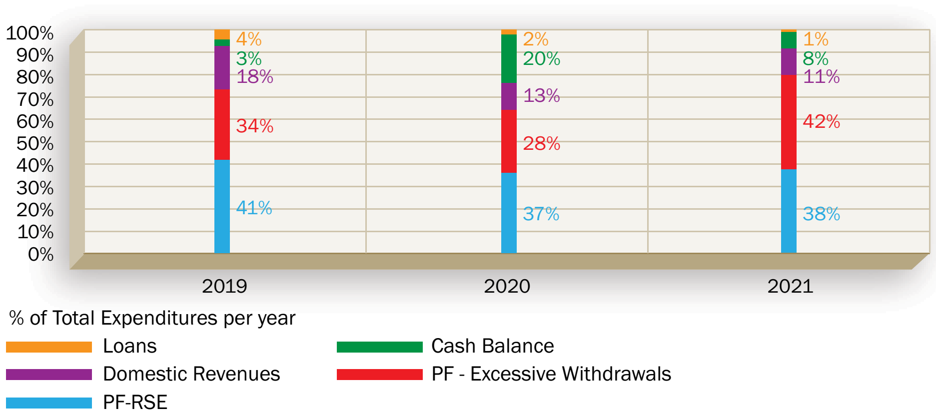
In its 2021 Budget, the Government planned to use $1,378 million from the Petroleum Fund, having withdrawn from the PF only $1,148 million to finance its actual expenditure throughout the year. It should be noted that this figure represents an increase from the $964 million used in 2020, due to higher public spending and the higher non-oil fiscal deficit.

The State continued to make withdrawals from the Petroleum Fund well above its 2021's ESI, which resulted in a further reduction in the Fund's capital.

With this continued use of funds, the annual value withdrawn from the PF continues to be well above its estimated sustainable income (ESI), valued at $548 million ($544 million in 2020 and $529 million in 2019), which translates into a direct and continued reduction of the Fund's capital.

Chart **2.8**

Source of public expenditure Funding



Source: TL Transparency Portal and BCTL calculations

Non-oil public revenues financed only 11% of public expenditure in 2021, compared to 13% in 2020.

In terms of funding sources available to finance public expenditure, PF distributions continue to be the main source of funds, financing 80% of expenditure incurred in 2021. It should be noted that the increase in this ratio compared to 65% of the previous year is due to the existence of a higher Treasury cash balance in 2020, which had been accumulated during the duodecimal regime in 2020. Domestic non-oil public revenues financed, in turn, 11% of total expenditure in 2021, when in 2020 and 2019 they had financed 13% and 18%, respectively. This decrease is naturally due to the increase in public expenditure, as non-oil revenues recorded only a small fall in 2021.

Loans importance has remained low in terms of expenditure financing in recent years, having financed 1% of the total in 2021, compared to 2% and 4% in previous years. These loans, which have mainly served to finance investment in roads in the country, amounted to $15 million in 2021 ($30 million and $87 million in 2020 and 2019), which corresponded to an execution rate of only 27% of the respective budget. Thus, the capacity to execute the loans program fell in 2021, since in 2020 and 2019 50% and 57% of the respective budget had been implemented.

The continued reduction in PF's capital further increases the risks to public finances' medium-term sustainability.

In short, these considerations allow us to confirm the continued and immense dependence of state budgets from oil revenues or, more specifically, transfers originating from the Petroleum Fund, aggravated by the fact that the respective annual outflows have substantially exceeded the Fund's sustainable income.

Despite the existence of substantial oil and gas reserves in Timor-Leste's territory, the fact that ongoing exploration projects are expected to be terminated by 2023, makes the continued and considerable reduction of the Fund's capital a material risk to our Public Finances' medium-term sustainability.

2.3 Monetary and Foreign Exchange Sectors

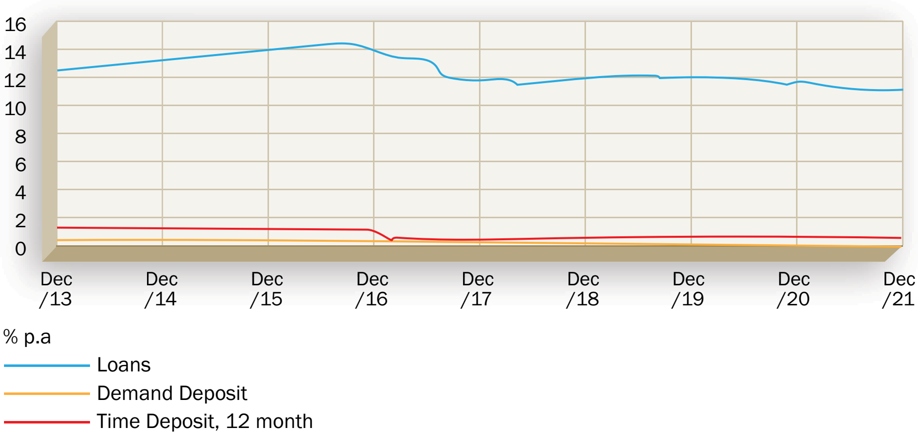
2.3.1. Interest Rates

Average lending interest rates remain relatively high compared to overseas USD benchmark lending rates. Standard economic theory generally states that when a small country adopts the currency of a large economy as its own, interest rates tend to converge to its anchor's rates. In Timor Leste this has not been true, especially for credit interest rates due to several reasons, mostly related to banking business risks in our country, which include local credit risks and the country risk itself.

Credit interest rates continue to be quite high, but fell slightly in 2021, as had been the case in 2020.

Chart 2.9

Key Lending and Deposit Interest Rates



Source: BCTL

As in the previous year, average interest rates on loans to the private sector recorded a renewed decline from 11.28% to 11.03% in 2021, which represents a positive development for companies and families that resort to banking sector financing. However, the average rate paid on 6-month deposits rose slightly in 2021 (+0.03%), to 0.69% at the end of the year. This distinct evolution of lending and deposit rates meant that the banking spread, or the differential between rates, fell again in 2021 to 10.48%, similarly to 2020, contrary to the increases recorded in 2019 and 2018.

Table 2.5

Commercial Banks Interest Rates - Weighted Averages (% year)

Periods		Loand+ 6 month Libor	Demand Deposit	Saving Deposit	Time Deposit			
					1 month	3 month	6 month	12 month
2020	Dec	11.28	0.07	0.46	0.64	0.65	0.66	0.64
2021	Jan	12.74	0.06	0.42	0.63	0.64	0.65	0.61
	Feb	11.14	0.07	0.43	0.64	0.65	0.66	0.61
	Mar	11.16	0.09	0.43	0.64	0.65	0.66	0.61
	Apr	11.14	0.09	0.43	0.63	0.64	0.66	0.62
	May	11.14	0.09	0.43	0.63	0.64	0.68	0.62
	Jun	11.12	0.09	0.46	0.64	0.66	0.69	0.62
	Jul	11.09	0.09	0.45	0.65	0.67	0.69	0.64
	Aug	11.13	0.09	0.44	0.65	0.66	0.69	0.62
	Sep	11.09	0.11	0.45	0.65	0.66	0.68	0.61
	Oct	11.07	0.10	0.44	0.65	0.67	0.71	0.61
	Nov	11.06	0.09	0.47	0.64	0.66	0.70	0.62
	Dec	11.03	0.10	0.48	0.63	0.65	0.69	0.64

Source: BCTL

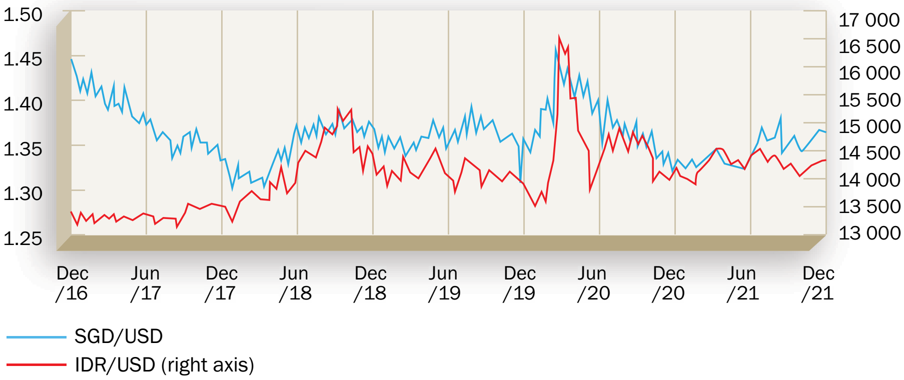
2.3.2. Exchange Rates

The dollar registered a slight and generalized appreciation against our trading partners' currencies in 2021.

The US dollar, Tmor Leste's official currency, recorded a slight and generalized appreciation against the currencies of our main trading partners in 2021. In the year as a whole, the dollar appreciated by 1% against the Indonesian rupiah, our main trading partner, having also appreciated 2% against the Singapore dollar, which is a reference currency in the Asian space. It should also be noted that exchange rate volatility was much lower in 2021, compared to the previous year.

Chart **2.10**

Selected Foreign Exchange Rates versus the USD



Source: Bloomberg

As our country continues to be highly dependent on imports of goods and services to satisfy domestic demand, the slight appreciation of the dollar contributed to contain price pressures for imported products and, in turn, to stabilize domestic inflation.

2.3.3. High-Powered Money, or Monetary Base

Monetary base, or 'high-powered money', which is one of the crucial variables in terms of monetary policy, increased notably $167 million in 2021, thus reinforcing the previous 2020 increase ($22 million). The monetary base was valued at $318 million at the end of 2021, with $26 million corresponding to coin in circulation and the remaining $292 million to bank deposits with the BCTL. The extraordinary expansion of the monetary base in 2021 was largely due to the increase in bank deposits with the BCTL, valued at $164 million.

The Monetary Base increased extraordinarily in 2021, due to the expansion of bank deposits with the BCTL.

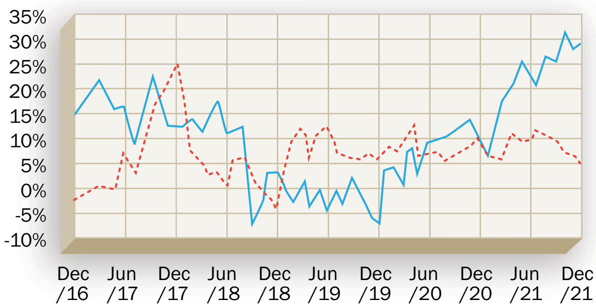
2.3.4. Money Supply

The compilation of monetary and financial statistics fundaments our assessment of relevant developments in our monetary and financial systems.

Financial sector development plays a vital role in facilitating economic growth and poverty reduction. The compilation and analysis of monetary and financial statistics allow us to gauge developments and changes in our monetary and financial systems. BCTL has been collecting and compiling these statistics systematically in order to build a comprehensive and detailed understanding of the financial sector and, in turn, support the development of BCTL's macro prudential and monetary policies frameworks. However, to date, BCTL does not yet have an autonomous monetary policy and respective instruments, as our country continues use a foreign currency, the USD, as its official currency.

Chart 2.11

Money Supply Growth



% annual change

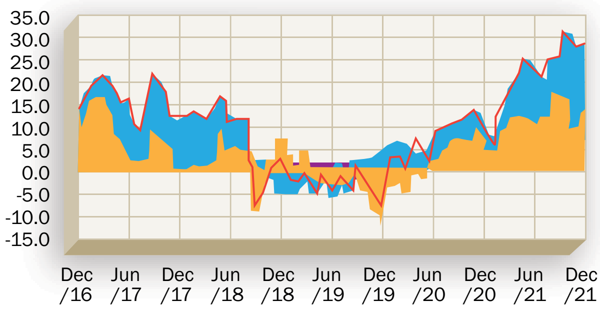
M2

Credit to Private Sector

Source: BCTL

Chart 2.12

M2 and its Components



% annual change & contributions

Other Deposit
Transferable Deposit
Currency in circulation (centavos)
M2

Source: BCTL

Although Timor-Leste is a "dollarized" economy, the BCTL is able to reasonably calculate the money supply aggregate M2.

Although Timor-Leste is a "dollarized" economy, BCTL can still reasonably calculate the aggregate money supply (M2 aggregate), excluding the dollar bills in circulation, which in most countries is used as a measure of the availability of means of payment. As usual, the money supply in Timor Leste is calculated by the sum of coins in circulation, current/checking account deposits - which, like currency, can be mobilized immediately to make payments - and "quasi-currency "(savings and fixed-term deposits), which can also be mobilized relatively quickly to make payments.

Charts 2.11 and 2.12 depict the evolution of the M2 monetary aggregate, over the period from 2017 to 2021. Note again that the M2 figures are approximate because, as the country uses the US dollar, it is difficult to accurately calculate the value of dollar bills in circulation. However, as this value should be a small and stable proportion of funds available for payments, our M2 estimate should serve as a reasonable measure of the size and changes of money supply in our economy.

The M2 aggregate thus calculated amounted to $1,119 million in December 2021, having registered an extraordinary expansion of $250 million compared to 2020, thus reinforcing the increase of $81 million recorded in 2020.

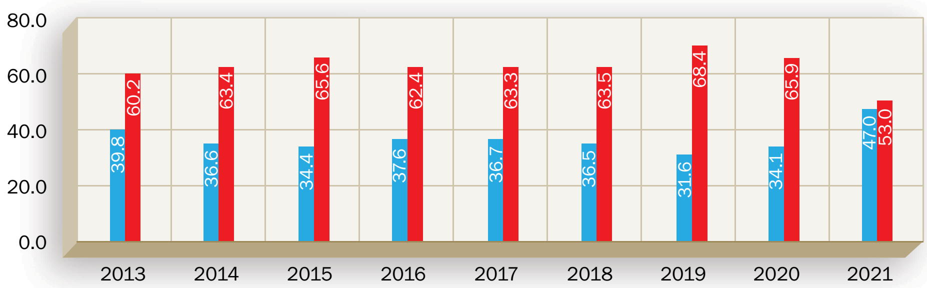
M2 increased in 2021 to $1,119 million, reinforcing the increase recorded in the previous year.

It is also important to assess the evolution of money supply components, shown in graph 2.12. Total deposits received by financial institutions were instrumental in the expansion of the money supply, with an increase of $248 million, reinforcing the increase of $77 million in 2020.

In terms of their ownership by institutional sector, as can be seen in chart 2.13, it can be seen that 53% of deposits are held by individuals and 47% by private companies. These percentages translate into a significant increase in the proportion of corporate deposits in 2021, which resulted in a substantial departure versus the average institutional weights recorded since 2013.

Chart **2.13**

Institutional Deposit Ownership



Source: BCTL

From another M2 components perspective, according to table 2.6 below, the increase in credit and net foreign assets explained the bulk of the increase in the money supply, despite having been curtailed by the increase in public sector deposits.

Table **2.6**

Money Supply Change & Driver

In millions US	Annual Flow 2020	Annual Flow 2021
Crédit to Private Sector	26.7	13.3
Government	-34.5	-78.3
Claims on Central Government	0.0	0.7
Deposit	34.5	79.0
Net Foreign Assets	31.6	388.9
Other net Assets	-56.8	74.3
M2	**80.7**	**249.6**

Source: BCTL

2.3.5. Bank Credit

In 2021, credit granted by banks to the private sector recorded a further increase of $14.8 million, or 5.8%, but which was less expressive than the increase of $26 million observed in the previous year.

Bank credit increased again in 2021 to $272 million.

Table 2.7

Bank Credit Composition

	Outstanding (million USD)		Growth		Composition in %	
	Dec-20	Dec-21	Nominal	%	Dec-20	Dec-21
Agriculture, Water & Forestry	1.3	1.9	0.6	47	0.5	0.7
Industry & Manufacturing	11.0	16.2	5.2	47	4.3	6.0
Constructions	36.1	32.6	(3.5)	-10	14	12
Transport & Communications	1.4	2.7	1.3	88	0.6	1.0
Trade & Finances	35.4	32.5	(2.9)	-8	14	12
Tourism & Service	6.5	3.3	(3.1)	-48	2.5	1.2
Individuals & Others	165.3	182.7	17.4	11	64	67
Total	**257.1**	**271.9**	**14.82**	**5.8**	**100**	**100**

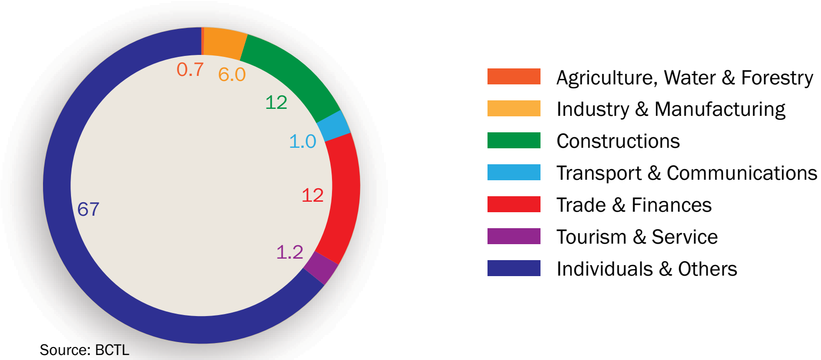
Source: Comercial Banks and BCTL analysis.

Even so, the previous table shows that credit granted to companies decreased again -$2.5 million in 2021, after having contracted -$14 million and -$24 million, in 2020 and 2019. Actually, the steady and substantial fall in corporate credit since 2017 has been one of the defining trends in the financial sector.

It is interesting to note that the robust increase in loans to individuals in 2021, 2020 and 2019, of $17, $40 and $37 million, more than compensated for the decline in corporate credit in recent years, having been solely responsible for the growth in global bank credit. As a result of this continued rise, loans to individuals were, at the end of 2021, the most important segment of bank loans as a whole, amounting to 67% of the total.

Chart **2.14**

Sector Credit - Dec 2021 - % Total



Source: BCTL

In terms of business sectors, as in 2020, there was a negative change in credit granted to some sectors of activity, particularly civil construction and services and tourism. However, on the positive side, the increase in credit to the primary sector (agriculture and fisheries) and to the industrial sector in 2021 stood out. Despite the growth in credit granted to these 2 productive sectors, the combined value of their loans remains low, amounting to just $18 million at the end of the year.

Loans to individuals constitute the most important part of bank credit, with 67% of the total.

Credit granted to individuals reinforced its first position in terms of credit composition, with a weight of 67%, compared to 64%, 54% and 41% in the previous 3 years. In the context of corporate credit, civil construction (12%) and the distribution and commerce sector (12%) continue to be the most important. The agriculture and industry sectors, two important sectors for the country's economic development, represent only 0.7% and 6% of total loans granted.

In addition to the "quantity" of loans, it is also important to analyse their "quality", which can be done based on indicators such as the amount of "bad debts" and the provisions of the system for credit risks. We thus note that the value of provisions for credit risks continued to remain at very low historical levels ($7.6 million), despite having risen from the $5.8 million at the end of 2020.

It should also be noted that banking institutions remain quite robust in terms of their ability to deal with a possible deterioration in credit quality, given that current levels of non-performing loans are very low and that the sector's operating profitability margins offer a robust basis for financing such an eventuality.

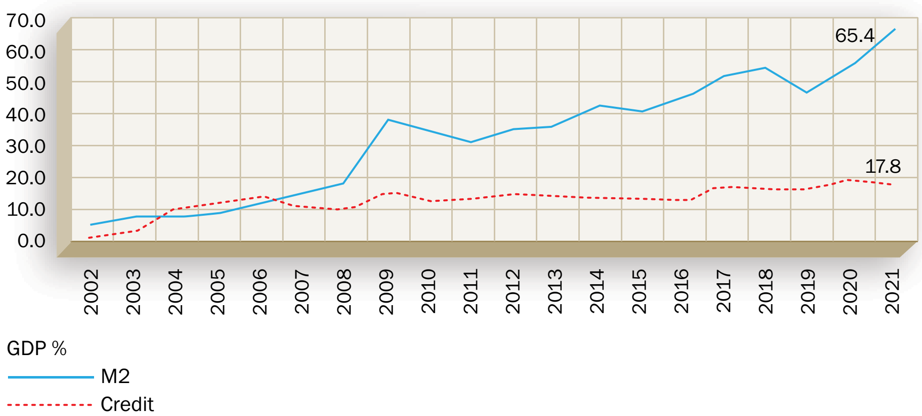
Despite the improvement in the quality of the balance sheet of financial institutions, overall bank credit has remained at levels much lower than that of deposits, providing commercial banks with excess liquidity that tends to be invested preferentially on bank deposits abroad.

2.3.6. Financial Depth Indicators

The degree of financial depth, also known as the degree of monetization of the economy, can be measured based on the ratio of M2-to-GDP. This ratio rose remarkably in 2021 to 65.4%, prolonging the upward trend seen since 2011. Another indicator that can also be used to monitor the degree of financial depth is the credit-to-GDP ratio. This ratio amounted to 17.8% at the end of 2021, having fallen by 0.4% compared to 18.2% in 2020, thus contradicting the upward trend recorded since 2016.

Chart **2.15**

Monetary Aggregates Versus GDP



Source: DGE and BCTL analysis

2.4 External Sector

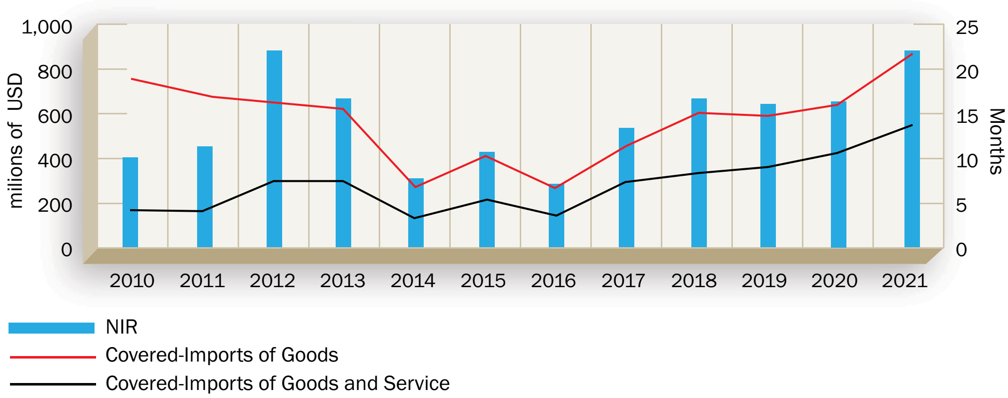
2.4.1. Net International Reserves (NIR)

Net international reserves (NIR) recorded a significant increase in 2021, corresponding to 13 months of coverage of the country's imports.

At the end of 2021, net international reserves (NIR) stood at $890 million, registering a significant increase compared to the average level of the last 3 years ($650 million). Expressed as months of coverage of total imports of goods and services, NIR correspond to 13 months, thus recording a substantial increase versus 10 months in 2020.

Chart 2.16

Net International Reserves



Fonte: DGE e BCTL

2.4.2. Real Effective Exchange Rate Index (REER)

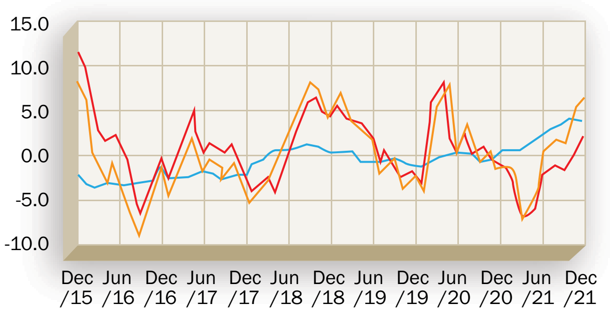
The REER appreciated 6.5% in 2021, contrary to the depreciations observed in 2020 and 2019.

The Real Effective Exchange Rate Index (REER) – an indicator used to assess the competitiveness of countries in terms of tradable products – appreciated 6.5% in 2021, inverting the real year-on-year depreciations of 2020 (-1.3%) and 2019 (-2.2%), as shown in chart 2.17a. It should also be noted that in 2021 the REER registered a notable reduction in its volatility compared to the previous year, which coincided with the most acute phase of the global pandemic crisis.

This development was mainly due to the contribution of the nominal appreciation of the dollar against the currencies of our trading partners, which is observable in the appreciation of the Nominal Effective Exchange Rate Index (NEER). The NEER recorded an annual appreciation of 2.9% in 2021, reversing the depreciations of -1.7% and -1.5%, recorded in 2020 and 2019.

Chart **2.17a**

REER Index

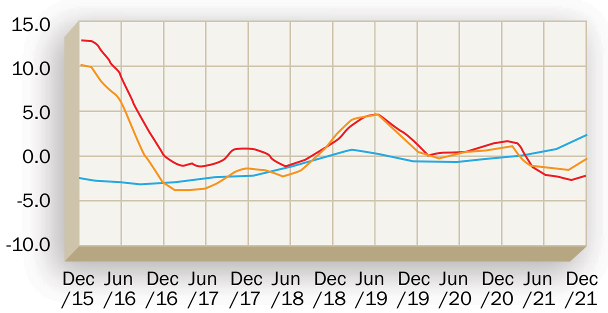


% annual change
CPI Index
NEER
REER

Source: Bloomberg and BCTL

Chart **2.17b**

REER Average Index



% annual change
CPI Index
NEER
REER

Source: Bloomberg and BCTL

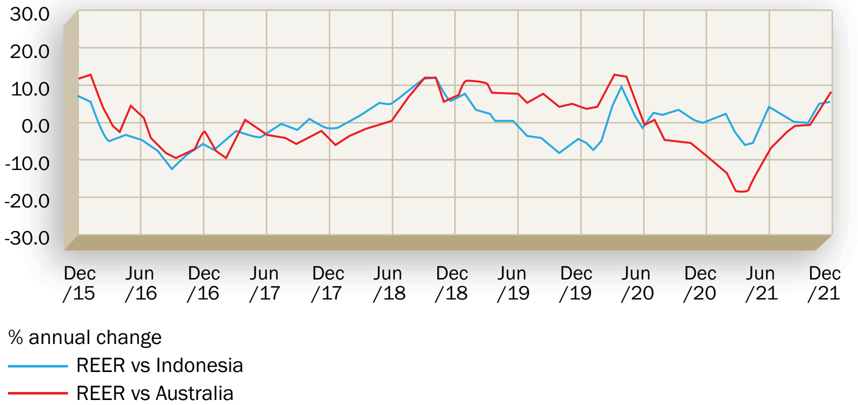
In terms of annual average changes (chart 2.17b), the REER recorded a slight depreciation at the end of the year of 0.1%, thus offsetting the upward trend recorded since 2018. This evolution was thus contrary to the year-on-year REER change in December 2021, which was due to the fact that the REER appreciation took place only in the last quarter of 2021, so that the 2021 REER average was not materially affected by this rise.

In bilateral terms, specifically versus the currencies of Indonesia and Australia, two of the country's main trading partners, the dollar appreciated notably or 5.5% against the rupiah and 8.0% against the Australian dollar. This evolution also followed the global REER trajectory in 2021, with the depreciation of the dollar in the first half of the year being followed by a continuous and intense appreciation in the last quarter.

In bilateral terms, the REER recorded depreciations against the Indonesian rupiah and the Australian dollar.

Chart **2.18**

Selected Real Exchange Rates- Indonesia and Australia



Source: Bloomberg and BCTL

Coffee exports remain the main and practically only trade export of our country. However, international coffee prices continue to be the strongest driver of these exports, as the respective export volumes are only slightly influenced by the changes in these effective exchange rates.

In bilateral terms, it should be noted that prices for goods imported from Indonesia remain much more competitive than those for similar goods from Australia, which is also confirmed by Indonesia's greater importance as a trading partner for our economy.

2.5 Balance of Payments

Timor-Leste's external current account's deficit rose further in 2021 to $248 million, rising $191 million compared to 2020. This deterioration resulted, above all, from the increase in the trade deficit ($151 million) and declining Petroleum Fund's income (PF, -$80 million). On the other hand, external oil revenues – which since the end of 2019 have been registered as goods exports in the trade account – increased $213 million in 2021, which helped to mitigate the rising current account deficit.

The current account deficit rose further in 2021, to $248 million.

The current account deficit corresponded to -15% of domestic non-oil GDP in 2021, thus returning to the average range levels recorded between 2015 and 2018. The combined balance of current and capital accounts, which determines the overall net external financing need for the economy, decreased to a negative value of -14% of GDP, compared to -3% in the previous year.

Table 2.8

Timor-Leste Balance of Payments

	In millions of USD			% GDP	
	2020	2021	% Change	2020	2021
Current Account Exclude Oil Income	**-824**	**-1,229**	**49**	**-52**	**-72**
Current Account	**-57**	**-248**	**333**	**-4**	**-15**
Goods, FOB	136	215	58	9	13
Service	-453	-683	51	-28	-40
Primary Income	297	213	-28	19	13
Secondary Income	-37	6	-117	-2	0
Capital Account	**12**	**13**	**2**	**1**	**1**
Financial Account	**272**	**194**	**-29**	**17**	**11**
Direct Investment	72	66	-8	5	4
Portfolio Investment	244	150	-38	15	9
Other Investment	-45	-23	-49	-3	-1
Errors & Omissions	**-227**	**320**	**-241**	**-14**	**19**
Grand Total	**227**	**-41**	**-118**	**14**	**-2**
Reserve Asserts (Change)	**-0.24**	**-278**	**114,433**	**0**	**-16**

Source: BCTL

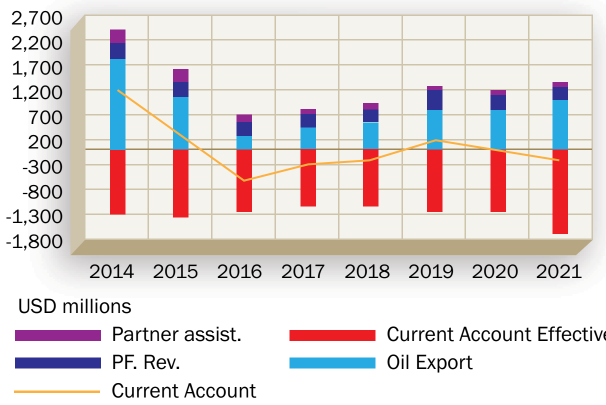
2.5.1. Current Account

Higher goods and services imports and the decrease in PF income were the factors that most contributed to the rise in the current account deficit.

As can be seen in chart 2.19a below, the current account deficit rose further in 2021, which, as mentioned above, was mainly due to higher goods and services imports and the reduction in PF's income.

Chart **2.19a**

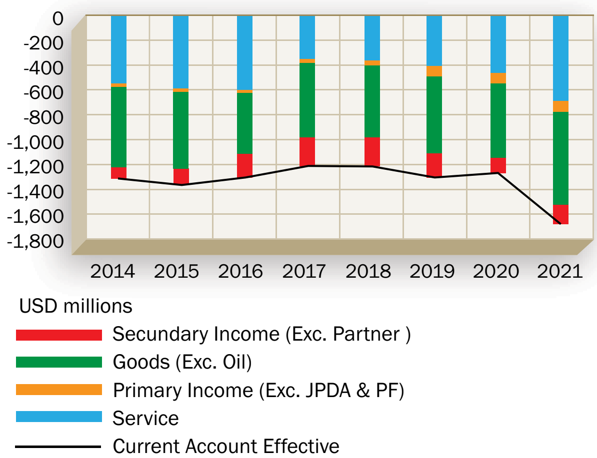
Current Account and Components



Source: BCTL

Chart **2.19b**

Effective Current Account



Source: BCTL

Since Timor-Leste's current account is strongly driven by three factors that are relatively independent of domestic economic developments – oil revenues, PF revenues and international assistance – BCTL considers that the external aggregate that excludes these variables ends up allowing a better assessment of substantive economic trends in terms of our external position.

In this sense, chart 2.19b depicts the evolution of the effective current account balance, which excludes those 3 factors from the global current account balance. Specifically, PF's income is excluded from the primary income account, oil revenues are deducted from the goods trade account (or primary income until 2019) and international assistance is subtracted from the secondary income account.

As can be seen, this effective external deficit increased $248 million in 2021, which was practically explained by the substantial rise in the goods trade deficit ($79 million) and services trade deficit (-$230 million), due to the aforementioned increase in public expenditure and economic recovery recorded in 2021. It should also be noted that the adjusted primary and secondary income accounts' deficits also rose by $84 million and $44 million in 2021.

The effective current account deficit, which excludes three extraordinary factors, rose in 2021, due to higher deficits for the goods and services trade accounts.

The changes recorded in 2021 ended up reinforcing the rising current account deficit trend recorded since 2017, which has been mainly due to the continued expansion of net services imports, but also to rising goods' imports.

2.5.1.1. Goods Trade Account

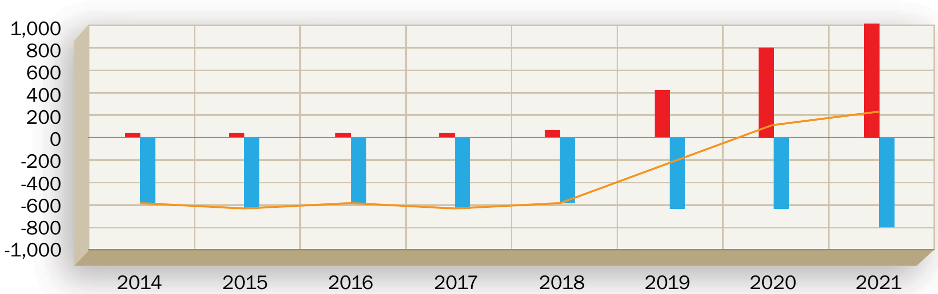
In 2021, the goods trade account, including exports of petroleum products, recorded a surplus of $215 million, which resulted in a further increase of $79 million compared to 2020. This change was mainly due to the rise in petroleum products exports (+$229 million), as goods' imports also grew $150 million.

The goods trade account has been in surplus since 2019, due the inclusion of petroleum exports since that date.

It should also be noted that the rise in exports since 2019 - due to the fact that exports of oil products are now accounted for in this sub-account instead of the primary income account - explain the substantial increase in the balance of the goods trade account since 2019.

Chart **2.20**

Goods Trade Account



In millions of USD

Export

Import

Good Account Deficit

Source: BCTL

However, if oil revenues were excluded from the goods trade balance, then this sub-account deficit would have recorded a higher deficit in 2021, amounting to $134 million, due to higher goods imports during the year, as the country's non-oil goods exports continue to be very small.

Export of Goods

As is well known, coffee is our biggest and almost only export. Coffee exports are characterized by a strong seasonality, being concentrated almost exclusively in the second half of each year, after the end of the harvest.

Table 2.9

Export Destinations

	Millions of USD			% Total	
	2020	2021	Annual Change %	2020	2021
USA	4	9	148%	25%	24%
Indonesia	1	2	56%	10%	6%
Portugal	0	1	-	0%	2%
Australia	1	1	-6%	7%	3%
Germany	0	5	-	0%	13%
Taiwan	0	0	-84%	2%	0%
Japan	1	1	23%	6%	3%
Other	8	20	162%	50%	50%
Total	**15**	**39**	**162%**	**100%**	**100%**

Source: DGE and BCTL calculation

The value of exported coffee increased substantially in 2021 from $24 million to $39 million[1], thus reversing the fall recorded in 2020.

The main destination of our exports during 2021 continued to be the USA, receiving 24% of total exports, amounting to $9 million. There was also a notable increase in coffee exported to non-traditional markets, with emphasis on the rise of Canada bound exports, to $7.2 million in 2021.

1 Before the corresponding adjustment in the balance of payments.

Import of Goods

According to the DGE and before the respective balance of payments' adjustments, goods imports rose $92 million in 2021 to $589 million, reversing the declines recorded in 2020 (-$38 million) and 2019 (-$8 million).

The main imported products continued to be fuel (21% of the total, compared to 22% in 2020), vehicles (9%) and cereals (9%). The rise in the imports of the most important items was partly due to the rise in prices and inflationary pressures in international markets in 2021, but also due to the recovery in domestic demand over the year.

The main imported products continued to be fuel, followed by vehicles and cereals.

Table **2.10**

Imported Goods – Main Articles

	Millions of USD			% Total	
	2020	**2021**	**Annual Change %**	**2020**	**2021**
Mineral Fuel	108	124	14%	22%	21%
Vehicle	49	55	12%	10%	9%
Cereal	38	53	42%	8%	9%
Beverages	22	21	-6%	4%	4%
Electrical Machinery	29	31	8%	6%	5%
Mechanical Machinery	23	26	13%	5%	4%
Meat & Derivatives	18	25	35%	4%	4%
Cement & Substitutes	18	20	7%	4%	3%
Cereal - Refined	18	20	13%	4%	3%
Iron and Steel - articles	12	33	186%	2%	6%
Edible Oils	12	13	6%	2%	2%
Milk, Eggs & Substitutes	10	7	-27%	2%	1%
Others	140	161	15%	28%	27%
Total	**497**	**589**	**18%**	**100%**	**100%**

Source: DGE and BCTL calculation

The geographical structure of imports and their annual changes are shown in table 2.11.

Indonesia has remained the country's top trading partner, although China has continued to gradually increase its importance.

Table **2.11**

Imported Goods - Countries of Origin

	Millions of USD			% Total	
	2020	2021	Annual Change %	2020	2021
Indonesia	186	194	5%	37%	33%
China, Peoples Republic of	78	112	43%	16%	19%
Singapura	52	72	39%	10%	12%
Hong Kong	39	10	-74%	8%	2%
Vietnam	21	25	23%	4%	4%
Thailand	3	7	124%	1%	1%
Australia	11	13	17%	2%	2%
Malaysia	29	24	-18%	6%	4%
Japan	8	7	-15%	2%	1%
Brazil	9	12	29%	2%	2%
Portugal	3	4	24%	1%	1%
Korea Republic of	3	1	-65%	1%	0%
Other	54	99	82%	11%	17%
Total	**496**	**580**	**18%**	**100%**	**100%**

Source: DGE and BCTL calculation

Indonesia, which has remained the country's main trading partner, represented 33% of total imports in 2021, which resulted in a decrease compared to 37% in 2020, with imports from this country increasing 5% to $194 million. The decline in the relative importance of Indonesian imports was thus due to the stronger increase in imports from other countries.

In addition to Indonesia, imports from China and Singapore continued to rank 2nd and 3rd on this list, representing 19% and 12% of total imports in 2021. It is also worth noting that aggregate imports from other countries, which have not traditionally been our largest trading partners, have continued to rise in 2021.

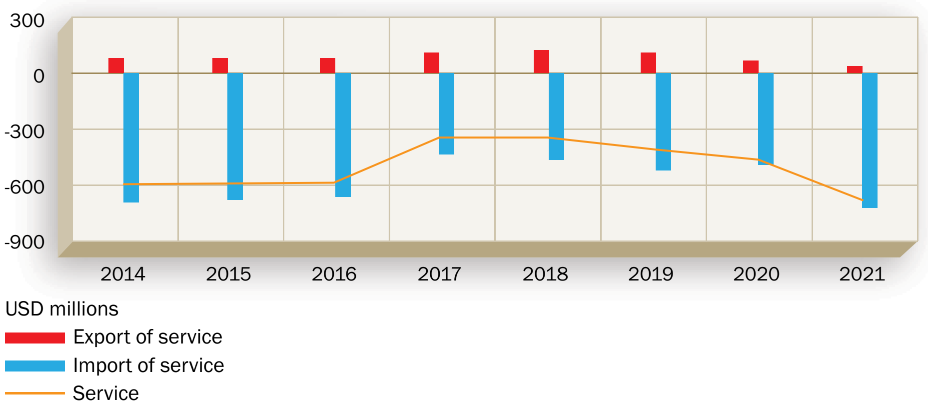
2.5.1.2. Services Trade Account

In 2021, the services trade account recorded a deficit of $683 million, which represented a substantial increase versus 2020's deficit, amounting to $230 million. As shown in chart 2.21, this change was mainly due to the increase in services imports in 2021 ($218 million), but also to lower services' exports (-$12 million) in the same year.

The services trade account recorded a higher deficit in 2021, amounting to -$683 million.

Chart 2.21

Services Trade Account



Source: BCTL

The decline in services' exports was particularly driven by the continued decline in travel services exports (-$13 million). On the imports side, it is worth noting in 2021 the substantial increase in construction services' imports (+$96 million).

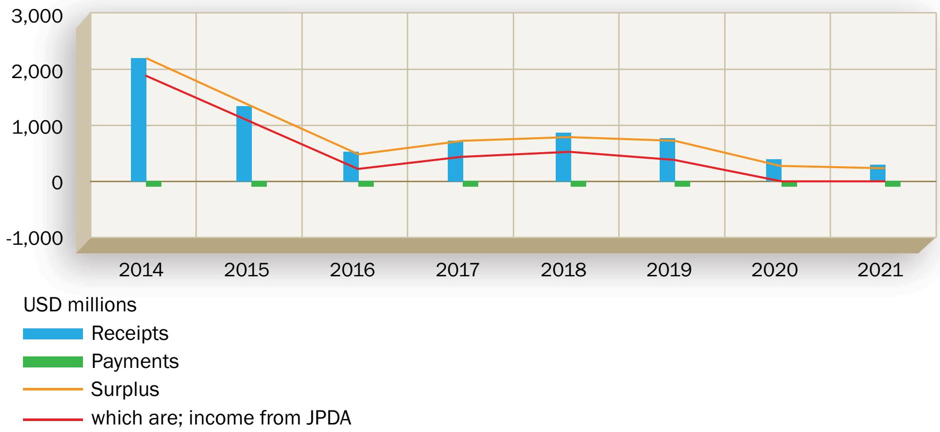
2.5.1.3. Primary Income Account

As mentioned above, oil revenues are no longer recorded in the primary income account since the end of 2019, being instead included in the goods trade account, after Timor-Leste ratified the maritime border agreement with Australia. This change explains the substantial decline in the primary income account surplus since that date.

The primary income account surplus declined in 2021, which was mainly due to the decrease in Petroleum Fund's income.

Chart **2.22**

Primary Income Account



Source: BCTL

In 2021, the primary income account surplus further declined to $213 million, which was mainly due to the decrease in the Petroleum Fund's investment income.

2.5.1.4. Secondary Income Account

Inward and outward workers' remittances registered further rises in 2021.

The secondary income account recorded a net inflow of $6.5 million in 2021, which translated into a substantial improvement compared to the negative balance of -$37 million recorded in 2020.

It should also be noted that remittances of foreign workers residing in Timor-Leste increased again by $27 million, to $318 million in 2021. On the other hand, the value of remittances received from emigrant Timorese workers also rose again by $48 million in 2021 to $171 million, contributing to partially offset the impact of higher outward remittances on the sub-account balance.

2.5.2. Financial Account

In the period under review, the financial account, which includes flows related to the economy's external financing sources, recorded a net inflow of funds of $194 million, which corresponds to a reduction compared to the $272 million in 2020.

The financial account recorded a net inflow of $194 million in 2021.

financial account continues to be mainly determined by portfolio investment flows, specifically by PF's related flows, which registered total inflows of $150 million in 2021. It should also be noted that the foreign direct investment (FDI) continued to remain close to $70 million in annual terms, which shows that FDI has remained robust when compared to post 2014 annual investment flows.

Table **2.12**

External Funding Sources

USD millions	2020	2021
Financial Account	**272**	**194**
Net Direct Investment	72	66
Portfolio Investment	244	150
PF investment in foreign	244	150
Others Investments	-45	-23

Source: BCTL

2.6 Banking System

2.6.1. Banking Assets

The banking system continued to remain stable and robust in 2021.

The banking system in Timor-Leste remained stable and solid during the period under review. The sector continues to be financed practically solely on the basis of resident deposits, lending only a fraction of these resources to companies and individuals, so that, as a whole, the banking system continues to record a robust liquidity position.

The following tables and diagrams provide a set of information about the country's banking system, which was composed, at the end of 2021, by a bank based in Timor-Leste --- the National Bank of Commerce of Timor -East --- and local branches of four important foreign banks, based in Portugal (CGD/BNU), Australia (ANZ) and Indonesia (Banco Mandiri and BRI).

Banking assets increased again by 24% in 2021, to $1,867 million.

The total assets of the banking system recorded a renewed and expressive growth of 24% to $1,867 million, which resulted in an annual increase of +$361 million and the extension of the upward trend registered since 2017. This evolution resulted, mainly, from the increase in resources invested with the BCTL (+$171 million) and other banking institutions (+$105 million), but also from the expansion of investments in securities and, to a lesser extent, bank credit.

Table 2.13

Banking System Asset

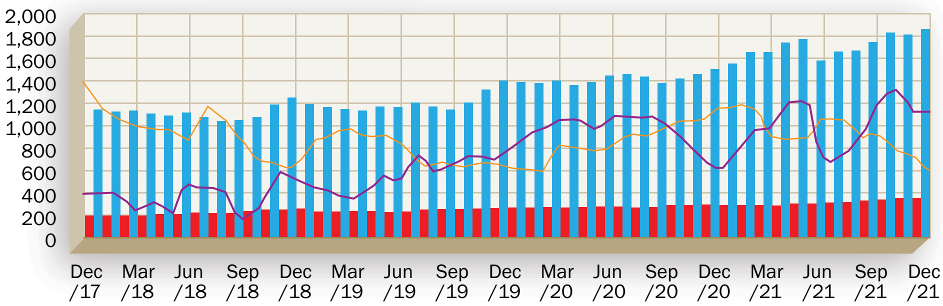
In millions of USD				Change	
	Dec-20	Dec-21	Weight (%)	%	Value
Cash & BCTL Balance	166	337	18	103	171
Placement to other Banks	1,012	1,117	60	10	105
Investment	32	98	5	208	66
Loans	278	293	16	5	15
Fixed Asset	15	16	1	3	1
Other Asset	5	6	0	41	2
Total	**1,507**	**1,867**	**100**	**24**	**361**

Source: BCTL

It is also worth noting that the growth rate of net credit has remained above or close to the growth rate of bank assets since 2017, which has resulted in a gradual and steady increase in the relative importance of credit within overall banking assets. It should be noted, however, that in 2021, contrary to what happened in the previous year, credit growth did not exceed the rate of expansion of total banking assets.

Chart **2.23**

Banking Assets Levels and Changes



USD millions and % annual change
Banking Asset
Total Credit (Net)
%Change in Credit
%Change in Asset

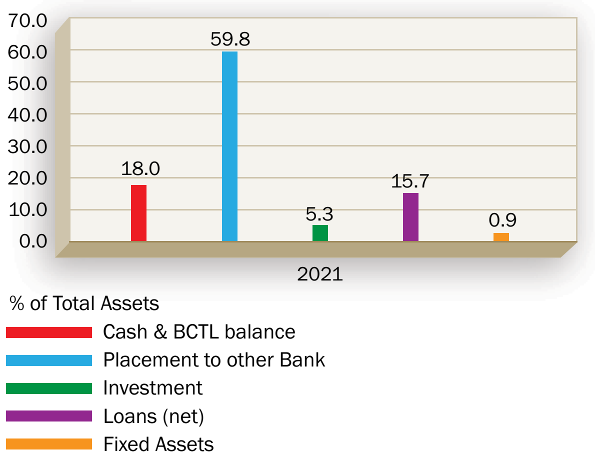
Source: BCTL

Deposits with other banking institutions, however, continue to dominate the structure of banking assets. Their weight in total assets decreased in 2021, representing 59.8% of the total at the end of the year, compared to 67.1% recorded in 2020 (charts 2.24a 2.24b). This decrease was mainly due to the increase in the weight of deposits with the BCTL.

Deposits with other banks continue to be the most important type of banking assets.

Chart **2.24a**

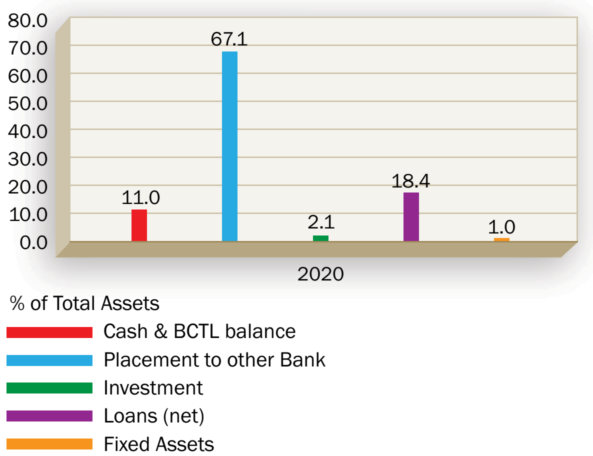
Banking Assets Composition



Source: BCTL

Chart **2.24b**

Banking Assets Composition



Source: BCTL

Credit now occupies the third position in terms of the structure of banking assets (15.7%), as the absolute increase in credit did not match the strong increase in global banking assets. The value of the banks' net loan portfolios reached $293 million at the end of 2021, having continued to grow by 5% over the year, despite the challenging macroeconomic environment.

In December of 2021, the deposits with the BCTL amounted to $337 million, which corresponds to 18% of total assets, having registered a strong and renewed expansion compared to 2020.

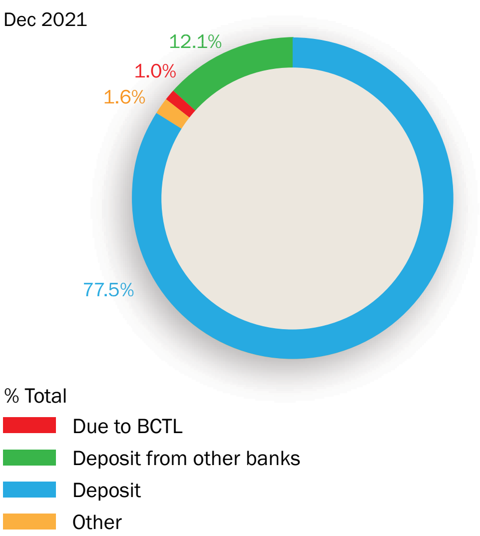
2.6.2. Banking Liabilities

Clients' deposits continue to represent the largest source of funds for credit institutions. These deposits represented 77.5% of the banks' liabilities and capital at the end of the year, having significantly increased by $340 million in 2021, while in 2020 deposits of $1,108 million represented 73.5% of liabilities and available capital.

Client deposits continue to represent the largest source of funds for commercial banks.

Chart 2.25a

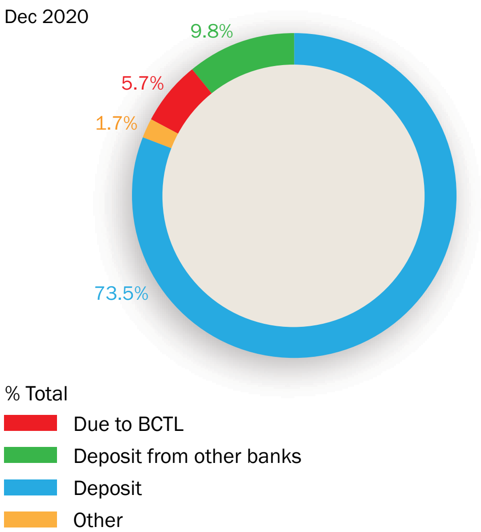
Banking Liabilities Composition



Source: BCTL

Chart 2.25b

Banking Liabilities Composition



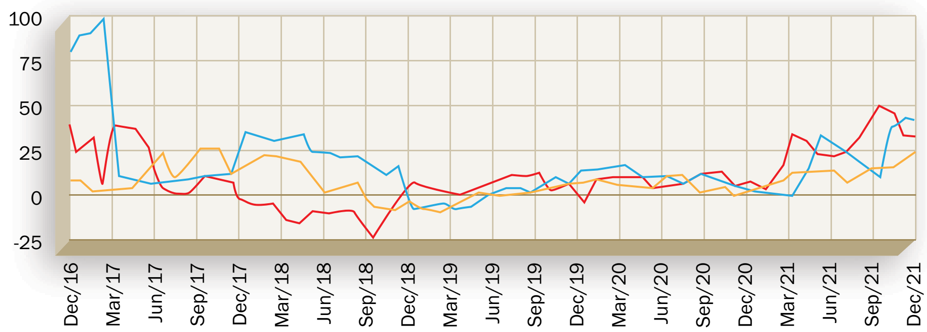
Source: BCTL

In 2021, liabilities owed to the Central Bank registered a decrease of -$68 million to 1% of resources, while deposits owed to other financial institutions increased again ($79 million), to 12.1% of consolidated liabilities. It should be noted that both categories, especially deposits received from other financial institutions, have registered large rises since 2017.

In terms of customer deposits, current/checking deposits increased $205 million in 2021, while fixed-term and savings deposits recorded increases of +$82 and +$52 million in the year, substantially reinforcing the gains seen in 2020 and 2019.

Chart **2.26**

Deposits Growth



% annual changes
Demand Deposit
Time Deposit
Saving Deposit

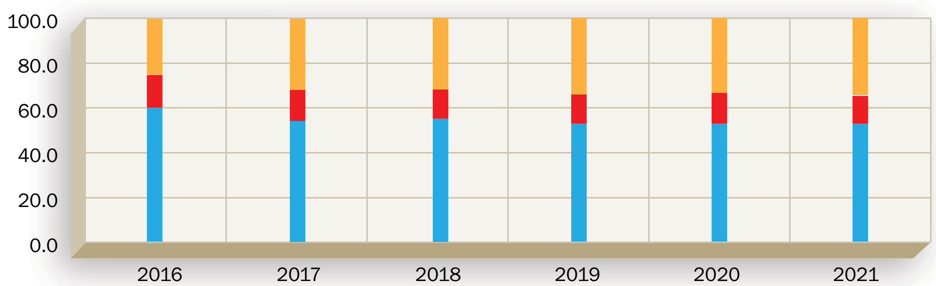
Source: BCTL

As a result of these developments, the structure of deposits registered a change in its composition, with checking and fixed-term deposits increasing in importance, in detriment of savings deposits. On-demand deposits thus continued to represent the largest component of total deposits, with 55.7% of the total. The amount invested in fixed-term deposits increased to 20.1% of the total, while savings deposits, with 23.2% of the total at the end of 2021, lost a relative importance of -2.4%, compared to their weight in 2020.

Retail deposits lost relative importance, but continue to represent the majority of banking deposits.

Chart **2.27**

Deposits Term Composition



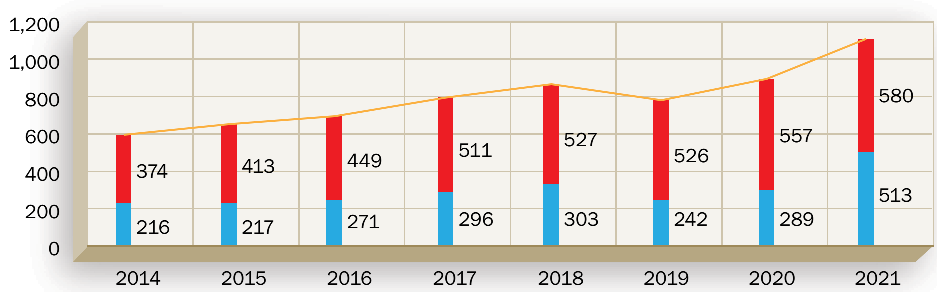
% of Total
Demand Deposit
Time Deposit
Other Deposit

Source: BCTL

In terms of deposits ownership, there was a significant change in deposits held by private residents, with individuals' deposits losing importance to 53% of total deposits and private companies deposits rising to 47% of total deposits in 2021. This development thus caused a significant increase in the weight of corporate deposits, to a level well above their relative importance over the last 10 years.

Chart **2.28**

Private Residents Deposits



In millions of USD
Particular
Private Companies
Total

Source: BCTL

As can be seen above, the significant increase in the absolute value of corporate deposits (+$224 million) explained the significant increase in their weight in 2021, as retail deposits continued to increase by $23 million in 2021.

2.6.3. Banking Profitability

Banks' operating revenues consisted of interest and fees charged to their customers, amounted to a total of $42.8 million, representing a decrease of -$4.1 million compared to 2020 and slightly offsetting the upward trend recorded since the end of 2018.

Banks' gross operating income declined in 2021 to $40 million.

As a result of their activity, the banks presented the following consolidated earnings in 2021, which are compared with the equivalent values of 2020 in the following table:

Table 2.14

Banking System Consolidated Earnings

Items	In millions of USD		% Annual Change	% Gross Op. Result	
	2020	2021		2020	2021
Net Interest	34.0	30.7	-10%	78%	77%
Commission & Other revenue Op.	12.8	12.0	-6%	29%	30%
Gross Operating Result	**43.6**	**40.2**	-8%	100%	100%
Provision & Impairments	-2.7	-2.5	-7%	-6%	-6%
Operational Expenses	-22.1	-21.9	-1%	-51%	-55%
Net Operations Income	**18.7**	**15.8**	-16%	43%	39%
Net Income	**17.1**	**14.3**	-16%	39%	36%
RoA % - Return on Assets	1.16%	0.78%	-33%		
RoE % - Return on Equity	13.1%	10.6%	-19%		

Source: BCTL

In terms of variations, we already highlighted the decrease in operating revenue, including both interest and fees. Given the simultaneous decline in interest costs and commissions paid by banks, gross operating income declined by just -$3.4 million in 2021. In line with the decline in gross income, given stable operating expenses including provisions, banks' net operating income fell to $15.8 million, from $18.7 million in 2020.

Finally, taking into account extraordinary revenues and costs as well as income taxes for the year, the system's consolidated net income decreased to $14.3 million in 2021 from $17.1 million in the previous year.

The banking system continues to present robust profitability levels, which were, however, lower than in 2020 and 2019.

This decrease explained the bulk of the contraction in return on assets (RoA) ratio in 2021 to 0.78%, compared to 1. 16% in 2020 (1.53% in 2019), as well as the reduction in the return on equity (RoE) ratio to 10.6% from 13.1%. It should be noted, however, that these two ratios decreased more than the fall in absolute net income, which was explained by the expansion of banks' assets and capital. Banks continue to maintain liquidity ratios above those required by the central bank and the existing regulatory framework.

2.6.4. Money Transfer Services

2.6.4.1. Remittances Transfers - Commercial Banks

In 2021, money transfer services, reported by commercial banks operating in Timor-Leste, recorded total number of transfers abroad of around 110 thousand, with an aggregate nominal value of $1,741 million. The number of this type of operations carried out by banks increased 20% and the total transferred amount grew substantially by 17%, compared to 2020.

The net balance of international transfers intermediated by commercial banks fel further to -$1,024 million in 2021.

On the other hand, the number of received transfer operations jumped 48% in 2021 to 84 thousand transactions, with the amount received also growing by 24% to $717 million.

As a result of these transactions, the net balance of transfers received and originated by commercial banks decreased in 2021 to -$1,024 million, compared to the negative balance of -$912 million in the previous year.

2.6.4.2. Remittances Transfers – Other Transfer Operators (OTOs)

In 2021, other money transfer operators (OTOs) recorded a total value of transfers abroad of $137 million, compared to $103 million in 2020. Transfers from abroad and intermediated by these operators amounted to $135 million, compared to $88 million in 2020. This evolution translated into a renewed improvement in the deficit balance of this type of transfers, to -$1.7 million only, compared to -$15 million in 2020.

The net balance of transfers intermediated by OTOs improved again in 2021 to -$1.7 million, compared to -$15 and -$48 million in 2020 and 2019.

Personal transfers continued to represent the largest share, both in terms of inflows and outflows, amounting to 44% and 92% of total transfers, either way. Personal transfers aggregate the ‘family’, ‘education’ and ‘savings’ justifications invoked in the transactions.

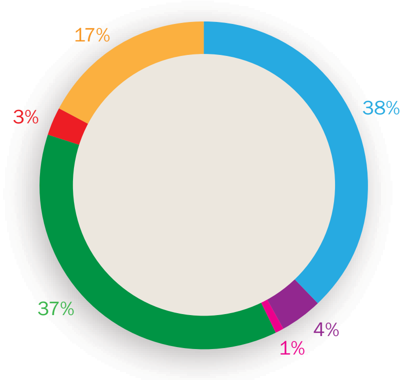
In geographic terms, most inflows continued to be originated in Europe, accounting for $74.4 million in 2021 (55% of the total), compared to $55 million in 2019, mostly explained by the remittances from Timorese workers residing and working in Europe. Remittance outflows operated by OTOs were, for the most part, sent to the Asian region ($120 million), especially Indonesia ($96.7 million, with 71% of total outflows), which continues to benefit from remittances sent by citizens Indonesians residing and working in Timor-Leste.

Remmitances inflows continue to be mainly originated in Europe, while outflows continue to be mostly sent to Asian countries and, in particular, Indonesia.

Diagrams 2.29a and 2.29b depict the composition of outward and inward transfers, according to their purpose, intermediated by other money transfer operators in 2021.

Chart **2.29a**

OTOs Outward Transfers, by Purpose



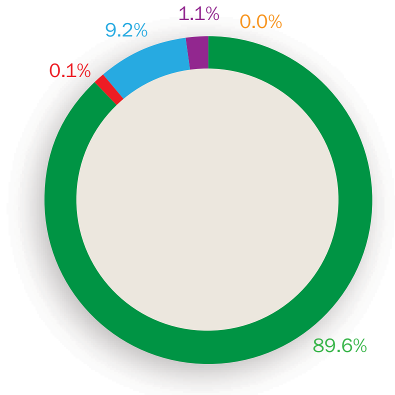
% Total

Familiar | Education
Investment in the company | Purchase
Saving | Other

Source: BCTL

Chart **2.29b**

OTOs Inward Transfers, by Purpose



% Total

Familiar | Education
Investment in the company | Purchase
Saving | Other

Source: BCTL

2.7 Relevant Socio-Economic Monitoring and Support Initiatives

This subsection describes the overall substantial damages and socio-economic impacts caused by the pandemic crisis and April 2021's massive floods, as well as the respective policy programs implemented by public authorities to address these extraordinary events and respective impacts. It also includes a detailed overview of relevant socio-economic surveys implemented by the BCTL in 2021.

2.7.1 Pandemic and 2021 Floods Socio-Economic Impact Assessment

As all countries around the world, Timor Leste's society and economy have been deeply impacted by the Covid-19 pandemic since 2020. In addition to the ongoing pandemic challenges, the country was also terribly affected in 2021 by the massive floods caused by the onset of tropical cyclone seroja, which, in addition to its terrible human and health tragedies, produced substantial and widespread damage to the country's public infrastructure, private housing and agricultural land.

Covid-19 Pandemic Impacts

Covid-19 has been a serious public health issue in the country since 2020. Up to 15 December 2022, the virus had infected 19,830 people in the country and caused 122 deaths (Table 2.15). These values amount to 9.4% and 0.1% of the total number of people tested for Covid-19. Up to December 15, 2020, there were only 31 reported cases.

Table **2.15**

Number of people testing positive for Covid-19 and number of deaths

Data	Total cases	New cases	Total death	New death	Total recovered	Active cases	Total people tested
15-Dec-20	31	0	0	0	30	1	14,932
15-Jun-21	8,285	0	18	0	6,731	1,536	92,122
14-Oct-21	19,690	9	119	0	19,438	38	169,501
16-Nov-21	19,810	1	122	0	19,682	6	169,501
15-Dec-21	19,830	1	122	0	19,704	4	211,166

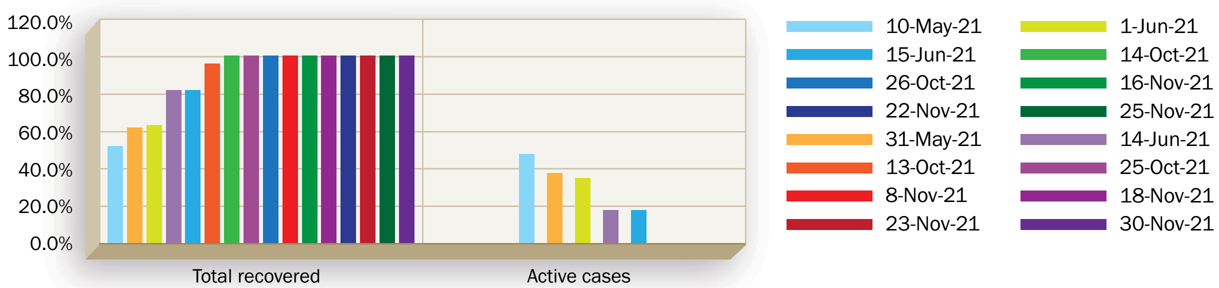
Note: Unchanged row numbers indicate that no new cases were reported.

Source: Worldometer

Up to December 15, 2021, 211,166 people were already tested for Covid-19 and of the total affected, 99.4% have recovered, which confirms the country's low covid lethality rate. As shown in chart 2.30, the percentage of people that recovered from Covid-19 during May-December 2021 increased, while the percentage of people affected by it decreased during the same period. The period between May and June corresponds to the pandemic peak in the country, up to now. We also note the low prevalence of the virus in the country at the end of 2021, as there were only 6 and 4 active cases in November and December of 2021.

Chart **2.30**

Percentage of People Affected by the Covid-19 virus



Source: Worldometer

The total number of people tested for Covid-19 rose 84% in December of 2021 to 211,166, from the 14,032 tested up to December of 2020, as shown in table 2.16.

Table **2.16**

Evolution of number of people tested for Covid-19, 15 December 2020 – 15 December 2021

14,932	**92,122**	**169,501**	**211,166**
15 December 2020	31 May 2021 – 15 June 2021	13 October 2021 – 15 November 2021	10 December 2021 – 17 December 2021

Source: Worldometer

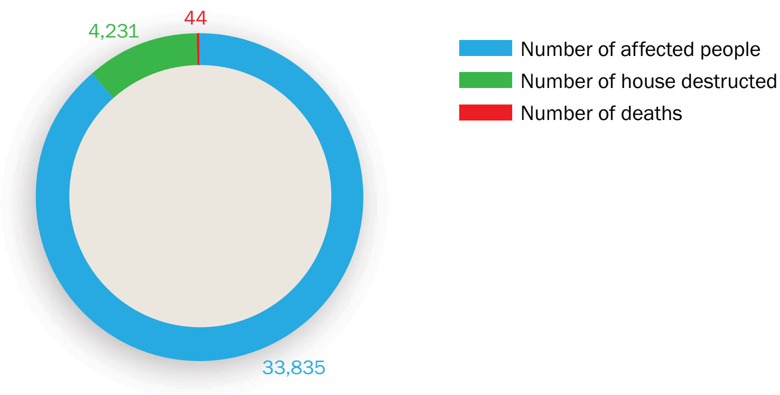
Beyond the tragic loss of lives and impact over our people's health, the pandemic has substantially weighed down domestic economic activity, due to the imposition of the state of emergency, strict confinements and sanitary enclosures. These public-health policies forced most businesses to close, with the exception of businesses that sold essential goods such as supermarkets, pharmacies and construction materials' wholesalers and retailers. Naturally, these widespread negative impacts required immediate public policy responses, which we will detail below.

April 2021 Floods Impact (tropical cyclone seroja)

In addition to the pandemic, the April of 2021's tropical cyclone seroja and subsequent mass-floods compounded the damages to our society, causing further tragic life losses, impairment to many public infrastructures and civil population's houses country wide. As shown in chart 2.31, 33,835 people were affected by the cyclone, 44 people died or went missing and 4,231 houses were destroyed by floods and landslides, due to heavy rains from March 29th to April 4th of 2021.

Chart **2.31**

Number of people affected and houses destroyed by tropical cyclone seroja



Source: United Nations-Timor Leste and Tatoli 2022

A total of 183 public facilities were also devastated during this period, as shown in table 2.17. The Ministry of Public Works's (MOP) survey reported that 78 infrastructures were destroyed (excluding public buildings) during the tropical cyclone seroja and that a total of 183 public infrastructures and buildings in 28 locations were substantially impaired. Those facilities specifically included public roads, bridges, protection walls, electricity lines and public buildings. Additionally, a total of 2,163 hectares of agricultural lands were also affected by the floods, which further weighed down on agricultural production and food availability in the country (UNRCO, 2021). The scale of the damages required the approval of an amended public budget in May of 2021, urgently required to finance the respective relief, recovery, renovation and rebuilding activities.

Table **2.17**

Number of infrastructures destroyed during the tropical cyclone seroja

No	Infrastructure	Quantity	Unit
1	Roads	22	Roads
2	Bridges	8	Bridges
3	Protection walls	20	Walls
4	Electricity lines	28	Locations
5	Public building	105	Buildings
	Total	**183**	**Units**

Source: Timor Post, Ministry of Public Works and GMNTV

2.7.2 Public Policies Implemented to address these Situations

Beyond the enforcement of social distancing measures, mask usage, border and people movement controls and provision of free food baskets to households around the country, the Government undertook two main programs to address and mitigate the pandemic impacts: the vaccination and credit moratorium programs.

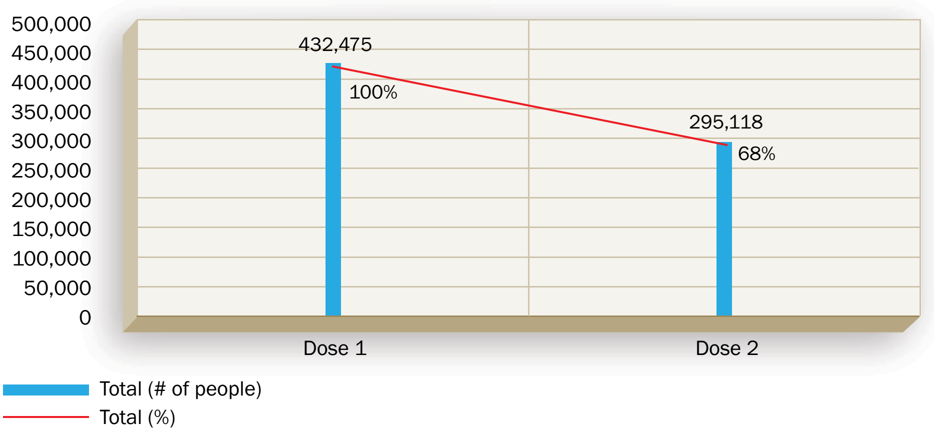
Vaccination Program

As around the world, vaccination programs have become in 2021 the principal mitigation policy to address the dissemination and lethality of the Covid-19 virus. Vaccination programs were implemented to improve people's immunity against covid-19 although they do not fully prevent the virus onset and its dissemination.

As shown in figure 2.32, as of December 2021, 432,475 people across the country were already vaccinated, while 68% of them had already received 2 full doses of either AstraZeneca, Sinovac or Pfizer's vaccines, which amounts to 22.7% of the total population.

Chart **2.32**

Total number of vaccinated people



Source: RSETL

Of those vaccinated, 40.1% reside in Dili while the rest (59.9%) live in other municipalities. We also highlight that 32% of the 432,475 vaccinated people still need to receive their second dose, to have a higher degree of immunity.

Given the ongoing public vaccination program efforts, we expect the population inoculation rate to increase above these 2021 levels, but note that this rate is still substantially below the world's top countries' vaccination rates.

Credit Moratorium Program

In order to directly support households and companies dependent on financing from commercial banks, the Government designed and implemented the credit moratorium program, aiming to extend general loans' maturities for nine months. Initially, this program was planned for three months only and was introduced in August 2020 to respond to the intitial pandemic stage. According to the program's guidelines, the State subsidizes 60% of lending interest costs to commercial banks while borrowers pay only 40% of the lending interest costs during the program's period. Borrowers will be required to pay both principal and full loan interest costs after these nine months, as mandated under the credit moratorium program.

In 2020, 4,124 people across 13 municipalities benefitted from the program, whose total amount was $0.67 million (BCTL, 2021). For 2021, no official beneficiaries' data was yet reported, as this program is expected to last for nine months, ending in March of 2022.

Public responses to April 2021 Mass-Floods

Our government and the country's development partners spent a total of $32 million in order to address the devastation caused by the massive floods' crisis (Timor Leste Government and United Nations, 2021). Of these $32 million, $8.8 million were allocated to immediate relief efforts and $23.9 million for short term recovery and rebuilding plans that directly helped 65,000 people and indirectly benefited all the flood affected population. At least 86 organizations participated in the joint relief plan which lasted for 7 months until December 2021. This set includes 9 UN agencies, 63 humanitarian partners and 14 public ministries and departments (Table 2.18).

Table **2.18**

Number of Agencies involved in the Joint Recovery Efforts

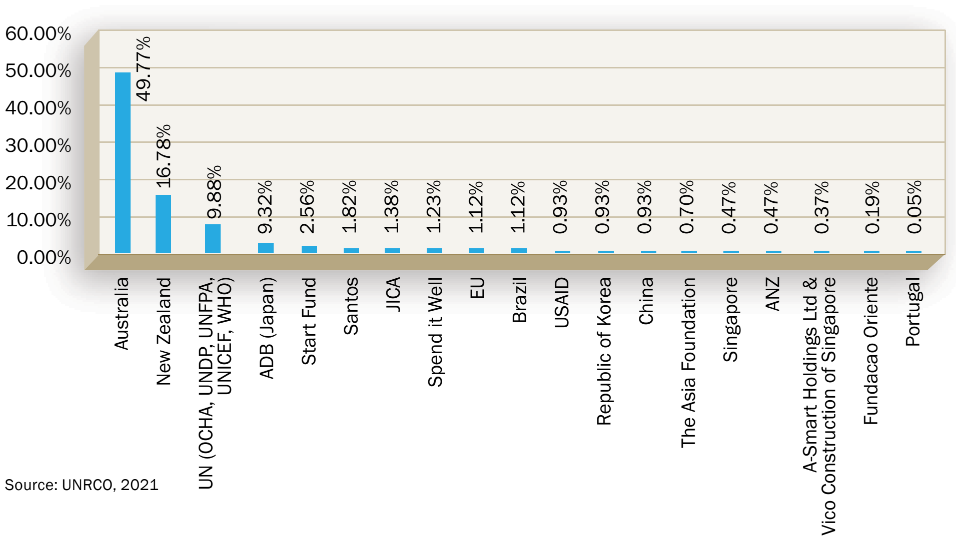
Agency	# of involved agencies
UN	9
Humanitarian partners	63
Ministries and Department	14
Total	**86**

Source: United Nations-Timor Leste in Tatoli, 2021

From the $10.7 million allocated by development partners to assist the cyclone's victims, the most part was financed by the Australian government (49.8%), New Zealand government (16.8%), United Nations (9.9%) and Asian Development Bank (9.3%). In addition, less than 3% of the total contribution came from other 15 international partners as depicted in chart 2.33. In total, 19 international organisations were involved in the flood recovery program. The State, through the Secretary of State for Civil Protection, also offered food and non-food items to 12,197 flood affected households across the 13 municipalities. These goods included 317.5 metric tons (MT) of rice, 104 MT of other edible items and more than 18 MT of non-food articles (UNRCO, 2021).

Chart **2.33**

Development Partners Contribution towards
Assisting Cyclone Seroja's Victims



Source: UNRCO, 2021

Together with the immediate and short-term recovery efforts, the government allocated a total $287.6 million to finance the overall relief and rebuilding programs, including also the public programs to mitigate the pandemic effects.

This allocation included an increase of the contingency fund's budget from $23.8 million to $65.2 million in April 2021 to mitigate the pandemic impacts in 2021 and for responding to the April 2021 cyclone seroja's damages. The covid-19 fund was mostly used to procure vaccines, protective equipment and materials for virus testing and medical treatment. Part of the covid-19 fund was also used to finance employment support programs, students' internet access, students' enrolment fees, wage supplements for front-line workers and basic consumption baskets for all deprived households in the country.

2.7.3 Economic Activity and Financial Inclusion Survey

The BCTL together with Escola Secundaria de Nossa Senhora do Carmo, Lete-Foho (ES-NOCAR), prepared and implemented a case study survey in the administrative post of Lete-Foho, municipality of Ermera, between January and June of 2021. The survey intended to collect and assess socio-economic data regarding the types and value of economic activities and financial inclusion trends for households in Lete-Foho.

Picture 2.1. Survey Socialization Activities

This activity consisted in a field survey undertaken by ES-NOCAR in the 8 sucos belonging to Lete-Foho, specifically: Dukurai, Eraulu, Goulolo, Hatugau, Haupu, Katrai-Kraik, Katrai-Leten and Lauana.

The survey showed that: the majority of these households work for the coffee industry; most of their income is used for consumption or daily needs; and that the majority of the households in Lete-Foho still does not have access to formal financial services. In addition, the long distance to financial services' access points is considered the main obstacle faced by households in that administrative post, in terms of their access to financial services.

Picture 2.2.
Survey Participants

2.7.2.1 Economic Activity Survey

The economic survey showed that 85% of households in Lete-Foho work in coffee farming, 19% are involved in business activities, 13% in horticulture, forestry or mining activities and that only 9% are involved in livestock activities.

Chart **2.34**

Lete-Foho - Economic Activities

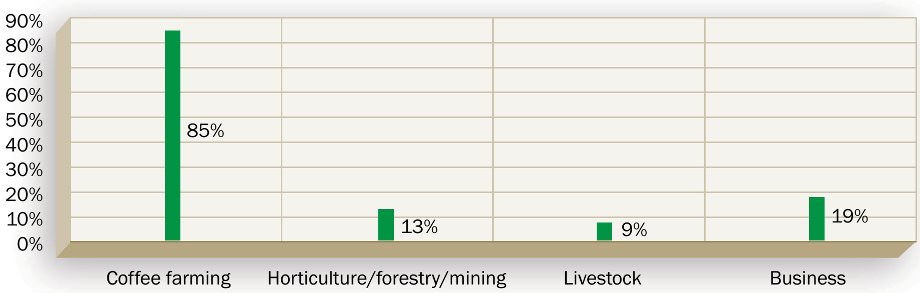
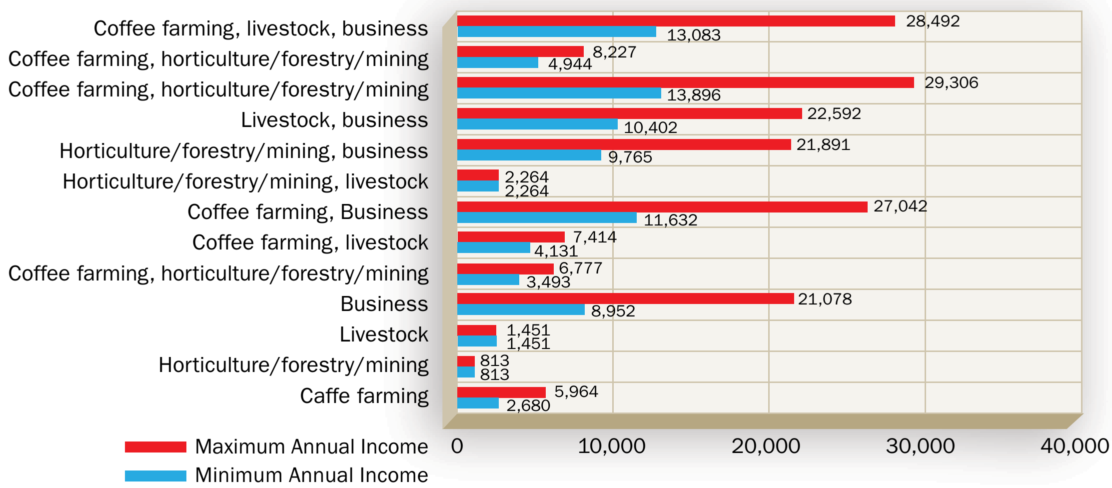


Chart 2.35 shows the minimum and maximum household income in each one of the 4 economic activities, considering also a business or livestock segmentation.

Chart **2.35**

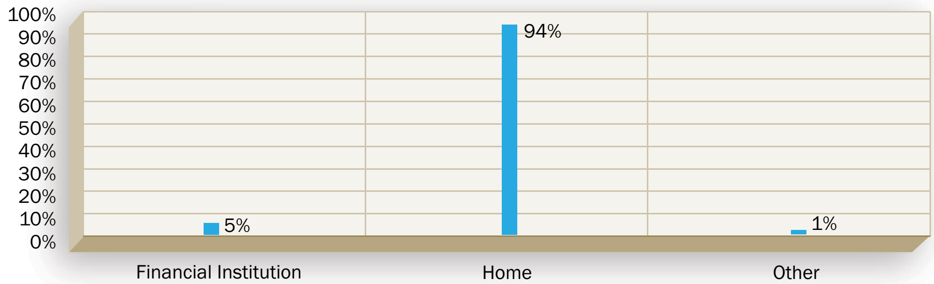
Lete-Foho Income From Economic Activities



The survey results showed that 94% of households hold their cash balances at home, 5% in financial institutions and 1% stated that their income was kept with the cooperatives to which they belong or the CCT.

Chart **2.36**

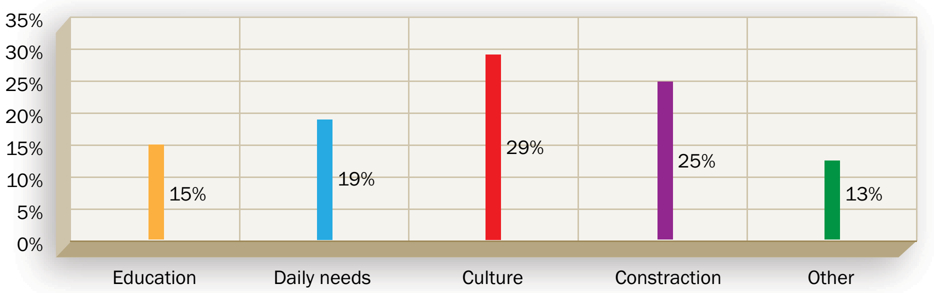
Income Savings



In terms of household spending needs, the survey results showed that: 29% of net income is used for cultural activities, 25% for housing (house rehabilitation or construction), 19% used to meet daily needs, 15% for education and 13% used for other expenses or investments. These other expenses category includes the purchase of vehicles or motorcycles, livestock, retail business inventory, loan repayments and external agricultural workers wages, mostly for coffee production activities.

Chart **2.37**

Lete-Foho Spending Needs

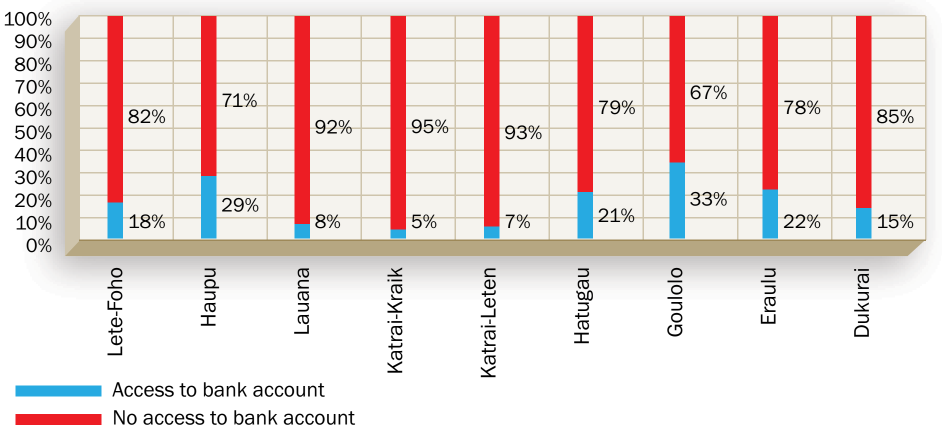


2.7.2.1 Financial Inclusion Survey

This simultaneous survey concluded that 82% of households in Lete-Foho do not yet have a bank account, while only 18% of them reported having a bank account. In terms of considered Sucos in Lete-Foho, we obtained the following bank account access percentages: in suco Goulolo 33% of households have a bank account, in suco Houpu with 29%, Eraulo with 22%, Hatugau with 21%, Dukurai with 15%, Lauana with 8%. Katrai-Leten with 7% and finally Katrai-Kraik with only 5%.

Chart **2.38**

Lete-Foho Bank Accounts Access



For those who already have a bank account, 55% are BNCTL clients, 25% are Moris Rasik Financial Service clients, 8% are BNU and Mandiri clients respectively, 4% are KIF clients and BRI only has 2% of clients in Lete-Foho.

Of those households which have a bank account, 49% reported that it is mostly used to get acess to bank credit, 19% reported that their bank account is used for savings, 17% informed that their bank accounts are intended to receive their wages and 15% stated that their bank accounts serve to receive benefits or subsidies.

Chart **2.39a**

Lete-Foho FIs Bank Accounts Shares

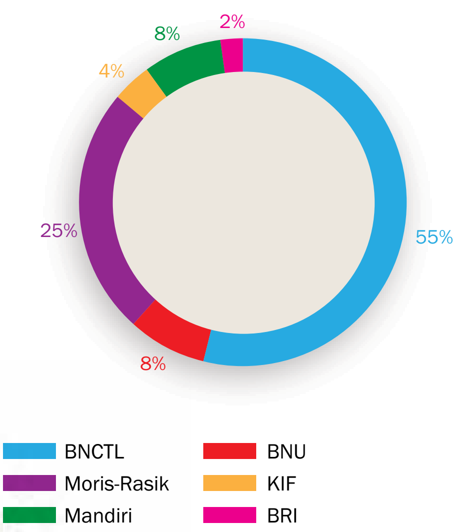
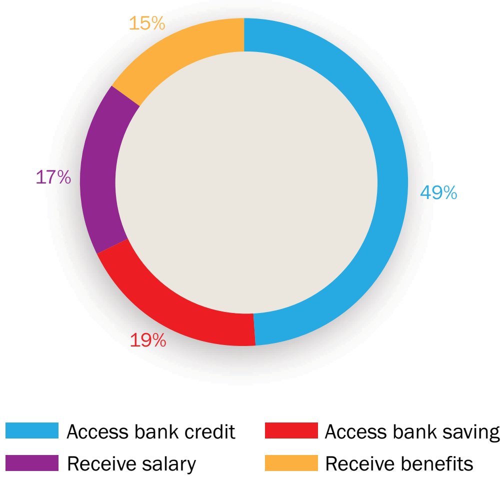
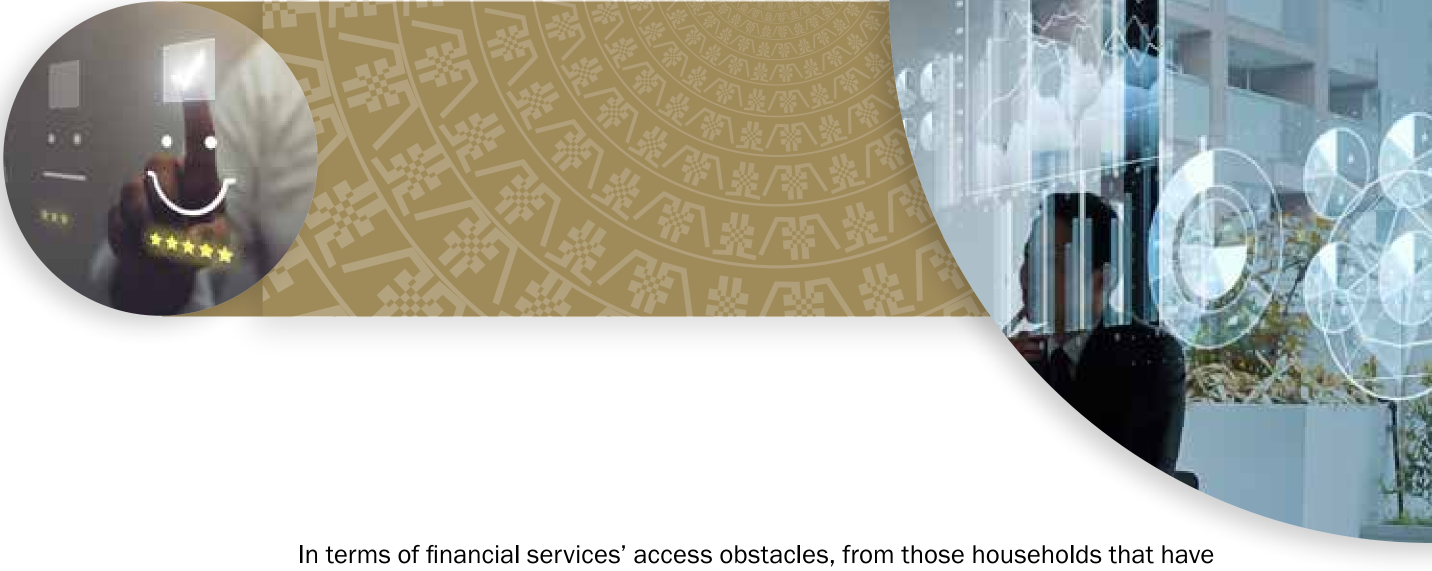


Chart **2.39b**

Bank Accounts Uses

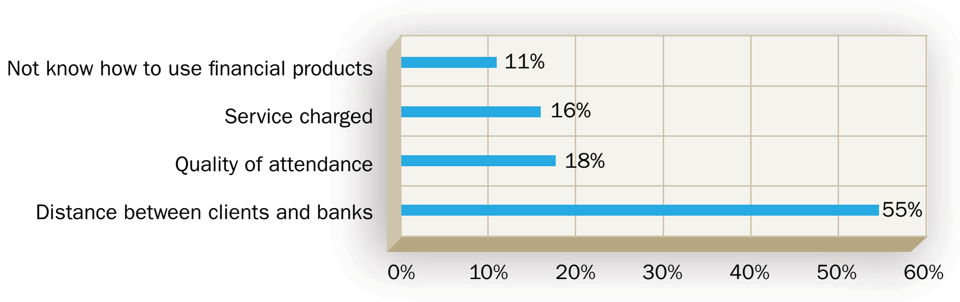




In terms of financial services' access obstacles, from those households that have already accessed to financial services or that already have a bank account: 55% reported that the main issue in accessing financial services was the material distance to financial institutions' (FI) agencies; 18% were mostly affected by poor FI's service, 16% were unsatisfied with FI's services costs and 11% reported that they do not yet know how to use existing financial products, such as ATMs.

Chart **2.40**

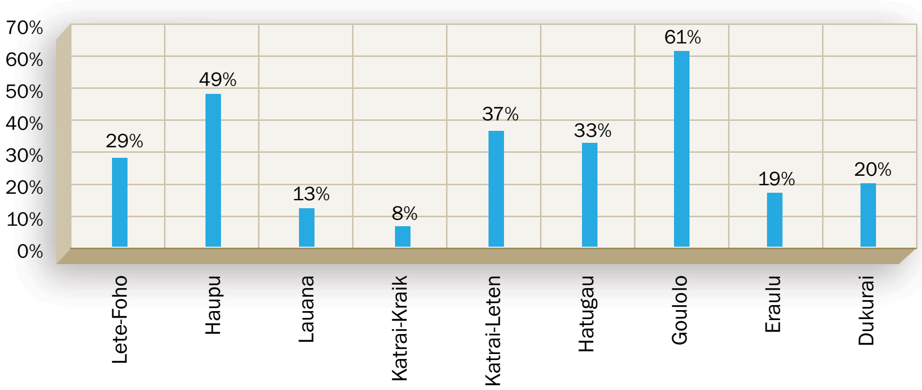
Lete-Foho - Obstacles to Financial Services Access



The survey further showed that 29% of households have already had access to formal bank credit or to private informal loans. From these households, 66% obtained bank credit in financial institutions, 25% had borrowed loans from other households or private businesses and 9% reported having had access to NGOs' credit facilities.

Chart **2.41**

Lete-Foho - Access to Bank Credit or Informal Loans

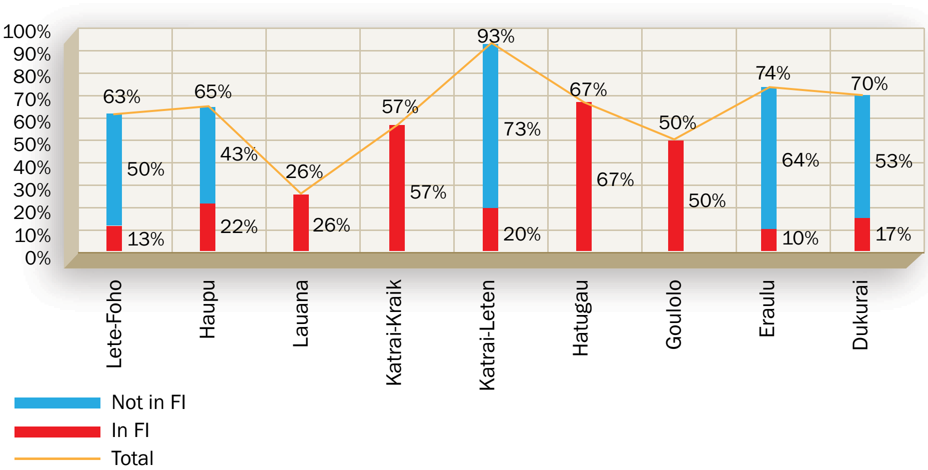


In terms of actual needs, 63% of households reported having the need to access bank credit or private loans. Of these, 50% stated that they intend to access credit through FIs and 13% reported that they do not wish to access FIs loans.

In terms of Sucos, 93% of Katrai-Leten's households have the need to access credit or loans, while 73% intend to acess credit through financial institutions. In the meanwhile, in sucos Goulolo, Hatugau and Lauana, all the households that will need loans intend to do so through FIs credit (details in chart 2.42).

Chart **2.42**

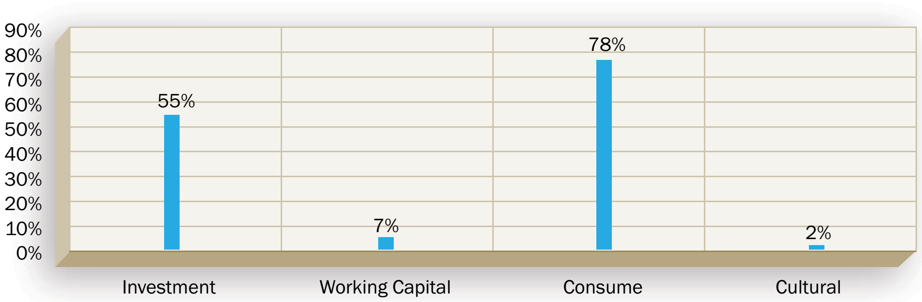
Lete-Foho - Future Credit Financing Intentions



Of those interested in accessing bank credit or loans, 78% report that they will use this for daily consumption, 55% inform that they will use it for investment, 7% plan to use it to cover working capital needs and 1% state that it will used for undertaking cultural activities.

Chart **2.43**

Lete-Foho - Future Financing Usage Intentions



The BCTL: **Mission and Core Mandates, Organization, Governance and Activities**

Chapter 3

The BCTL main mission consists in continuing to ensure and improve the quality of the services it provides to the Community, while maintaining a stable monetary system, as well as promoting a robust and functional financial system.

This mission is pursued by maintaining: a low and stable inflation rate, a secure and efficient payment system; credible functioning of all financial institutions, through the implementation of appropriate legal and regulatory standards and banking supervision; the financial education of the population; and conducting studies on the national economy, supported by rigorous and useful statistics.

Taking into account the BCTL's mission, this chapter provides an overview of the institution's mandates and functions, its governance structure and key activities carried out during 2021, as well as its 2022 action plan. The brief summary of annual activities also details the main initiatives developed throughout the year by each of the various functional areas of BCTL.

3.1 Core Mandates and Functions

The BCTL is a legal person governed by public law, with administrative and financial autonomy and its own assets. The BCTL, its entities, employees and agents, enjoy independence and cannot receive instructions from external entities, and its Organic Law guarantees the necessary independence of the Central Bank vis-à-vis the Government.

As is common in most international central banks within the area of economic policy, BCTL's main objective is to ensure the stability of domestic prices. Other equally important objectives are the promotion of a financial system based on market economy's principles, where there is appropriate competition, which works in favour of citizens and the economy in general. Having these objectives and principles as a guiding line, the Central Bank should also support the Government economic policies.

In order to achieve its objectives, the functions of the BCTL are, under the terms of the law:

a) Define and implement the country's monetary policy;
b) Define and adopt the exchange rate regime as well as the associated exchange rate policy;
c) Carry out operations in foreign currency;
d) Hold and manage the country's official external reserves;
e) Hold and manage the State's gold reserves;
f) Issue and manage the official currency of Timor-Leste --- at this time the country uses the US dollar as its currency;
g) Collect and distribute statistical information regarding the areas within its competence, namely monetary, financial and balance of payments statistics;
h) Inform the National Parliament, the Government and the general public about the policies it implements;
i) Establish, promote and supervise the national payment system, in order to guarantee the efficient and safe execution of payments;
j) Regulate, license and supervise financial institutions operating in the country;
k) Advise the Government on matters within its competence;
l) Act as fiscal agent of the Government;
m) Participate in international organizations and meetings that concern the above-mentioned points;
n) Be part of contracts and establish agreements and protocols with national or foreign, public or private entities; and
o) Perform any other activities as defined by law.

Currently, some of these functions are not yet performed by the BCTL due to the adoption of the US dollar (USD) as the official currency of the country.

3.2 BCTL Organization and Governance

BCTL's highest authority is its Board of Directors, which formulates the institution's strategies and policies and oversees their implementation, including the supervision of the Bank's executive management and operational activities.

The Governor is the highest executive body of BCTL, or its Chief Executive Officer and is assisted by two Vice-Governors and a Management Committee composed of the Directors and heads of various departments of the Bank. At the end of 2021, the year of this report, the Board of Directors was composed by the Governor, two Vice-Governors and four non-executive members. The composition of the Board of Directors and the Management Committee are presented at the end of the chapter.

BCTL is internally organized into four main departments: Financial System Supervision; Banking and Payments Systems; Petroleum Fund Management; and Administration. Some Divisions and Units report directly to the Governor, namely the: Legal Unit, Internal Audit, Economics and Statistics Division, the Institutional Cooperation Affairs Unit, Human Resources Division (which previously belonged to the Administration Department) and the Financial Information Unit. The Accounting and Budget Division is dependent on the Deputy Governor responsible for the supervision of the financial system. The central bank is also in charge of the secretariat of the Advisory Board for the investment of the Petroleum Fund.

BCTL's Board of Directors continues to adopt the motto abbreviated by the acronym **TIMOR**, representing **T**ransparency, **I**ntegrity, **M**obilization, **O**bligation and **R**esponsibility, essential slogans in the day-to-day operations of the institution and of its employees.

Institutional **Values**

Transparency

We are a role model for society and for the institutions, our procedures and rules are clear and applied in a rigorous, universal and consistent way, both internally and externally.

Integrity

We exercise our business with honesty, high ethical and moral standards, respecting the confidentiality and legality in all actions and decisions involving our interests and resources.

Mobilization

We mobilize to provide the best service to the Timorese community, through the ability to consult, listen and learn so committed.

Ownership

We exhibit a sense of belonging and involvement, establishing as priority the objectives of the institution and showing availability to perform activities beyond the scope of our role.

Responsibility

We invest in expanding our technical and professional skills, deliver on the responsibilities that are assigned to us and that we proactively seek, through ongoing monitoring of the consequences of our decisions and actions.

BCTL has long adopted a code of ethics applicable to all employees, also covering appropriate guidelines in dealings with external entities to the Bank. The code of ethics includes strict rules on various aspects of the behaviour of those to whom it applies. Note, for example, the obligation of every Bank employee to perform its duties solely on the basis of serving the BCTL and general public interest, and not their individual interests, which includes not receiving instructions, whatever they may be, from entities other than the legally appointed structures of the Central Bank.

Bank employees are also, of course, forbidden to receive any remuneration from any persons or institutions who may be interested in influencing their decisions.

3.3 BCTL Activities in 2021

As part of the BCTL's mission to promote monetary and financial stability, the development of the financial system and the promotion of a secure and efficient payment system, the following set of activities and initiatives were planned and implemented in 2021.

In the context of implementing the Master Plan for the Financial Sector in Timor-Leste, the BCTL, in 2021, continued to modernize the national payment system. In this regard, we highlight the final implementation of additional R-TiMOR functionalities to serve the needs of the Ministry of Finance and its sub-accounts and producing activity analysis reports on a monthly and annual basis. These new services allow the Ministry of Finance and its sub-accounts to now have access to historical statements, prepare cash management and project cash flows in real time.

The Central Bank also introduced new payment features, that enable users to pay taxes and undertake B2W2B transfers. The functionality of B2W2B, in addition to making it possible to pay taxes, also allows any holder of a P24 card to transfer money from their bank account to a Mosan e-wallet account and vice versa.

The BCTL's Board of Directors took several decisions throughout 2021, from which we highlight, among others, the granting of licenses to companies with the aim of enhancing and facilitating Timor-Leste's population access to the financial sector.

The Board of Directors also approved several instructions and regulatory frameworks related to the financial sector and good governance, as exemplified by the Internal Audit Manual.

The celebration of the 7th anniversary of the National Savings Day, on 29 November 2021, took place at the administrative post of Maubisse, in the municipality of Ainaro. The program consisted of carrying out the 1st anniversary of the "Campo Digital" pilot program, with the participation of local authorities, representatives of commercial banks, fintech companies and their agencies, users of financial services, students and the Maubisse community.

Due to the continuation of the pandemic situation in 2021, BCTL had to postpone again the implementation of some activities, including initiatives to promote the national private sector, namely the basic accounting training module for Micro, Small and Medium Enterprises (MSMEs) staff, in cooperation with IADE and the Timor-Leste Chamber of Commerce and Industry (CCI-TL).

The BCTL also continued to develop, through its “Institutional Cooperation Affairs” Unit, its cooperation activities with similar institutions and relevant organizations, both nationally and internationally. These activities have mainly focused on the areas of technical assistance and internal capacity building, with the aim of reinforcing the effectiveness of the cooperation program and strengthening BCTL’s institutional partnerships. Most of the cooperation activities between the BCTL and its counterparts throughout 2021 continued to be carried out virtually, due to the ongoing pandemic situation.

These and other BCTL activities carried out in 2021 are described in more detail in the following section.

3.3.1. National Payment System

3.3.1.1. Interbank Clearing and Settlement System

During the period covered by this report, the Central Bank continued to act in a consistent manner so as to always maintain sufficient cash reserves to meet the cash payment requirements of state entities and commercial banks. In this context, BCTL ensured the permanent functioning and execution of interbank financial transactions through the Clearing House and Real Time Gross Settlement (RTGS) systems. It should be noted, however, that the activities of the automatic “Clearing House” system could not be carried out during the year due to the implementation of social distancing measures, to mitigate the impacts of the pandemic. This fact meant that in 2021 it was not possible to record the movements and values liquidated in the Interbank Clearing and Settlement System (CEL) in Dili.

3.3.1.2. The SWIFT and R-Timor (RTGS) Systems

BCTL’s payment services are subdivided into 1 of 2 categories: Domestic or International. Domestic payments, in turn, can also be 1 of 2 types, depending on their size: Large Amount or Retail. International payments from the country to the outside and vice versa are always made through the SWIFT system. Domestic payments, especially retail payments, are directly processed in the automated clearing house, two times per day. These payments include salaries, subsidies to veterans, payments to suppliers, which, among others, are processed and transferred to commercial banks. Payments of large sums, above USD 200,000, are always made through the RTGS.

Table **3.1** International and Domestic Payments

(Value in million USD, Quantity in 10^3)

	2020		2021		Change (%)	
National Payments	Quantity	Value	Quantity	Value	Quantity	Value
Automatic Clearing House	575.07	265.70	1,208.29	523.78	110.1	97.1
RTGS-FICT	14.80	4,329.76	14.73	4,015.63	-0.5	-7.3
RTGS-SCCT	77.32	800.23	76.49	1,206.87	-1.1	50.8
Sub Total	**667.19**	**5,395.69**	**1,299.52**	**5,746.27**	**108.58**	**140.69**
International Payments						
Outgoing Transfer-SWIFT	2.48	981.80	1.32	1,088.85	-46.6	10.9
Incoming Transfer-SWIFT	0.20	93.69	0.18	77.77	-8.6	-17.0
Sub Total	2.67	1,075.49	1.50	1,166.62	-55.3	8.5
Total	**669.86**	**6,471.18**	**1,301.02**	**6,912.89**	**53.32**	**149.17**

Source: BCTL

Table 3.1 shows payment statistics, both national and international, during the period under review. With regard to national payments, 1.3 million operations were processed, corresponding to a total of $5,746 million, representing a growth of 109% in number and 141% in value compared to 2020. The significant increase, both in quantity and value, was due to the inclusion of transactions carried out by the automatic clearing house.

On the other hand, within the scope of international payment activities, 1,500 operations were processed, amounting to $1,167 million, which represented a decrease of 55% in terms of number, in contrast to an increase of 8.5% in value, compared to 2020.

The reduction in the level of international transferred quantities was due to the simultaneous decrease in transfers received and sent abroad, which fell by 47% and 9%, respectively.

Table 3.2 also presents data regarding international transactions, corresponding to transfer and receipt transactions carried out by commercial banks in 2021, thus only includes transactions carried out via SWIFT.

Table **3.2** SWIFT Transfers Incoming and Outgoing

(Value in million of USD, quantity in 10^3)

	2020		2021		Change (%)	
	Quantity	Value	Quantity	Value	Quantity	Value
Transfers Incoming						
SWIFT	26.1	289.3	39.7	355.5	51.8	22.9
Non-SWIFT	10.0	183.0	52.9	805.0	429.4	339.9
Sub Total	**36.1**	**472.3**	**92.6**	**1.160.5**	**156.4**	**145.7**
Transfers Outgoing						
SWIFT	14.2	488.1	33.3	906.5	134.1	85.7
Non-SWIFT	55.1	797.7	60.9	807.5	10.7	1.2
Sub Total	**69.3**	**1,285.8**	**94.3**	**1,714.0**	**36.0**	**33.3**
Total	**105.4**	**1,758.1**	**186.9**	**2,874.4**	**77.3**	**63.5**

Source: BCTL

External transfers received and carried out in 2021, via SWIFT, amounted to a total of 39.7 thousand and corresponded to the value of $356 million, thus increasing by 51.8% in number and 23% in value. On the other hand, transfers made via non-SWIFT channels reached a volume of 52.9 thousand, which corresponded to a value of $805 million. This was translated into a significant increase of 429% and 340%, respectively. Meanwhile, transfers abroad totalled 94.3 thousand transactions, amounting to $1,714 million, which resulted in an increase of 36% in terms of quantity, and of 33% in terms of the amount transferred. Transfers of this type via SWIFT were the ones that most contributed to explain the increase in activity, having risen 134% in volume and 86% in terms of value.

3.3.1.3. The P24 System

The P24 system makes use of R-TiMOR interbank network, allowing P24 to automatically settle the net value of each bank's transactions on a daily basis. The main objective in the implementation of the system was to reduce the use of physical cash in our citizens' daily transactions and allow people without bank accounts, or those who are far away from banks, to have electronic means of payment, in addition to cash, accepted in local markets and stores.

Table 3.3 summarizes the evolution of transactions carried out in the P24 system in the country.

Table **3.3** P24 System

(Value in millions of USD, Quantity in 10^3)

	Financial Transactions				Non-Financial Transaction
	Cash Withdrawal		Transfer		Balance Inquiry
	Quantidade	Valor	Quantidade	Valor	
2020	1,423.4	171.6	9.1	4.2	0.5
2021	1,512.1	187.7	22.6	8.0	0.5

Source: BCTL

These figures show the continued significant growth of P24's financial transaction activities in 2021. In 2021, 1.5 million cash withdrawal operations (in kind) were carried out through the P24 system, corresponding to a value of $188 million, which resulted in an increase of 6% in volume and 9% in value. Regarding the level of transfers carried out in P24, 23 thousand operations were registered, totalling $8 million, which corresponds to a significant increase of 148% and 90%, respectively, compared to 2020.

3.3.1.4. The Mosan System Service (E-Wallet)

The Mosan system is an electronic money wallet (E-Wallet) service that allows its users to transfer funds, withdraw and deposit money in their wallets, top up mobile phone balances, make electricity prepayments and consult balances and historic transactions reports.

For prudential reasons, limits have been imposed on the 'Mosan' system, stipulating a maximum balance per account of $500 dollars and the maximum depositable per day at $300 dollars. By the end of 2021, the authorized companies - Telemor and Telkomcel - already had more than 2,648 branches and 97,424 customers in the various municipalities. Mosan Agents, which act as 'transaction points', allow their customers to:

- Transfer and receive funds;
- Deposit and withdraw money;
- Register user/account and update customer information.

'Mosan' thus allows access to basic financial services to citizens of sucos and villages who live far from the main urban centres and to citizens who still do not have the possibility of accessing formal financial services in Timor-Leste.

Table 3.4 summarizes the statistics on transactions carried out by this service in 2021. In 2021 there was an exponential increase in the usage of the system, which confirms its social utility. The total number of transactions was 880 thousand, corresponding to $62 million, which despite the 69% decrease in volume, translated into a remarkable growth of 168% in value, in relation to 2020. Given the expectations regarding network expansion and substantial growth of its customers, these values and volumes are expected to grow materially in the coming years.

Table **3.4** Mosan Service Transaction

(Value in millions of USD, Quantity in 10^3)

	2020		2021		Change (%)	
	Quantity	Value	Quantity	Value	Quantity	Value
Transfer	150.0	15.2	374.2	50.0	149.5	227.0
Cash-in	248.0	3.7	3.4	0.1	-98.6	-98.6
Cash-out	15.0	1.9	298.3	7.9	1,888.9	313.0
Top-up	2,388.0	2.1	8.5	0.2	-99.6	-88.3
Buy data	9.0	0.02	173.7	0.2	1,829.6	956.6
Payment utility	6.0	0.03	21.9	3.5	264.6	11,822.9
Total	**2,817.0**	**23.0**	**879.9**	**61.7**	**-68.8**	**167.5**

Source: BCTL

3.3.1.5. Banking system

The statistics presented in table 3.5 summarize the evolution of transactions in 'kind' (coins or banknotes) and other means carried out by commercial banks in Timor-Leste. The number of 'currency' transactions carried out in 2021 totalled 1.3 million, or 59% of the total number of transactions carried out, with a nominal value of $2,879 million. These figures translate into a 72% decrease in number and a 14% increase in value, compared to 2020. Transactions undertaken via in non-cash means accounted for 41% of the total number of transactions in the country, or 0.89 million transactions, but corresponded to an aggregate value of $1,737 million, or 38% of the total value. These values represent increases of 147% in number and 23% in value, compared to 2020.

Table **3.5** Cash and Non-cash Transactions

(Value in millions of USD, Quantity in 10^3)

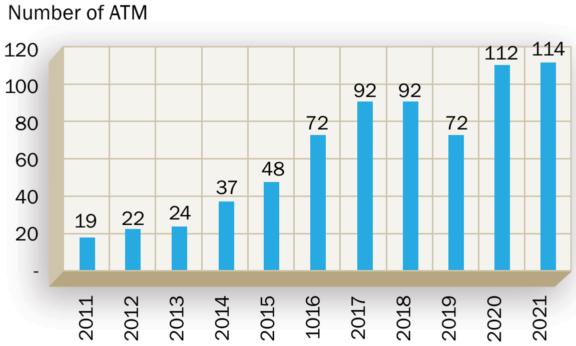
	2020		2021		Change (%)	
	Quantity	Value	Quantity	Value	Quantity	Value
Cash Transactions	4,579	2,520	1,295	2,879	-71.7	14.2
Non-cash transactions	360	1,416	888	1,737	147.4	22.7
Total	**4,939**	**3,937**	**2,183**	**4,616**	**-55.8**	**17.2**

Source: BCTL

BCTL plans and is consistently working towards assuring that the settlement of transactions in the economy becomes progressively more efficient, through the increased usage of electronic payments and digital financial services. Consequently, BCTL continues to prioritize the substantial expansion of the network and range of digital payment services that do not use cash, but instead make use of the national payments system. Specifically, the switch system is increasingly fostering the expansion of payment services, encouraging the widespread use of debit and credit cards, as well as of mobile phones as platforms for making payments.

Chart **3.1**

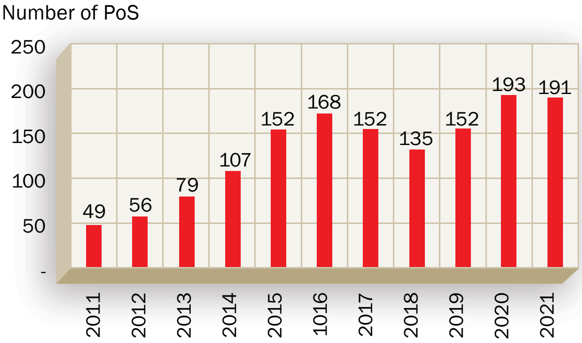
Automatic Teler Machines (ATM)



Source: BCTL

Chart **3.2**

Automatic Point of Sale (PoS)



Source: BCTL

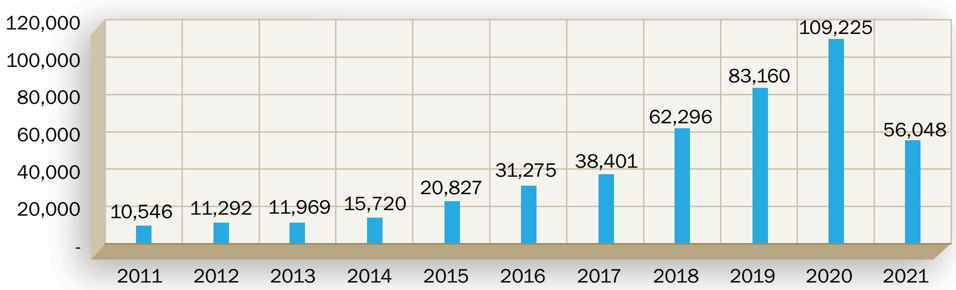
Charts 3.1 and 3.2 depict the evolution of the number of payment terminals installed in the country, including automatic teller machines (ATM), which totalled 114 units in 2021 and 191 units of points-of-sale terminals (PoS). These values, when compared to December 2020, represent an increase of 2% for ATMs and a decrease of 1% for PoS.

The annual evolution of issued bank cards in Timor-Leste can be seen in chart 3.3. In December 2021, the number of active cards in the country totalled around 56 thousand, which corresponds to a decrease of 49% compared to the previous year. Regarding the composition of the total number of debit and credit cards, there was a relevant change against the importance of debit cards, with the number of these cards falling significantly (-49%), after the significant expansion observed in 2020. On the other hand, the number of credit cards grew considerably (173%) compared to 2020, which resulted in an increase in their importance of overall national bank cards.

The continued growth in the number and degree of use of bank cards reflects the effective interest of users in these means of payment and the modernization and increasing digitalization of our financial system.

Chart **3.3**

Number of Credit and Debit Card



Source: BCTL

Box 1: "Campo Digital" National Program

The "Campo Digital" Program is a National Program initiated by the Central Bank to promote the use of digital financial services in Timor-Leste. The Program also aims to expand, in the medium-long term, access points to integrated and interconnected financial services in rural areas, such as the use of digital media (Mobile, ATM and PoS) to carry out financial transactions (payments, transfers and balance inquiries). The program's participants are the financial institutions that are interconnected with the electronic wallet systems within the P24 Network.

The objective of the project is to promote the knowledge and widespread use of these new technological tools in the daily financial activities of the population. The education and familiarization of the rural population with the development of the national payment system and with digital financial services is also one of the objectives of the program. In addition to these objectives, it is also intended to expand, in the medium to long term, the number of access points to integrated and interconnected financial services that will serve rural areas.

On November 29, 2021, the Central Bank celebrated the 7th anniversary of National Savings Day, simultaneously with the launch of the "Campo Digital" pilot program at the Maubisse Administrative Post, in Ainaro Municipality, with the participation of local authorities, representatives of Commercial Banks, Fintech Companies and their agencies, users of financial services, students and the Maubisse community.

The pilot project in Maubisse was frankly positive, benefiting from the efforts of BCTL and the two agents contracted by BCTL to monitor, raise awareness and disseminate the use of existing digital financial systems among the community and local merchants. This success was yet another proof of the project's progress, which mainly aims to enhance the use of electronic wallets (e-wallets). The implementation of the program also allowed the installation of a new P24 ATM in Maubisse, in order to enhance the use of P24 cards in this locality.

On December 20, 2021, the Central Bank also implemented the National "Campo Digital" Program at the Administrative Post of Baguia, in the Municipality of Baucau, preceded by the dissemination of information on digital payments and continued training of Fintech Agents and Customers, in order to facilitate and streamline the payment of salaries at local Fintech agents. This event was attended by the local authority, school principals, civil servants, veterans, companies, e-wallet agents and customers.

At the end of 2021 in Maubisse, the system included 754 customers, 26 "merchants" - retailers that accept payments from electronic wallets, through the QR code scanner or via transfers between accounts - and 11 agencies, having registered a total of 27,561 transactions in the e-wallet system throughout the year.

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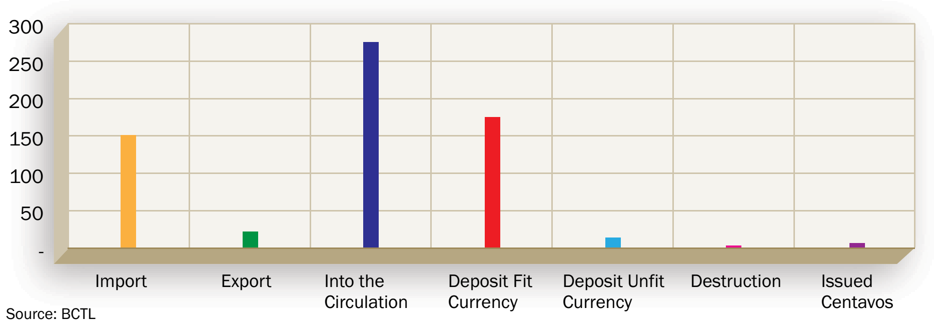
3.3.1.6. Currency Imports and Exports

One of the fundamental functions of the Central Bank is to ensure that the national economy has access to the necessary means of payment to support its economic agents' economic activities, as well as their expected growth. In this regard, the Central Bank effectively fosters the public confidence in the country's currency, by supplying an adequate level banknotes and coins that, at all times, must meet the demand of the public, while also ensuring the physical integrity of notes and coins.

Since the country uses banknotes from another country and its own metallic coins, which are not manufactured in the national territory, supplying the national economy with physical means of payment (coins and banknotes) requires importing them and, in the case of banknotes, when they reach a very low degree of conservation, their re-export to the country of origin, the United States.

Chart **3.4**

TL: Currency Transaction in millions of USD



Source: BCTL

During 2021, BCTL imported $150 million of dollar bills, representing an increase of 37.4% compared to 2020, having issued into circulation a total of $273 million, including coins (cents), which corresponds to a decrease of 41.1% compared to 2020. The issued amount was higher than the imported amount, due to deposits inflows and the existence of reserves. It should also be noted that the 20-dollar bills continue to be the most used in transactions in the country, followed by the 10-dollar denomination.

The 20- and 10-dollar banknotes represented, respectively, 65% and 34% of total imports, 66% and 32% of circulation in the economy, and 66% and 32% of the total (re) deposited ("fit currency") by banks with the central bank (Table 3.6).

Table **3.6** Coin Transactions and Movement

(Value in millions of USD)

Denomination	Import		Re-circulation		Deposit		Peso 2021 (%)			Change (%)		
	2020	2021	2020	2021	2020	2021	Import	Re-circulation	Deposit	Import	Re-circulation	Deposit
100	4.800	0	7.000	1.300	6.900	1.300	0.0	0.5	0.8	-100.0	-81.4	-81.2
50	1.600	0	4.350	1.150	5.650	1.050	0.0	0.4	0.6	-100.0	-73.6	-81.4
20	66.880	97.280	302.641	177.200	257.961	109.547	64.8	66.4	66.0	45.5	-41.4	-57.5
10	33.760	50.560	139.051	85.810	123.411	53.050	33.7	32.1	31.9	49.8	-38.3	-57.0
5	2.160	2.240	3.415	1.455	4.210	1.143	1.5	0.5	0.7	3.7	-57.4	-72.8
	109.200	**150.080**	**456.457**	**266.915**	**398.132**	**166.090**	**100**	**100**	**100**	**37.4**	**-41.5**	**-58.3**

Source: BCTL

As for coins, a total of $6 million dollars were issued into circulation in 2021. The 200-cent coin had a total amount in circulation of 1 million cents. This figure represents a decrease of -62.2% compared to 2020. On the contrary, the 100-cent coin increased by 54% to 2.8 million cents, thus exceeding the value of the 200 and 50 cent denominations. The latter denomination had a value in circulation of 1.5 million cents, amounting to 24% of the total coins in circulation, with an decrease of 4% compared to 2020.

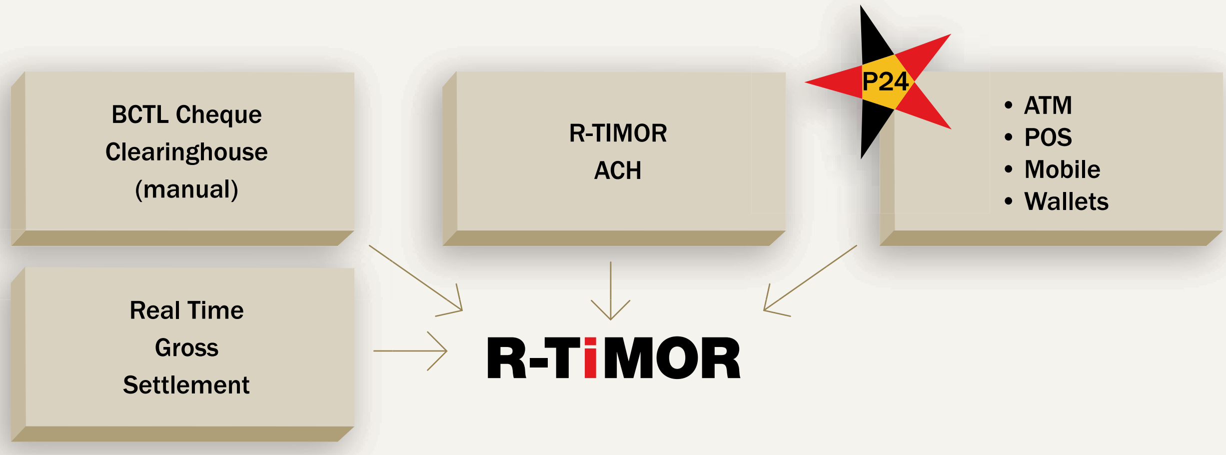
Box 2: Modernization of Timor-Leste's Payment System

1. The R-TiMOR System

The R-TiMOR system, established in 2015, consists in an interconnected network of systems and platforms that allows individuals, companies, State organizations and other entities to make electronic payments in Timor-Leste. The Central Bank continued to play the role of coordinator between the service provider and R-TiMOR users in order to improve services to ensure the existence of an efficient and effective payments system, in particular through the implementation of the Direct Processing module (STP), which ensures that payments are executed in an efficient and secure manner. The STP has already been implemented and is currently used in all commercial banks and in the Ministry of Finance

At the end of 2021, 6 direct participants and 77 indirect participants were registered in R-TiMOR. The number of indirect participants increased by 35% over the previous year. Indirect participants consist of Autonomous Agencies, Municipalities and Special Funds. The system allows indirect participants to process their payments directly using the Government Resource Planning (GRP) system installed at their workplaces.

The Central Bank also continues to coordinate with the R-TiMOR system provider and with the participants the implementation of other necessary improvements to facilitate direct large amount payments, carry out all types of payments to the State (taxes, bids, etc.), from any bank participating in the R-TiMOR.



2. The National Card and the Payment Switch Projects

In March 2017, BCTL hired SIBS International de Portugal to develop and implement the National Card Project and the Interconnection of the Payment System. The interconnector/switch, designated "P24" (the "P" derived from the words 'Pagamentu, Pagamento and Pembayaran'), offers a wide range of financial services and is always available 24 hours a day.

The P24 system went officially live in 2019, with the integration of CGD and Banco Mandiri's ATMs networks during the first phase and allowing customers of each bank to carry out transactions at the ATMs of other banks with the P24 logo.

BNCTL then joined in December 2019 and BRI also joined in early February 2020. Some ATMs from both banks are already integrated into the P24 system, which allows P24 cardholders to carry out financial transactions on the network of ATMs of these banks and other participants in the system.

In 2021, with the collaboration of P24 participants, the Central Bank completed the implementation of the "Mobile Switch" with the P24 system now interconnecting e-wallets, which allows e-wallet customers to now carry out fund transfers from bank accounts to e-wallet accounts and vice versa (B2W2B).

The interconnection of the electronic wallets subsystem with the P-24 system now allows holders of these wallets to transfer funds from their bank account to the Telemor Fintech Lda wallet (Mosan brand) or the Digital Telin Solution Lda wallet (T- Pay), as well as carrying out transfers from wallets to bank accounts (W2B) from the wallets of Telemor Fintech Lda (Mosan) or Telin Digital Solution, Lda.

In October 2021, BCTL also completed the full operationalization of the Tax Payment module through the P24 ATM network, which has always been one of the essential elements and objectives of the National Payment System. This important milestone in the development of the national payment system now allows P24 cardholders of all participating bank customers to pay their taxes electronically, through ATMs with the P24 logo, without having to go to their banks. As the P24 system is also interconnected with the Central Bank's R-TiMOR settlement system, the BCTL then credits the payment of taxes received through R-TiMOR to a State account at the Central Bank. It should also be noted that, for the service to work, banks have to request their customers to exchange their previous bankcards for the new P24 bankcards.

This new tax payment functionality was later jointly launched by BCTL and the Ministry of Finance, in an official ceremony held on 5 March 2021. At the ceremony, the Governor and the Minister of Finance appealed to the business communities, service providers and Timorese citizens to increase the use of electronic payment tools through the P24 network. Providing access to these services has been one of the Central Bank's key strategies to modernize, strengthen and develop the financial sector to support economic growth and one of the Government's priorities to promote "e-government" in the sense of simplifying and facilitating the use of public services and the inclusion of citizens.

At the end of 2021, BNCTL, in collaboration with BCTL, completed the integration of Union Pay International with the P24 system, with the status of "acquisitor". This integration allows international Union Pay cardholders to carry out transactions at BNCTL ATMs in Timor-Leste with the P24 logo.

Since VISA has also been integrated into the P24 system, BNU Timor, in collaboration with BCTL and service providers, has already implemented the use of the "contactless" payment method for its visa cards and the issuance and operation of security protocols "Visa 3D Secure", fully compliant with Visa's operational requirements.

3.3.2. Financial and Banking Systems

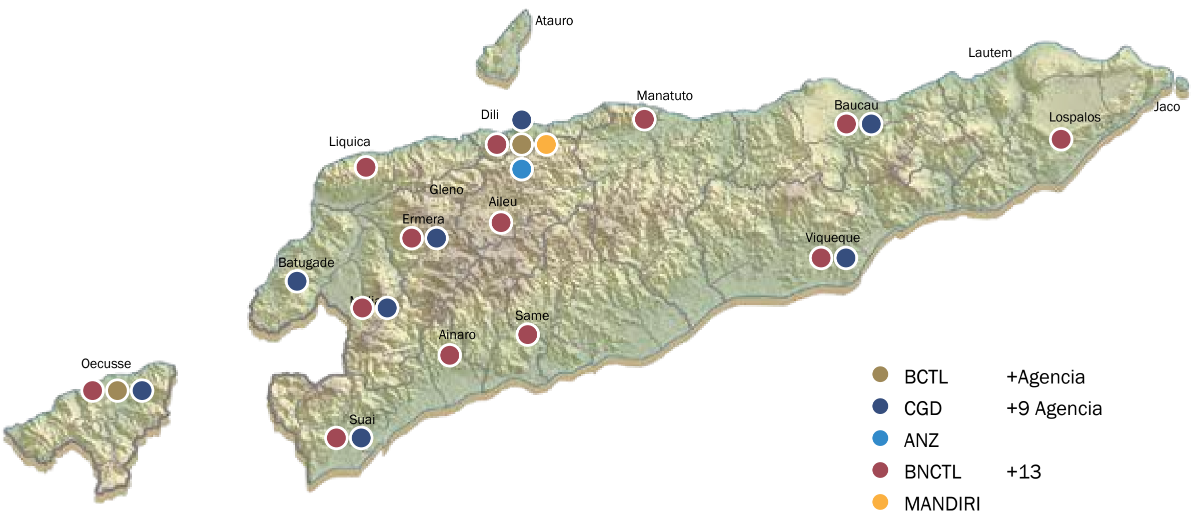
3.3.2.1. Licensing and Supervision

Timor-Leste Financial System is composed by commercial banks, insurance companies, other deposit receiving institutions, money changers and money transfer operators (MTOs), and also several credit unions. The financial system has been stable and robust throughout the year, continuing to significantly contribute to national economic stability

Articles 5 and 29 of Law No. 5/2011 and the Organic Law of the Banco Central de Timor-Leste grant BCTL the exclusive power to regulate, license and supervise all financial institutions. BCTL's Supervision Division is responsible for the licensing and supervision of banks, money changers, insurance companies or insurance intermediaries, other deposits receiving institutions and money transfer operators (MTOs) operating in the country.

During 2021 financial year, this Division submitted to the BCTL's Board of Directors, the approval of two licenses to companies that intend to facilitate the access of the population of Timor-Leste to the financial sector, including a company that intends to offer insurance products in the country and a second company that wants to provide payment services.

Banking Services in Timor-Leste



Box 3: Financial Education Program Implementation

3.1. Financial Literacy Program in Primary Schools

This year, the celebration of the seventh anniversary of the National Savings Day was held at the administrative post of Maubisse, in the municipality Ainaro. The program consisted of carrying out the 1st anniversary of the Campo Digital pilot program, and implementing the digital financial literacy program that combines financial education with the theme of digital payments. The implementation of the digital financial literacy program took place in several elementary schools in the municipality, including mainly students in the 5th and 6th year. The financial literacy materials presented in this program cover topics such as: currency circulating in Timor-Leste and methods of detecting counterfeit money, identifying needs and wants, spending and saving, Ha'u-nia Futuru savings account and introduction to the digital payment systems available in Timor-Leste. The following table presents data regarding the schools and students that attended the financial literacy program.

It should be noted that students from the 2nd cycle of basic education were the main recipients of the financial literacy program, with 267 students from this group actively participating in the program. Additionally, 110 students are in the third cycle of primary education and 70 secondary school students are students specializing in agriculture education.

No	School	Male	Female	Total
1	EBC Rimori	9	17	26
2	EBC Aituto	26	34	60
3	EBC Fleicha	38	35	73
4	EBC Fleicha third cycle	49	61	110
5	EBC Beremoli	33	12	45
6	Agriculture Vocational school	21	49	70
7	EBC Rita	31	32	63
Total		**207**	**240**	**447**

A quiz competition was organized between primary schools that received materials on financial literacy and digital payments. The questions covered topics that were taught, combined with general questions, related to the history or constitution of our country. The Instituto Superior de Cristal also supported the technical assistants in carrying out this competition. Representatives of the Ministry of Education, Youth and Sports, the municipal director of Ainaro, also participated in this activity. The winners of the contest were, from first to fifth place: EBC Aituto, EBC Fleixa, EBC Rita, EBC Riamori and the EBC Beremoli. These winners will receive money, in the form of savings for participating children, to be deposited into their Hau' Nia Futuru accounts.

3.2. National Savings Day

PROGRAMA NASIONAL BA EDUKASAUN FINANSEIRA

"Poupa Agora Diak Ba Futuru"

The celebration of the 7th anniversary of the National Savings Day in Maubisse consisted of the celebration of the first day of the "Campo Digital". This event was attended by guests from the Secretary of State for Cooperative Affairs, municipal authorities, financial institutions, teachers and students, as well as people from other interested parties. At the event, the Central Bank and the Secretary of State for Cooperative Affairs signed a memorandum of understanding for the cooperation in the field of financial literacy for cooperative members.

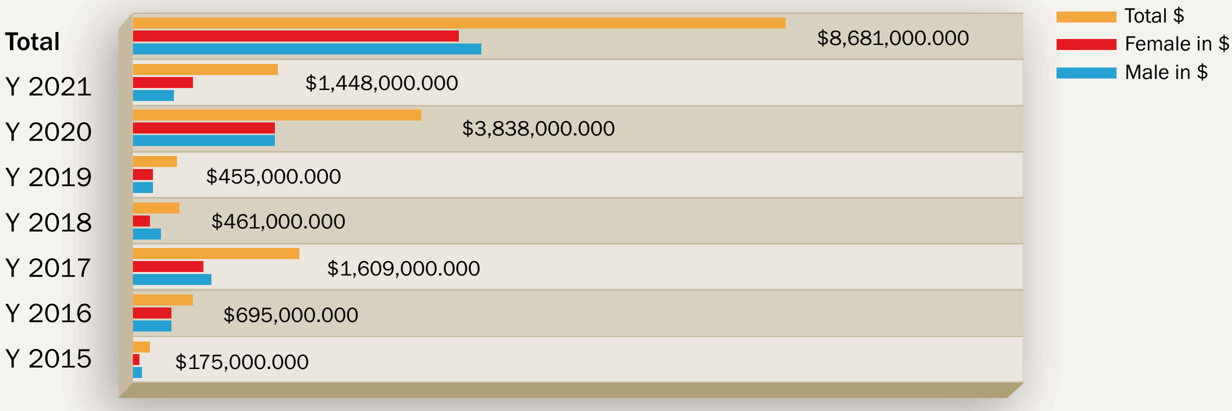
During the celebration, the Central Bank distributed prizes to the winners and awarded certificates to the schools involved in the financial literacy program and the digital field project. The celebration of this event was attended by at least 1,259 people.

3.3. "Ha'u-Nia Futuru" Savings Accounts

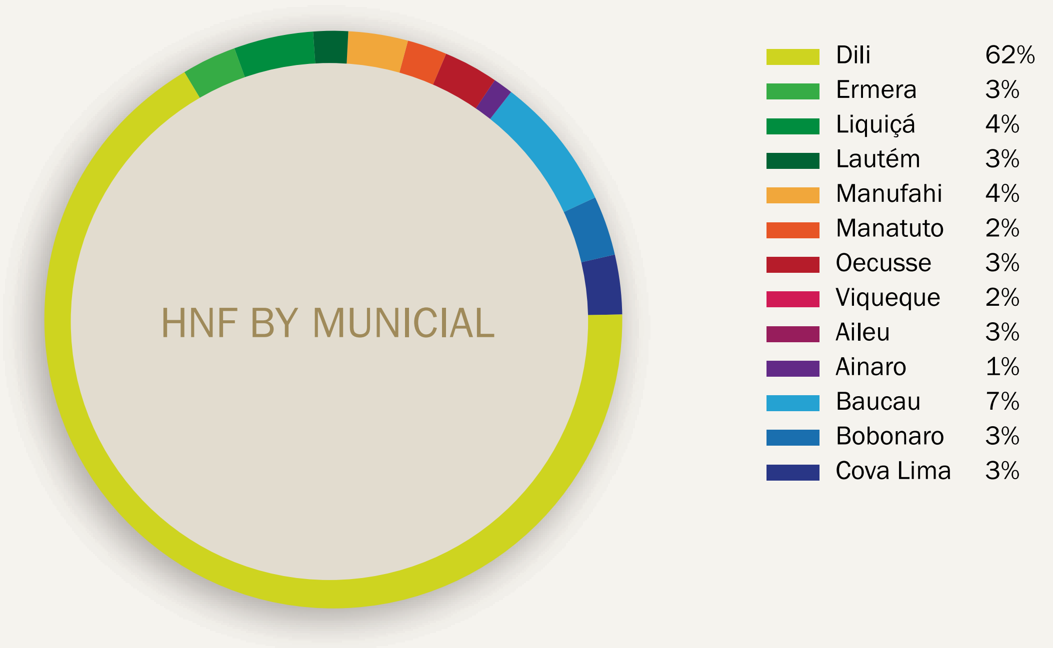
CHILDREN'S SAVINGS ACCOUNTS "HA'U-NIA FUTURU"

The Ha'u-nia Futuru savings program was developed for children up to the age of 17, with the main objective of promoting the formal financial inclusion of children and families. Every month, banks provide BCTL with reports on the progress of Hau Nia Futuru savings program in order to monitor its development. The benefits of these savings are that children only need one dollar (US$1) to open an account, there are no administration fees and they benefit from an annual income of 1.5%. To open this account, only the birth certificate and the parents' ID cards are required.

HNF SINCE THE BEGINNING



From the beginning of the program until the end of 2021, the amount invested in Ha'u Nia Futuru accounts amounted to US$ 8.6 million. Annual data show that in 2021 the savings volume decreased by about 62% to $1.44 million, against the $3.83 million saved in 2020. It should be noted that most of the funds invested in these accounts are concentrated in the capital Dili (62%). The lowest expression was registered for the municipality of Ainaro, which represents only 1% of the total amounts. At the end of 2021, there were 24,352 customers, of which 51% were male and 49% female.



3.4. Cooperation with the Ministry of Education, Youth and Sports

Since the signing of the second memorandum of understanding in early 2020, the Central Bank continues to strengthen its coordination and cooperation with the Ministry of Education, Youth and Sports of Timor-Leste, to define the terms and methods of implementing financial literacy for the basic education, specifically for students from the 1st to the 6th year of schooling.

During the pandemic, a joint team from the Central Bank and the Ministry of Education, Youth and Sports carried out a review of the financial literacy textbook to facilitate teachers' teaching and students' understanding through concrete examples available in their social contexts. The review aimed to make the material more relevant and adapted to the Timorese reality. The complete series includes a book for each school year, with detailed lesson plans, activities, games and exercises to facilitate the learning process.

The financial literacy program aims to introduce financial concepts and prepare students for the future and teaches topics related to spending decisions and the importance of saving for the future. The program requires students to express their levels of knowledge about money and economic terms, use their mathematical skills to solve problems, and reason critically and analytically. The collaboration between the Ministry of Education, Youth and Sports, INFORDEPE and the Central Bank of Timor-Leste has been fundamental in the implementation of this program in all schools in Timor-Leste. The revised financial literacy program book was approved and nominally adopted by the Minister of Education, Youth and Sports and the Governor of the Central Bank.

In addition to this review, the Central Bank and the Ministry of Education, Youth and Sports, through the National Institute for the Training of Teachers and Education Professionals (INFORDEPE), also revised the Teacher Guidance Manual to teach the Literacy Program Financial.

3.5. Formalization of the new MoU with SECOOP

During the celebration of the 7th National Savings Day, BCTL signed a Memorandum of Understanding with the Secretary of State for Cooperatives (SECOOP) within the scope of cooperation in the area of training in financial education, monitoring and supervision of the implementation of the educational program for cooperatives. The main objective of this MoU is to improve the capacity of cooperatives within the field of financial education.

Pursuant to this MoU, BCTL will support SECOOP in defining and delivering financial education training for cooperatives and will support the preparation of materials to support the financial education training activity for cooperatives. The BCTL will also manage, together with the Secretary of State for Cooperatives, training in financial education for cooperatives and, if possible, directly monitor the training of trainers to teach financial education to members of cooperatives selected by SECOOP. BCTL will also prepare training materials and tools for financial education and subsequently support SECOOP in monitoring and supervising the implementation of the financial education program in Cooperatives.

For its part, SECOOP will have the role of appointing qualified trainers to participate in the financial education training and will be responsible for the financial costs necessary for the training and education of the cooperatives carried out by BCTL. In addition, SECOOP should ensure that the BCTL is involved in the training motorization program together with the SECOOP team, if necessary.

SECOOP must also ensure the involvement of SECOOP trainers in the training program or other financial programs carried out by BCTL, free of charge. Upon completion of the training, SECOOP will be responsible for awarding certificates to participants.

3.6. National Financial Literacy Strategy Review

During 2021, BCTL conducted a review of the existing document that guides the National Financial Literacy Strategy program. The national financial literacy program is designed for a period of five years. This program provides guidance to the central bank in carrying out its financial literacy activities. The first program covered the years 2016 to 2020, so it needed to be revised to guide the next five years, from 2021 to 2026.

In the previous five years, the central bank carried out financial literacy activities, such as financial literacy programs dedicated to 1st to 6th grade students, members of small and medium-sized enterprises and cooperatives. In this context, BCTL also sought to disseminate among parents and students the benefits of creating savings for a better future, often done annually during the celebration of National Savings Day. The review of the program was based on dialogues and interviews with various stakeholders from both the public and financial sectors and various non-governmental organizations operating in Timor-Leste.

Institutions interviewed by the BCTL

Institution	Number of Interviews
Bank	5
fintech	2
government entity	3
Insurance	2
money transfer operator	2
international NGO	4
Other deposit-taking institution	2
United Nations Agency (UNCDF)	1
Total	**21**

These interviews sought to assess and include the respective feedback, as well as to assess the participants' knowledge of the various topics taught. The central bank intends to further the involvement these participants, so that more people can benefit from relevant lessons and knowledge in the field of financial literacy.

According to the plan, the BCTL will publish the new strategy document in 2022, after which it plans to proceed with the respective implementation phases.

3.7. Financial Inclusion Report-2020

The financial inclusion report (FIR) must be published by the Central Bank of Timor-Leste every two years. However, there was a slight difference in the 2020 financial inclusion report compared to the previous publication, with the 2020 report now considering supply and demand data.

The report, entitled "Boosting Financial Services Access through Digitalization", highlighted the impact of the modernization of the National Payment Systems in the expansion of access points through the interoperability of ATM and ETFPOS networks, the integration of e-wallet services, as well as the connectivity with international payment systems.

The main conclusions of the report were:

- FIR2020 observed significant improvements in access points in Timor-Leste, resulting from the increased coverage of sucos (cities) with, for the first time, all Administrative Posts being covered by at least one type of financial services access points;
- Exponential growth of e-wallet services from a pilot service in 2018 to more than 3,000 agents and 86,000 registered customers in 2020
- Modernization of the National Payments System: interoperability of e-wallets and connection of e-wallet services to banks, allowing customers to transfer money from bank accounts to their e-wallet accounts
- The use of banking services has increased moderately since 2016. Other deposit-taking institutions and e-wallet service providers recorded higher growth.
- The Timorese Government and BCTL implemented a Credit Moratorium Program in 2020 to support the economy, directly benefiting companies and families affected by COVID-19. The program supported a total of 4,135 entities, most of them individual borrowers.
- A demand-side survey results showed that some bank customers do not know they have a bank account, as they have been forced to open accounts to receive payments from the Government. These customers use their bank accounts as a "mailbox" and do not yet understand the services available.
- The Central Bank launched the "Campo Digital" awareness campaign to promote digital financial services among Timorese in rural and urban areas.

The report evidenced progress in all relevant dimensions of financial inclusion.

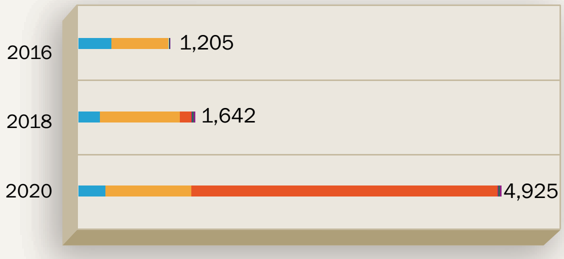
Photo: The first FIR was published in 2016, the second FIR in 2018 and the third FIR in 2020

Photo: The Governor of the Central Bank Mr. Abraão de Vasconselos, at the launch of the financial inclusion report, presented the report to Mr. Phan Thanh Tung, from the Fintech company Telemor MOSAN, for his significant contribution in increasing access points through the presence of his agents in many locations in the country.

Furthermore, access to financial services has significantly improved since 2018. The number of access points has increased by 200%, mainly driven by e-wallet services, with all types of financial services except insurance increasing their number of access points since 2018. The distribution of access points to financial services now covers the 12 municipalities and the RAEOA and, for the first time, all 65 administrative posts. At the suco level, 391 sucos have at least one access point to financial services, but 61 sucos do not yet have any access point. The report also included a coverage map of access points in the country.

Financial Services Access Point Evolution

Financial Services access points tripled in the last two years.
All types of financial services increase the number of access points, except insurance. The e-wallet services had the most significant progress.

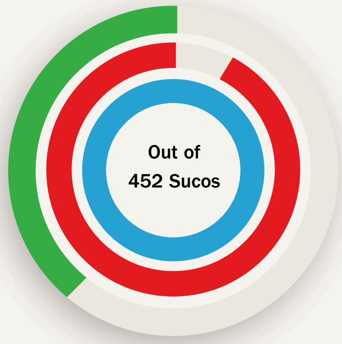


Banks, ODTIs and E-wallet Access Points Coverage by Administrative Posts

Banks, ODTIs and E-wallet Access Points Coverage by Sucos

Banks' access points are limited to urban areas. ODTIs' access points are more widespread than banks. E-wallet's access points are almost everywhere.

25 Bank access points
60 ODTIs access points
65 E-wallet access points



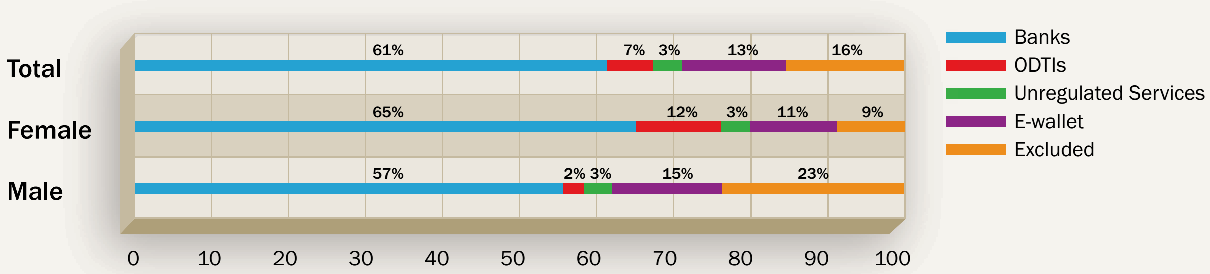
67 Bank access points
284 ODTIs access points
344 E-wallet access points

Bank access points ODTIs access points E-wallet access points

Timorese adults are now using more financial services compared to 2018. At the end of 2020, around 61% of the adult population were bank customers, 7% were ODTI customers, 3% were members of credit unions or multi-sector cooperatives that offered credit and 13% were customers of e-wallet systems. In 2020, around 16% of the adult population was still excluded from all financial services, compared to 35% in 2018. In terms of gender, women use more financial services than men, with the exception of e-wallet services.

In case you want access to this comprehensive report, please find it in the Central Bank of Timor-Leste website at https://www.bancocentral.tl/en/go/financial-inclusion-report. The report addresses the development of financial inclusion in terms of access points, degree of coverage of the adult population, access to credit, frequency of use of customer accounts, means of savings, main reasons for not having a bank account and other topics.

Population Using Financial Services in 2020



3.3.2.2. Insurance Companies

In 2021, the domestic insurance sector continued to be composed by two institutions: SinarMas (SMI) and Federal Insurance Timor (FIT). The sector registered a further progressive improvement in the range of services offered in the country and in the provision of general insurance to the various sectors of activity, at affordable prices and an adequate level of competition.

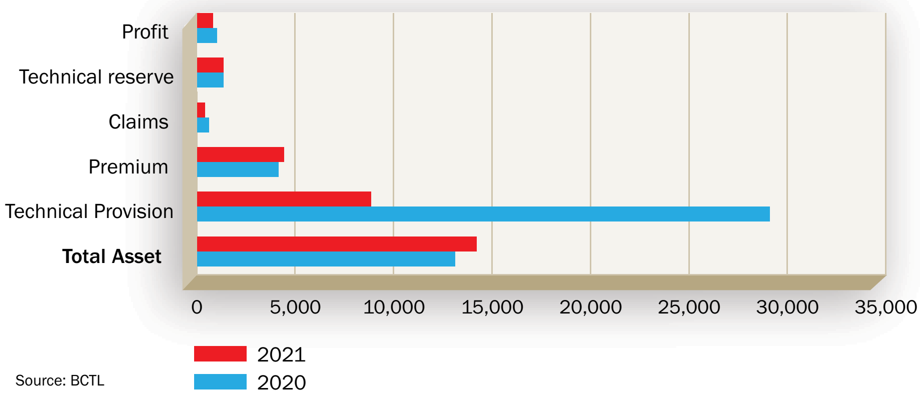
The sector recorded total assets of $14.185 million in December 2021, accounting for a growth of 13.5% compared to 2020, within which liquid funds - cash and bank deposits - constitute the vast majority. In the same year under review, total liabilities increased by 8% to $9 million at year end, a large part of which corresponds to technical reserves and other liabilities. The sector's equity also rose 23% to $5.2 million, largely comprising current and carry-over earnings.

Chart 3.5 illustrates the evolution of the main metrics used to assess the insurance business's annual performance in Timor-Leste.

Chart **3.5**

Insurance Performance

In millions of USD



Source: BCTL

3.3.3. Petroleum Fund Management

According to the framework defined in the Petroleum Fund Law - Law no. 9/2005, subsequently amended in 2011 - the Central Bank continues to be responsible for the operational management of the Fund. According to this legislation, the Ministry of Finance is responsible for defining the overall investment strategy of the Petroleum Fund and the Central Bank is responsible for the operational implementation and specific management of the investment mandates that implement that strategy.

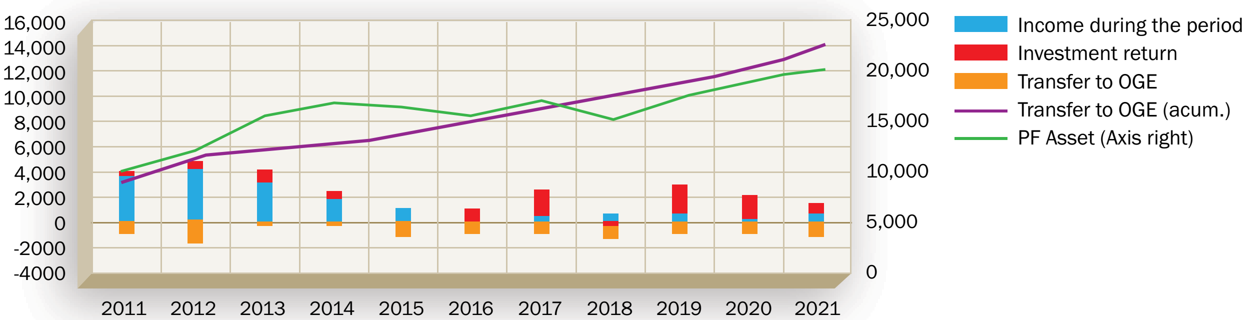
At the end of 2021, the Fund's capital amounted to $19,651 million, an increase of 3.5% compared to the previous year. Annual oil revenues - taxes and royalties - amounted to $717 million, resulting in a significant increase of 231% compared to 2020. On the other hand, PF's withdrawals to finance the annual State Budget were $1,148 million.

In terms of its financial performance, the Fund accumulated a gross income of $1,104 million, which corresponds to approximately 6% of the Fund's value at the end of 2021 ($19,651 million). The breakdown of this income allows us to observe that the income from interest and dividends totalled 1.4% of the Fund's value (1.8% in 2020), while capital gains were 4.3%, resulting in a decrease compared to the substantial capital gains recorded in 2020 (8.2% of the Fund's value).

Chart 3.6

Petroleum Fund Asset Evolution

In millions of USD



Source: BCTL

The Petroleum Fund registered a relevant change in terms of investment strategy in 2021, after the Minister of Finance adopted the recommendation of the Investment Advisory Committee (IAC) to segment the Fund into two sub-portfolios, namely: the liquidity portfolio and the growth portfolio. The liquidity portfolio is invested in highly liquid securities with maturities of less than 3 years, in order to cover the expected withdrawals to finance the State Budgets projected in the next 3 years. The growth portfolio is mostly invested (65%) in fixed income securities and global equities (35%) and is expected to provide a higher potential return for the invested capital.

In 2021, the performance of asset classes for the period under review was mixed, with the global bond portfolio losing -2.25% and equity investments posting again notable gains of 22.7%.

The negative performance of the bond portfolio was due to the increase in interest rates on global sovereign bonds, particularly US Treasury bonds in which the Petroleum Fund is substantially invested. The pandemic situation continued to substantially affect the evolution of the financial markets in 2021, but the development and approval of vaccines by the health authorities at the end of 2020 allowed for a more positive and dynamic in 2021. However, due to initial logistical problems, vaccination rates grew slowly at the beginning of the year, but made significant progress in the second half of the year. However, when vaccination rates improved, the Delta variant emerged, which proved to be more contagious and to cause more severe disease. Consequently, most countries then reintroduced restrictions and border controls to contain the spread of this variant. However, progressively, people began to learn to live with the virus which, together with the rise in vaccination rates, allowed the authorities to gradually ease their social restrictions and facilitate the resumption of economic activities. With the substantial pick-up in global economic demand, inflation picked up and interest rate hikes expectations rose, which in turn led to higher bond interest rates. Additionally, the better prospects for economic growth also led investors to move away from less risky assets (treasury bonds) in favour of riskier assets, with higher potential returns.

The Petroleum Fund's bond portfolio is mainly invested (70%) in US Treasuries with maturities between 3 and 5 years, 15% in US Treasuries between 5 and 10 years and 15% in the global Treasury bonds issued by global developed countries, excluding the US. 5-year US Treasury bonds rates increased 0.90% in 2021, while the 10-year yield increased 0.60%. Similarly, interest rates on sovereign bonds from other countries also increased in 2021. UK 10-year interest rates rose 0.77%, German 10-year yields rose 0.23% and Japanese rates for the same maturity rose 0.05%. Since yields change inversely with bond prices, 2021's generalized rise in rates has caused a widespread fall in global bond prices, especially for US Treasury bonds.

On the other hand, the global stock market recorded a robust return in 2021 supported by several factors: the substantial recovery in economic activity, solid corporate earnings and the extension of main central banks' monetary stimulus programs. The global stock market index (MSCI World) appreciated 20% in 2021, led by the USA, which rose 26.5% in the period, while the European sub-index (ex-UK) was up by 22.6%. This contrasted sharply with the anaemic performance of emerging markets, which registered a marginal loss in the year of -0.2%.

Despite the higher number of COVID infections during the year, people around the world are now better prepared to mitigate and live with pandemic risks. Improving global vaccination rates from mid-2021 onwards has been very helpful in fighting the pandemic. Since the start of the pandemic, governments around the world have expanded their budgetary support, including generous subsidies to households and businesses, to prevent people movements and the spread of the virus. However, consumers were unable to spend these subsidies due to restrictions imposed on business activities and people. The data collected show that overall household savings increased by 7.5% in 2021. When economies reopened, consumers were finally able to spend these savings, which, in turn, supported higher corporate revenues and, naturally, stronger companies' profits.

The economic reopening was not exclusively positive for investors, as it also caused a substantial increase in inflationary pressures. Typically, given a rise in inflation pressures, central banks tend to raise interest rates to prevent the economy from overheating, which is then reflected in the rising cost of financing for private companies, states and consumers. However, major central banks, particularly the US Federal Reserve (FED), considered this initial rise in inflation to be transitory, mostly due to pandemic restrictions and associated with extraordinary workforce shortages and unusually high consumer spending. The Fed believed that as time progressed and restrictions were eased, the workforce would tend to return to the labour market to support the supply response to the substantial recovery in demand. This line of reasoning led the Fed and other major central banks to keep their interest rates unchanged in 2021 to support their respective economic recovery.

3.3.4. Institutional Strengthening

BCTL continues to develop and strengthen the Timorese financial system and modernize banking supervision. The most relevant actions carried out in 2021, relating to the Bank's institutional strengthening program, are highlighted below:

- BCTL established the framework for the Promotion of Financial Markets and the regulation on the issuance and trading of Central Bank certificates.
- It implemented a new Audit Manual, which sets out the procedures related to the internal audit program.
- In order to improve the reporting and prudential reporting of commercial banks and other financial institutions, the Board of Directors approved an instruction to regulate the financial reporting by financial institutions through the BSA.
- It adopted the International Financial Reporting Standards (IFRS) to be applied by commercial banks and other Deposit-taking Institutions (ODTIs) in the presentation of their reports.
- The Board of Directors evaluated a proposal to amend the instruction on Credit Risk Management so that commercial banks can manage their credit risks and simulate the impact of possible macroeconomic risks on their credit portfolios. This instruction was revised based on the principles contained in the previous instruction and on the requirements stipulated by IFRS.
- BCTL operationalized the instruction relating to the classification of credits, regulatory capital, provisions and reserves. This instruction revoked other pre-existing instructions and took into account instruction no. 11/2021 on the adoption of International Financial Reporting Standards (IFRS). Additionally, this new instruction is intended to help enforce appropriate policies and procedures for the timely identification and management of problematic assets, as well as maintain adequate provisions to the effective quality of the respective assets.
- BCTL also enacted the instruction on the classification of insurance activity, namely with the aim of segmenting the licencing and supervision framework for the life and non-life segments within this sector.
- Following-up on the cooperation established with the Griffith University of Queensland in Australia, in 2021 two joint research works were carried out, the publication of which was postponed to 2022, due to the pandemic situation.
- Within the scope of cooperation in the area of financial education training, as well as monitoring and supervision of this training program for cooperatives, BCTL signed a Memorandum of Understanding with the Secretary of State for Cooperatives (SECOOP).

3.3.5. Employees and Training Programs

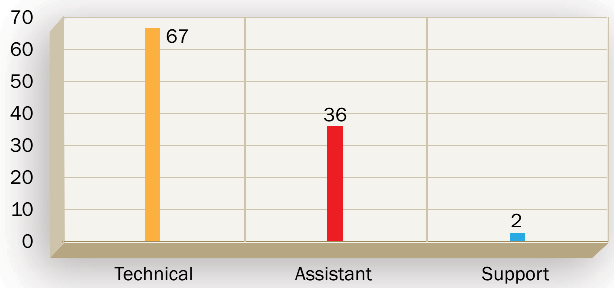
At the end of the period under review, BCTL had 103 employees, which represented a marginal decrease compared to 105 in 2020.

The plan for 2022 intends to move forward with the hiring of 2 new employees to fill the official career positions for legal assistants in the Legal Affairs Division.

The number of BCTL employees, including the 2 employees expected to be recruited in 2022, distributed across the various professional categories, is shown in chart 3.7:

Chart 3.7

Professional Categories



With regard to the Performance Assessment system for BCTL employees, throughout 2021, the vast majority of employees were able to achieve the objectives established by the institution and respective departments and divisions.

The Performance Assessment system is implemented by the various Department managers, with the aim of valuing the work of the respective employees and analysing their contributions towards achieving the BCTL objectives, as planned by each department for the 2021 financial year.

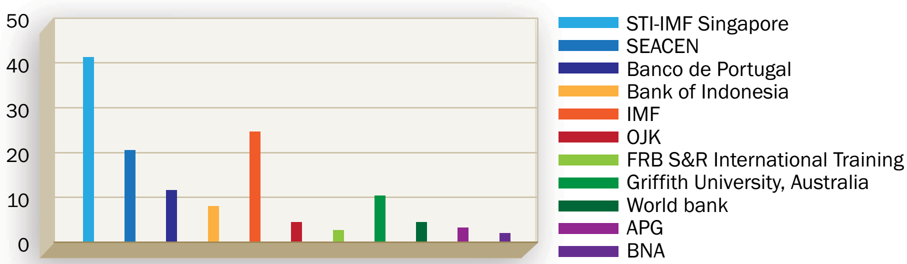
The dimensions used in assessing the performance of employees have remained unchanged from the previous year, as indicated in the diagram below, namely: Objectives, Activities and Skills for technical career employees; and Activities and Skills for assistants and support professionals.

BCTL continues to allocate an appropriate amount to finance the development of skills and knowledge of its employees, who continued to benefit from the participation in seminars and training programs, held both in Timor-Leste and abroad. In addition, BCTL continues to grant scholarships to its employees to attend master's and doctoral courses abroad.

Due to the pandemic situation, all trainings planned for 2021 that required the physical presence of employees, organized by the BCTL, other central banks or international financial institutions, were cancelled. However, some employees and officials managed to participate in the meetings and seminars that still took place, based on videoconferencing or other virtual means.

Chart **3.8**

Number of participants in Courses, Workshops and Virtual activities in 2021



3.3.6. Institutional Partnerships

The “Institutional Cooperation Affairs” Unit continued to develop its cooperation activities with similar institutions and relevant organizations at both the international and national levels. These activities have focused mainly on the areas of technical assistance and the internal capacity building, with the aim of enhancing the effectiveness of the cooperation program, strengthening BCTL institutional partnerships and coordination with other Central Banks.

Most of the cooperation activities between BCTL and its counterparts throughout 2021 continued to be carried out virtually, as in 2020, due to the pandemic. The participation of BCTL in the cooperation activities in 2021 was satisfactory and the degree of participation of BCTL increased significantly compared to 2020. The BCTL and its employees and officials thus continued to participate in the various activities related to meetings, conferences, workshops, seminars and information sharing events, within the most relevant areas of banking activity.

In addition to the natural cooperation with the central banks of the Community of Portuguese Speaking Countries (CPLP), BCTL also continued its cooperation program with other central banks, namely: Bank of Indonesia, Bank Negara Malaysia, Reserve Bank of the USA and Australia, SEACEN, STI-Singapore, APRA and Pacific Islands central banks. This cooperation included the participation in meetings, seminars, conferences and virtual courses organized by the various cooperating entities. Additionally, the BCTL continued its cooperation activities with the Monetary Authority of Macau, currently focused in terms of technical assistance for insurance supervision.

Regarding cooperation at the national level during 2021, BCTL continued to strengthen its cooperation with relevant entities to promote public access to the financial sector. We highlight, in 2021, the signing of a Memorandum of Understanding between BCTL and the Secretary of State for Cooperatives (SECOOP), which aims to frame the partnership for the financial education training to national cooperatives. BCTL also continues to cooperate with the National University of Timor-Leste, providing internships for finalists from its Law Faculty.

With regard to the cooperation with Griffith-Queensland University, Australia, which was established last year, BCTL continued to develop efforts within the framework of ongoing joint economic research projects.

Box 6: BCTL Plan Implementation in 2021 and Action Plan for 2022

6.1. 2021 Plan Implementation

The most relevant BCTL programs carried out in 2021 were the following:

1. In collaboration with the tax authority of the Ministry of Finance, the Central Bank managed to launch, in March 2021, the interconnection between the tax payment system of the Tax Authority and the P24 system, in order to allow bank customers to carry out tax payments from any ATM in the P24 network. In June, BCTL also managed to interconnect the banks' ATM system with the P24 Integrated Management System Terminal (SiGIT), which allows banks to carry out the technical monitoring of the ATMs that are part of the P24 system, improving the efficiency of the technical response to possible operational failures.
2. In November 2021, BCTL as a P24 service provider, in collaboration with BNCTL and "Union Pay International", successfully interconnected the BNCTL system with the "Union Pay International" system. This development now allows Union Pay International customers visiting Timor-Leste to use P24 network ATMs.
   The Central Bank also continues to collaborate with one of the providers of the "Switch" in Indonesia in order to interconnect the national payment system with the regional system. This project is already in the testing phase in the "issuing" aspect (usage tests of P24 cards in the ATMs of the associated members of the GPN network – Gerbang Pembayaran Nasional).
3. The Central Bank continued to collaborate with the Government in the operationalization of the second phase of the credit moratorium program in 2021, which is a public program that aims to boost economic recovery in Timor-Leste.
4. During the year, BCTL implemented other notable programs and initiatives, namely:

a. It managed to interconnect the national switch systems with the mobile switch, allowing the integration of bank account systems with electronic wallets (Mosan and T-Pay) in the P24 system. This integration now allows customers of all banks (except Mandiri, which is in the internal testing phase) and Fintech companies to carry out transfers between their bank accounts and e-wallet accounts.

b. Implemented a new regulatory instruction to regulate the provision of life insurance in Timor-Leste, establishing standards for minimum capital, allowed investment assets and the licensing of insurance companies operating in this segment.

c. Formalized a second agreement with the Ministry of Education, Youth and Sports (MEJD) to improve the implementation, monitoring and evaluation of the financial literacy program in basic education.

d. Carried out the pilot project of the "Campo Digital" at the administrative post of Maubisse, in the municipality of Ainaro. This is a national BCTL program aiming to promote the use of digital financial services in Timor-Leste.

6.2. The Strategic Priorities for 2022

The strategic priorities for 2022 continue to reflect the priorities set in the master plan for financial sector development and the plan for the national payments system.

Promoting Financial Inclusion

BCTL will continue to review the regulatory framework for financial institutions, in terms of liquidity and capital ratios (CAR), asset valuation policies, as well as the adoption of IFRS. BCTL will also complete the legal framework applicable to life and general insurance companies

BCTL will continue to promote stronger financial inclusion through the following programmes:

a. Providing training in accounting (new module of the basic accounting program) for Micro, Small and Medium Enterprises (MSMEs) mainly on productive sectors
b. In 2022 the DDSF team from the financial literacy program for youth will cooperate with Secretary of State for youth and Sport (SEJD)in order to develop the teaching of the program. In addition, training on financial products should also be carried out at youth centres in several municipalities.
c. In 2022 the BCTL team will continue to work together with Training of Teachers and Education Professionals (INFORDEPE) andMEJD to complete the training of basic education trainers (1st and 2nd cycles) who have not yet attended training in Financial Literacy, mainly teachers from the Municipalities of Dili, Viqueque and Covalima.
d. BCTL will improve its training program in accounting practices and book keeping. The team also plans to disseminate the results of this evaluation so that the quality of the program can be assessed and improved.

Promote Digital Financial Services and Develop the Digital Payments System

- The Central Bank will coordinate with commercial banks, Fintech companies and national authorities the launch of the second phase of the pilot project of the “campo digital” in the administrative post of Baguia, municipality of Baucau.
- BCTL will also coordinate with the Government and relevant authorities to promote the widespread use of electronic payments in medium-sized stores and service providers in Dili.

- BCTL will prepare the system rules for Fintech companies that are already part of the P24 system, also including the regulation framework for the supervision of electronic payment services (E-wallet).
- The Bank will also implement the sanctions regime for any undesirable actions by R-TiMOR participants, which will come into effect effectively in 2022, when all participants complete the full implementation of the “Straight Through Processing (STP)” module and other relevant resources. The central bank will also complete the first comprehensive regulatory framework for the national payments system.

- In terms of the “National Switch” system, BCTL will continue to integrate payment services via “e-wallets” and points of sale (PoS, Point of Sales), which have not yet been included in 2021.

- BCTL will complete the full operationalization of the interface between e-wallet operators in 2022, in order to allow financial transfers between different operators’ e-wallets.

- The Central Bank will work together with e-wallet operators in order to continue the discussion and agree on the technological solution to support the “single QR code” within the scope of P24, in order to allow customers to make purchases of goods and services through this code.

- The Bank will also work with EDTL to integrate EDTL's payment system with the P24 network, in order to allow the purchase of electrical "pulsa" through electronic wallets and ATMs.

- BCTL intends to finalize the regional integration of the national payment system, so that customers of banks in the Indonesian GPN network can carry out financial transactions at any P24 ATM in Timor-Leste, and so that customers of banks operating in Timor-Leste can use their P24 cards to carry out financial transactions on the "Prima Network" network in Indonesia.

- The Central Bank will develop and implement a single "Mobile Banking" application, to allow banking transactions to be carried out with any of the banks in the P24 network, which is the last operational phase of the plan to create the modern payment system in Timor-Leste.

- BCTL will finalize the certification of the "Master Card acquiring" and "Union Pay International Issuing" system, in order to allow its future interconnection with the P24. It should be noted that the certification proponents are BNU Timor, in the case of "Master Card" and BNCTL, in the case of "Union Pay International".

- Finally, BCTL will prepare the Standard Operating Procedures manual (SOP) related to the implementation of GPS location in electronic wallet applications, for agents of the 2 national fintech networks.

Promoting Access to Bank Credit

- BCTL will introduce and prepare guidelines to facilitate borrowers' access to emergency credits, allowing that, in the future, if necessary, the respective transfers of funds can be carried out efficiently via "E-wallets".

- BCTL will carry out socialization activities related to credit guarantee system (SGC) regulations and provide training to financial institutions (especially ODTIs) on how to access and use the SGC portal.

- BCTL will work together with BNCTL, KIF and Moris Rasik to operationalize the SIGIT online platform, which will allow its small and medium-sized enterprise (SME's) customers to access credit through this technological solution via web.

Research and Economic Studies

In this area, the emphasis will continue to be on the development of BCTL studies regarding the theme of the national currency, benefiting from cooperation with the Bank of Portugal, which has already presented a study and preliminary survey of the most relevant factors in 2020. This study has been suspended. in 2021, due to the pandemic situation, but it should be resumed in 2022.

BCTL will also continue to carry out economic research projects and studies on issues related to BCTL's main functions and statistics published by the Bank. These works should preferably focus on the following topics:

- Circulation and use of the monetary stock (currency) in Timor-Leste.
- Quantification and impacts of emigrants/immigrants' remittances from the perspective of demand for this type of services and what are the respective effects on the domestic economy. This research project will be jointly developed with Griffith University.
- Inflation drivers in Timor-Leste, also in collaboration with Griffith University.

Strengthening the Management and Investment Capabilities of the Petroleum Fund

- Continue to study and reassess the objectives and investment strategy of the Petroleum Fund and assess the impact on the PF resulting from the operationalization of national Treasury bonds.
- Proceed with the implementation of the Treasury Bonds project. After having already completed the framework for the implementation of this Project, BCTL is already working on the respective legal framework and operational implementation of these securities. These works will also include the implementation of the adaptations and functionalities within the R-TiMOR system to allow the operationalization of Treasury bonds.
- Study and implement the State's treasury management and financing strategy.
- Prepare the legal and operational framework for the issuance of national treasury bonds indexed to inflation "Treasury Inflation-Protected Security (TIPS)", which will be subject to approval by the Ministry of Finance.
- Define and agree with the INSS/RFSS the operational framework for managing the Social Security reserve fund.

Institutional Strengthening and Internal Capacity Development

a) Mobilize Human Resources and Develop Competencies

- Continue to strengthen the technical skills and competences of officials at home and abroad, particularly for those in the technical career. This will be done through the participation in trainings, workshops, seminars and conferences organized by the BdP, BNM, ADB, World Bank, IMF, AFI, PFTC and the Malaysian insurance institution.
- Provide training in Portuguese and English to all BCTL employees.
- Continue to offer employees participation in master's and doctoral scholarship programs.
- Extend the scholarship award program to obtain specific professional certifications - such as the "Chartered Financial Analyst" (CFA) and "Certified Public Accountant (CPA)" - with the aim of strengthening the technical skills of staff in accounting and finance issues.
- Based on the support of a human resources consulting company, carry out an analysis of the personal and professional growth potential of its technical and management staff and define internal policies aimed at fulfilling this potential.
- The BCTL will revise and harmonize the current cyber policies and procedures on current and future cyber threats. BCTL will also conducts security testing towards networks, systems and applications as well as deploying an additional protection and monitoring security.

b) Institutional Cooperation Strengthening

- Participation as a member of the AFI, APG and ASEL committees, and funding the participation of staff in the trainings, seminars and conferences offered in 2022.
- Organize the 7th meeting of supervisors and treasury of CPLP central banks.

Main Governing Bodies of the Central Bank of Timor-Leste (BCTL)

Board of Directors

The Governor
Abraão de Vasconselos

Deputy-Governors
Nur-Aini Djafar Alkatiri
Venâncio Alves Maria

Non-Executive Members
Maria Madalena Brites Boavida
Aicha B.U. Bassarewan
Francisco da Costa Guterres
Benjamin de Araujo Cortereal

Management Committee

The BCTL Management Committee includes all those responsible for the Bank's main organizational areas, as indicated:

The Governor
Abraão de Vasconselos

Deputy Governor
Nur-Aini Djafar Alkatiri

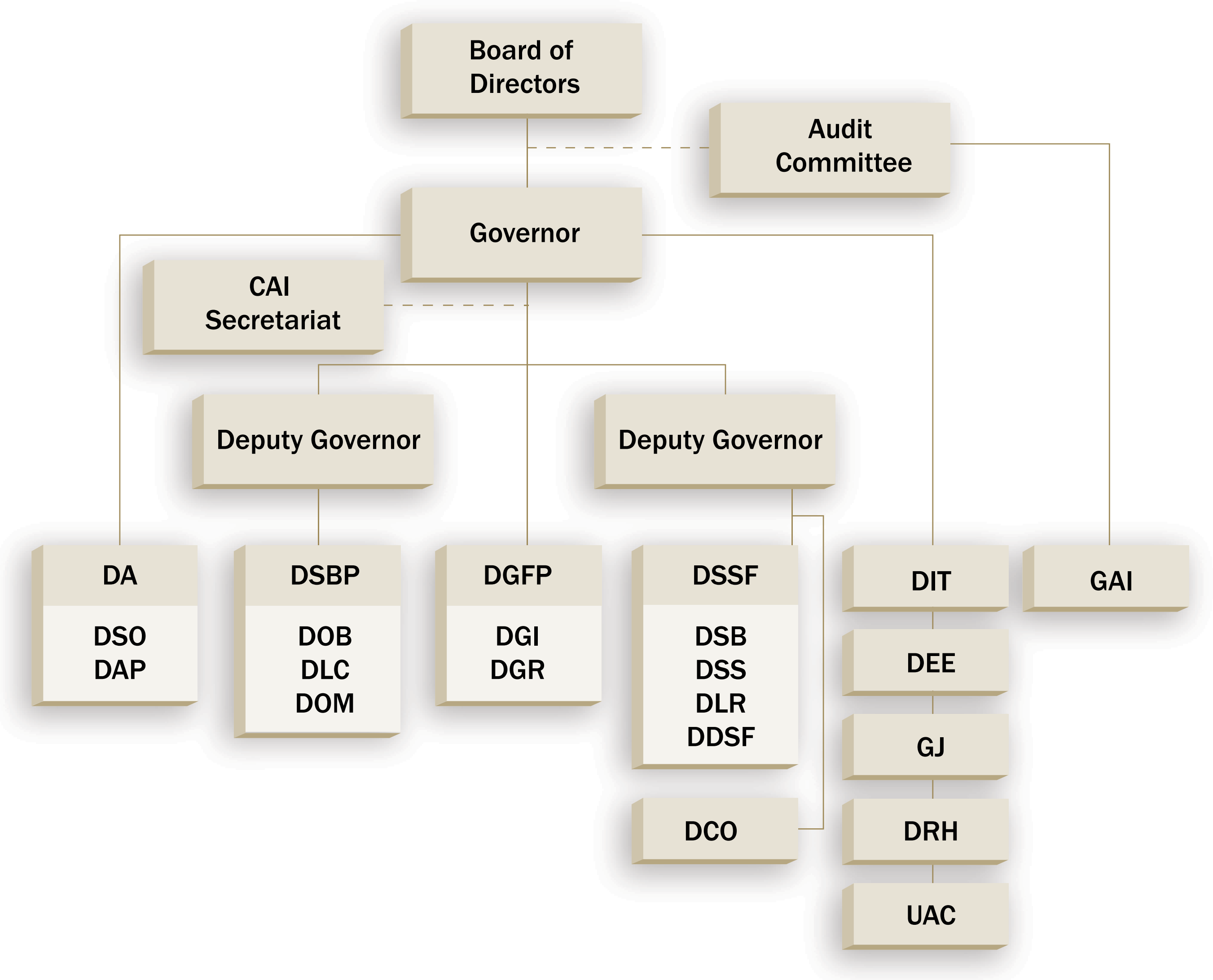
Deputy Governor
Venâncio Alves Maria

Accounting Division Director
Fernando da Silva de Carvalho

Administration Division Director
Maria Ângela de Sousa Soares

Institutional Cooperation Affairs Unit Director
Raquel da Costa Gonçalves

BCTL Internal Organization in December of 2021



Subtitle:

CAI Investment Advisory Committee

DA Administration Department
- **DSG** General Services Division
- **DAP** Provisioning Division

DSBP Department of Banking and Payment Systems
- **DOB** Banking Operations Division
- **DLC** Settlement and Confirmation Division
- **DOM** Operations Division currency

DGFP Department of Petroleum Fund Management
- **DGI** Management Division and Investment
- **DGR** Management Division and Risk

DSSF Financial System Supervision Department
- **DSB** Banking Supervision Division
- **DSS** Division Insurance Supervision
- **DLR** Licensing and Regulation Division
- **DDSF** Financial System Development Division
- **DCO** Accounting and Budget Division

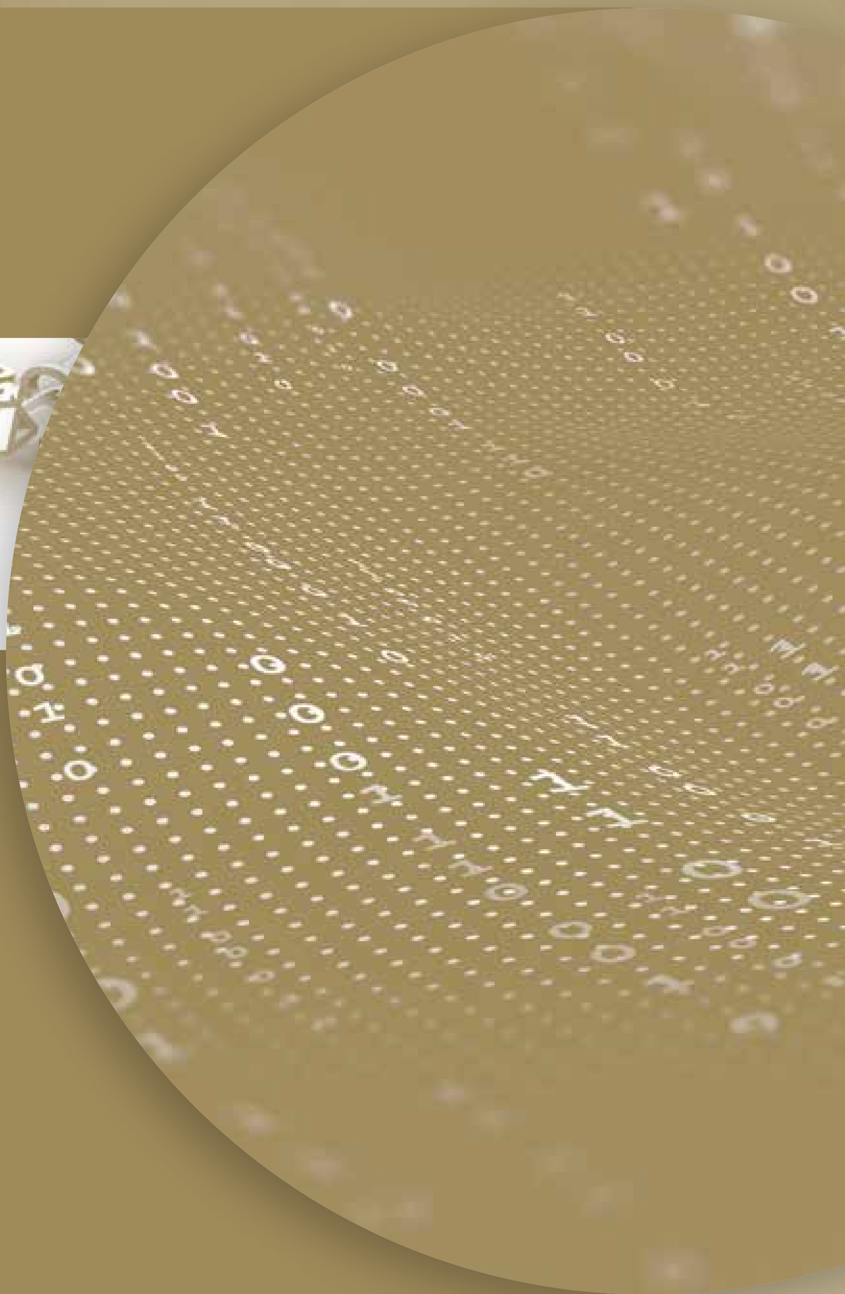
CE Audit Committee
- **GAI** Internal Audit Office

DIT Information Systems Division
DEE Division of Economics and Statistics
GJ Legal Unit
DRH Human Resources Division
UAC Institutional Cooperation Affairs Unit

Financial **Statements**

For the year ended
31 December 2021

31 March 2022



Chapter 4

Statement of Compliance

The Financial Statements on pages 154 to 157 and the Notes from pages 158 to 192 which form an integral part of these statements have been prepared by the Management and approved by the Governing Board of Banco Central de Timor-Leste.

I declare that these Financial Statements comply with the requirements of Central Bank Law no 5/2011 and fairly present the true financial position and performance of Banco Central de Timor-Leste as at 31 December 2021.

Dili, 31 March 2022

Abraão de Vasconselos
Governor

Statement of Financial Position

As at 31 December 2021

In thousands of United States dollars

	Note	2021	2020
Assets			
Cash and cash equivalents	7	665,600	731,717
Financial assets at fair value through other comprehensive income	8	249,327	-
IMF related assets and liabilities	10	68,827	35,488
Other assets	12	4,647	3,217
Property, plant and equipment	11	2,306	2,164
Total Assets		**990,752**	**772,586**
Liabilities			
Government deposits	13	504,420	497,486
Other deposits	14	365,484	167,446
Other Liabilities	15	22,521	11,905
Currency issued		25,805	23,446
Total Liabilities		**918,230**	**700,283**
Capital	16	70,000	70,000
Fair value through OCI		(366)	-
General reserve		762	762
Net profit		2,126	1,541
Total Equity		**772,522**	**72,303**
Total Liabilities and Equity		**990,752**	**772,586**

The above statement is to be read in conjunction with the policies and notes on pages 158 to 192

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 December 2021

In thousands of United States dollars

	Note	2021	2020
Operating Incomes			
Investment Income:			
Interest Income	19	184	1,387
Interest expense	19	-9	-514
Net interest income		**175**	**873**
Petroleum fund management fee	21	16,549	14,531
Petroleum fund administration expenses		-9,195	-7,976
Net fee and commision income		**7,354**	**6,555**
Interest on financial assets at fair value through other comprehensive income	20	144	-
Fees and commissions	22	659	666
Other Income		131	18
Total Operating Income		**8,463**	**8,112**
Expenses			
Personnel expenses	23,26	2,039	2,034
Currency distribution expenses		1,112	987
Administration expenses	24	2,573	2,984
Depreciation	11	613	566
Total Expenses		**6,337**	**6,571**
Profit		**2,126**	**1,541**
Other comprehensive income		-366	-
Total profit and other comprehensive income		**1,760**	**1,541**

The above statement is to be read in conjunction with the policies and notes on pages 158 to 192

Statement of Changes in Equity
For the year ended 31 December 2021
In thousands of United States dollars

	Capital	General reserve	Fair value through OCI	Net Profit	Total equity
Balance at 31-01-2020	**70,000**	**762**	**0**	**6,550**	**77,312**
Profit for the period	0	0	0	1,541	1,541
Other Comprehensive income	0	0	0	0	0
Total Comprehensive income	**0**	**0**	**0**	**1,541**	**1,541**
General reserve	0	0	0	0	0
Capital Increase	0	0	0	0	0
Cash dividends	0	0	0	-6,550	-6,550
Balance at 31-12-2021	**70,000**	**762**	**0**	**1,541**	**72,303**
Balance at 1-1-2021	**70,000**	**762**	**0**	**1,541**	**72,303**
Profit for the period	0	0	0	2,126	2,126
Other Comprehensive income	0	0	-366	0	-366
Total Comprehensive income	**0**	**0**	**-366**	**2,126**	**1,760**
General reserve	0	0	0	0	0
Capital Increase	0	0	0	0	0
Cash dividends	0	0	0	-1,541	-1,541
Balance at 31-12-2021	**70,000**	**762**	**-366**	**2,126**	**72,522**

The above statement is to be read in conjunction with the policies and notes on pages 158 to 192

Statement of Cash Flows

For the year ended 31 December 2021

In thousands of United States dollars

	2021	2020
Cash Flows from Operating Activities		
Profit for the period	2,126	1,541
Depreciation	613	566
Net Interest income	-175	-873
	2,564	**1,234**
Changes in receivables, prepayments & stock	-1,430	3,079
Changes in government deposits	6,933	48,419
Changes in other deposits	164,700	18,672
Changes in other liabilities	10,616	2,425
Changes in fair value	-366	0
	183,017	**73,829**
Interest received	184	1,387
Interest paid	-9	-514
Net cash from operating activities	**183,192**	**74,702**
Cash flows from investing activities		
Acquisitions of investment from financial assets at fair value through other comprehensive income	-249,372	0
Acquisitions of property, plant & equipment	-755	-693
Net cash from/used in investing activities	**-250,127**	**-693**
Cash flows from financing activities		
Currency issued	2,359	2,232
Transfer of surplus to Government	-1,541	-6,550
Net cash from/used in investing activities	**818**	**-4,318**
(Decrease)/Increase in Cash & Cash Equivalents	**-66,117**	**69,691**
Cash & cash equivalents at the beginning of year	731,717	662,026
Cash & Cash Equivalents at the end of the year	**665,600**	**731,717**

The above statement is to be read in conjunction with the policies and notes on pages 158 to 192

1. Reporting Entity and Statutory Base

These are the financial statements of Banco Central de Timor-Leste ("the Bank" or BCTL), a distinct autonomous public legal entity established by Organic Law number 5/2011 on the Central Bank of Timor-Leste. The head office of Banco Central de Timor-Leste is at Avenida Xavier do Amaral, no 9, P.O. Box 59, Díli, Timor-Leste.

The financial statements of the Bank are for the financial year ended 31 December 2021 and, in accordance with section 58 of the Organic Law no 5/2011, the accounts and records are maintained in accordance with International Financial Reporting Standards.

The primary objective of the Bank is to achieve and maintain domestic price stability. The other objectives of the Bank are to foster the liquidity and solvency of a stable market-based banking and financial system, to execute the foreign exchange policy of Timor-Leste, and to promote a safe, sound, and efficient payment system.

The Bank's role is to function as the central bank of Timor-Leste. The functions are defined in the organic Law 5/2011 and other laws, are summaries as the followings:

- to recommend broad policy guidelines to the government in areas under the Bank's responsibility;
- to issue coins called centavos, that have legal tender status in addition to the United States dollar;
- to formulate and implement measures for, and supervise and regulate, payments and settlement systems for transactions in domestic and foreign currency in Timor-Leste;
- to own, operate, or participate in one or more payment systems;
- to act as banker to the government and related agencies;
- to act as fiscal agent of the government and related agencies;
- to hold and manage all public financial resources, including the official foreign exchange reserves;
- to undertake the operational management of the Petroleum Fund of Timor-Leste;
- to hold foreign currency deposits of Commercial Banks;
- to ensure an adequate supply of banknotes and coins for the settlement of cash transactions;
- to maintain a depository for safe keeping of currency and securities;
- to license, supervise, and regulate commercial banks;
- to license, supervise and regulate currency exchange activities;
- to license, supervise and regulate insurance companies and intermediaries; and
- to conduct regular economic and monetary analysis of the Timor-Leste economy, make public the results, and submit proposals and measures to the government on the basis of such analysis.

2. Basis of Preparation

a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by International Accounting Standard Board (IASB).

The financial statements were authorised for issue by the Governing Board on 31 March 2022.

b) Basis of Measurement

The financial statements have been prepared on the historical cost basis except for certain financial assets which are measured at fair value.

c) Adoption of International Financial Reporting Standards

These financial statements incorporate all International Financial Reporting Standards in force at 31 December 2021. No standards have been adopted before the effective date.

d) Functional and Presentation Currency

The financial statements are presented in United States dollars, being the official currency of Timor-Leste and the Bank's functional and presentation currency. Financial information is presented in US dollars rounded to the nearest thousand dollars, unless otherwise stated. This may result in minor differences between accounts reported in the Income statement, Balance sheet and detailed supporting notes.

e) Use of Estimates and Judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in note 5.

3. Significant Accounting Policiess

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

a) Foreign currency transactions

Transactions in foreign currencies are translated into United States dollars at the spot exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated at balance date into United States dollars at the spot exchange rate at that date.

The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the spot exchange rate at the date that the fair value was determined.

The following United States dollar exchange rates have been used to convert foreign currency assets and liabilities to United States dollars for reporting purposes.

	31 DEC 2021	31 DEC 2020
Australian dollars (AUD)	1,3787	1,3139
Special Drawing Rights (SDR)	0,7145	0,6943
Euro (EUR)	0,8810	0,8159

b) Interest Rate Method

Interest income and expense are recognised in the income statement using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument but not future credit losses.

The calculation of the effective interest rate includes all fees and points paid or received transaction costs, and discounts or premiums that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the profit and loss statement include:

- Interest on financial assets and liabilities at amortised cost on using effective interest rate basis

c) Fees

Fee income, including account service fees, cash distribution, and investment management fees, are recognised as the related services are performed. Fee income from government is recognised upon appropriation by parliament and amortised over the period during which the services are provided.

Fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

d) Operating Profit

Operating profit comprises gains net of losses related to trading assets and liabilities, and includes all realised and unrealised fair value change.

e) Taxation

The Bank is exempt from taxes on its income under the provisions of Article 72, Organic Law no. 5/2011.

f) Financial Assets and Liabilities

i) Recognition

The Bank recognises loans, advances and deposits on the date at which they are originated. All other financial assets are initially recognised on the settlement date at which payment is made and title received according to market contractual arrangements.

A financial asset or financial liability is initially measured at fair value plus (for an item not at FVTPL), transaction costs that are directly attributable to its acquisition or issue.

The Bank enters into transactions whereby it acquires assets but does not acquire all the risks and rewards of the assets or a portion of them. Such assets, including assets acquired in connection with the Bank's management of the Petroleum Fund, are not recognised on the balance sheet.

ii) Classification

See accounting policies 3 (g), (h) and (i).

iii) De-recognition

Any interest in such transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability. On de-recognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

iv) Offsetting

Financial assets and liabilities are set off and the net amount presented in the balance sheet when, and only when, the Bank has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

v) Amortised cost measurement

The amortised cost of a financial asset is the amount at which the financial asset is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

vi) Fair value measurement

The determination of fair values of financial assets is based on quoted market prices for financial instruments traded in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets.

vii) Identification and measurement of impairment

At each balance date the Bank recognises an allowance for expected credit losses (ECLs) for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Bank expects to receive, discounted at an approximation of the original effective interest rate.

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

The Bank considers a financial asset in default when contractual payments are 90 days past due. However, in certain cases, the Bank may also consider a financial asset to be in default when internal or external information indicates that it is unlikely to receive the outstanding contractual amounts in full before considering any credit enhancements held by the Bank. A financial asset is written off when there is no reasonable expectation of recovering the contractual cash flows.

The Bank considers evidence of impairment of financial assets at both a specific asset and collective level. All individually significant financial assets are assessed for specific impairment. All individually significant financial assets found not to be specifically impaired are then collectively assessed for any impairment expected for the remaining life of exposure (lifetime ECL). Financial assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets with similar risk characteristics.

Impairment losses on financial assets subsequently measured at fair value through other comprehensive income are recognised by transferring the cumulative loss that has been recognised directly in equity to profit or loss. The cumulative loss that is removed from equity and recognised in profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

g) Cash and Cash Equivalents

Cash and cash equivalents includes notes and coins on hand, unrestricted balances held with other banks, which are subject to an insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments, including the maintenance of a supply of United States currency to ensure an adequate supply of banknotes and coins for the settlement of cash transactions in Timor-Leste.

Cash and cash equivalents are carried at nominal amount in the balance sheet, which approximates fair value.

h) Financial assets

On initial recognition, a financial asset is classified at amortised cost; Fair value through other comprehensive income (FVOCI); Fair value through profit or loss (FVTPL).

Financial assets are classified under these categories on the basis of both the Bank's business model for managing the financial asset and contractual cash flow characteristics of the financial asset.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- The financial asset are held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI).

The debt instruments do not meet the criteria for amortised cost because the Bank's business mode does not require holding the assets to maturity.

A financial asset (debt instrument) shall be measured at fair value through other comprehensive income if both of the following conditions are met:

a. the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and
b. the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

The BCTL holds financial assets in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets. In this type of business model, the entity's key management personnel have made a decision that both collecting contractual cash flows and selling financial assets are integral to achieving the objective of the business model. There are various objectives that may be consistent with this type of business model. For example, one objective of the business model is to manage the BCTL's everyday liquidity needs. To achieve such an objective, BCTL will both collect contractual cash flows and sell financial assets.

The BCTL reserves (debt instruments) meet both conditions (a) and (b) above, and accordingly are classified as Fair Value through Other Comprehensive Income.

Fair value through profit or loss
This is the default classification if the financial assets do not meet the tests for amortised cost or fair value through other comprehensive income. As the BCTL holdings of debt instruments already meet one of the defined classifications, this classification is not applicable.

BCTL classifies debt instruments at FVOCI when both of the following conditions are met:

- The instrument is held within a business model, the objective of which is achieved by both collecting contractual cash flows and selling financial assets
- The contractual terms of the financial asset meet the "solely payments of principal and interest" test defined in IFRS 9.

FVOCI debt instruments are subsequently measured at fair value with gains and losses arising due to changes in fair value recognised in OCI. Interest income is recognised in profit or loss in the same manner as for financial assets measured at amortised cost.

The ECL calculation for debt instruments at FVOCI is explained in Note [3f].

Where BCTL holds more than one investment in the same security, they are deemed to be disposed of on a first–in first–out basis. On derecognition, cumulative gains or losses previously recognised in OCI are reclassified from OCI to profit or loss.

i) International Monetary Fund

The Democratic Republic of Timor-Leste became a member of the International Monetary Fund (IMF) on 23 July 2002. The Bank was designated as the official depository under Article XIII of the IMF Articles of Association. In accordance with article 19 (f) of Organic Law no. 5/2011 the Bank holds the Timor-Leste reserve position subscription in the IMF.

The recognition of the transactions and balances with the IMF follows the indications given by this institution, which consider the specific characteristics of the financial relations of the member countries with the Fund.

The IMF Securities Account reflects the value of a Promissory Note payable by the Ministry of Finance as the fiscal agent of the IMF in Timor-Leste held by the Bank in favour of the IMF.

The Bank recognises an asset and a liability account in relation to the IMF Securities. They are both subsequently measured at amortised cost.

j) Reverse-Repurchase Transactions

The Bank enters into overnight reverse-repurchase agreements in the course of its cash management activities. These transactions are recognised in the balance sheet as cash and cash equivalents, and income is recognised in profit and loss on the transaction date.

k) Other Assets and Liabilities

Local and foreign currency cash, deposits, accounts receivable and payable, are valued at the transaction date, inclusive of any accrued interest.

Accounts receivable are recorded at expected realisable value after making due allowance for doubtful debts.

Unissued currency stocks are recorded as inventory at the cost of acquisition and expensed when issued. They are recorded at the lower of cost or net realisable value. Cost is determined on a weighted average basis.

l) Property, Plant and Equipment

i. Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses.

Cost includes expenditures that are reasonably attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

The land and head office occupied by the Bank is recognised at the cost of acquisition in 2000 at nil value. The Bank still carries these assets at zero value pending the establishment of a fair value at a future time when the land and property market in Timor-Leste operates on a sound legal basis and objective valuations can be derived from observable property market transactions.

ii. Subsequent Cost

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of replaced part is derecognised. The costs of day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

iii. Depreciation

Depreciation is recognised in profit and loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment.

The Bank categorises its assets into broad groups and depreciates them according to indicative useful lives as follows:

	2021	2020
Buildings and improvements	20 years	20 years
Plant	5 years	5 years
Office equipment	8 years	8 years
Computers and electronic equipment	4 years	4 years
Vehicles	5 years	5 years

Depreciation methods, useful lives and residual values are reassessed at the reporting date.

iv. Impairment

The carrying amounts of the Bank's fixed assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset exceeds its recoverable amount. Impairment losses are recognised in profit and loss.

m) Currency in circulation

Currency issued by the Bank in the form of centavos coins (which are legally a sub-unit of the United States dollar in Timor-Leste) represents a claim on the Bank in favour of the holder. The liability for the value of currency in circulation is recorded at face value on the balance sheet.

The Bank also issues collectors' currency. Although it is unlikely that significant amounts of collectors' currency will be returned for redemption, the Bank records the face value of the collectors' currency sold with currency in circulation.

n) Employee benefits

i) Short term employee benefits

A short-term benefits include the full amount of all staff benefits, including salaries and accrued leave. Accruals of personnel costs are recorded in the balance sheet under other liabilities.

Short-term employee benefit obligations are expensed as the related service is provided. A liability is recognised for the amount expected to be paid if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be measured reliably.

ii) Long-term employee benefits
There is no pension scheme for employees of the Bank.

o) Changes in accounting policies

i) Voluntary changes in accounting policies
During the year there were no voluntary changes in accounting policies from the ones used in the preparation of the previous year's financial statements presented as comparative information.

ii) New standards and interpretations applicable in the year
There was no significant impact on the accounting policies and disclosures from the adoption by the Bank of new standards, revisions, amendments and improvements to standards and interpretations which were applicable as from 1 January 2021. These new standards, revisions, amendments and improvements to standards and interpretations are the following:

- Interest Rate Benchmark Reform (Amendments to IFRS 9, IAS 39 and IFRS 7, IFRS 4 and IFRS 16)
- COVID-19 - Related Rent Concessions (Amendment to IFRS 16).

iii) New standards and interpretations applicable in the future years
The following new standards, revisions, amendments and improvements to standards and interpretations are applicable as from 1 January 2022:

- Onerous contracts – costs of fulfilling a contract (Amendments to IFRS 16)
- Annual Improvements to IFRS 2018 – 2020
- Property, Plant and Equipment: Proceeds before intended use (Amendment to IAS 16)

The Bank does not anticipate a material impact on the financial statements when these new standards revision, amendments and improvements to standards and interpretations are applied for the first time.

4. Financial Risk Management

a) Introduction and Overview

The Banco Central de Timor-Leste has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risks
- Operational risks

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and procedures for measuring and managing risk, and the Bank's management of capital.

b) Risk Management Framework

The Governing Board has overall responsibility for the establishment and oversight of the Bank's risk management framework.

The Governing Board is guided by the Bank's establishing law (Organic Law 5/2011), which sets broad risk management guidelines, including the following:

- Article 19 states that the Bank may hold in its investment portfolio any or all the following foreign assets: Gold and other precious metals held by or for the account of the Bank, including credit balances on account representing such gold and other precious metals; Banknotes and coins denominated in freely convertible foreign currencies held by or for the account of the Bank; Credit balances and interbank deposits that are payable on demand or within a short term denominated in freely convertible foreign currencies and are held in the accounts of the Bank, on the books of foreign central banks, or international financial institutions; Readily-marketable debt securities denominated in freely convertible foreign currencies issued by, or backed by foreign governments, foreign central banks or international financial institutions; Claims on international financial institutions resulting from repurchase agreements, sale and buy back and securities lending agreements for the foresaid debt securities; Special drawing rights held in the account of Timor-Leste in the International Monetary Fund; The reserve position of Timor-Leste in the International Monetary Fund.

- Article 71.1 prohibits the Bank from granting credit, engaging in commerce, purchasing the shares of any corporation or company including the shares of any Financial Institution, or otherwise have an ownership interest in any financial, commercial, agricultural, industrial, or other undertaking or acquire by purchase, lease, or otherwise any real rights in or to immovable property, except as it shall consider necessary or expedient for the provision of premises for the conduct of its administration and operations.
- Article 39 authorises the Bank to manage special fund owned by the state on the basis of management contract and maintain earmarked receipts on its books special accounts provided that the assets and liabilities shall be segregated from the other assets and liabilities of the Bank.

The Bank has established an Internal Audit Office, whose duties are to undertake both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Governor, and, at the discretion of the Chief Internal Auditor, the Governing Board.

c) Credit Risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meets its contractual obligations, and arises principally in connection with the Bank's investment and banking activities.

Regular audits of the divisions responsible for the investment of funds are undertaken by Internal Audit.

The Bank's exposure to credit risk, based on the ratings issued by S&P Rating, is as follows:

	Rating*	Dec 2021 US$ "000	Rating*	Dec 2020 US$ "000
Cash and cash equivalents				
Cash	AAA	98,628	AAA	62.432
Deposits at central banks	AAA	530,400	AAA	575,399
Resident banks	Baa2	21,506	BBB-	86,303
Non-resident banks	A-	15,066	A-	7,583
		665,600		**731,717**
Financial assets at fair value through other comprehensive income				
Investment in securities	AAA	249,372	N/A	0
IMF related assets and liabilities				
International Monetary Fund - "SDR"	N/A	68,827	N/A	35,488
TOTAL ASSETS		**983,799**		**767,205**

Summary by credit rating	Dec 2021	Dec 2021 US$ "000	Dec 2020	Dec 2020 US$ "000
AAA	89.29%	878,400	83.14%	637,831
A-	1.53%	15,066	0.99%	7,582
Baa2	2.19%	21,506	11.25%	86,303
Not applicable	7.00%	68,827	4.63%	35,488
TOTAL ASSETS	**100%**	**983,799**	**100%**	**767,205**

*Where a central bank is not rated, the sovereign rating has been used.

There were no impairment losses at balance date.
The carrying amount of these assets approximates their fair value.

d) Liquidity Risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations from its financial liabilities. Liquidity risk is also the risk that the Bank will have to sell a financial asset quickly at much less than its fair value.

The Bank is responsible for managing the daily liquidity of the banking system. This role includes the management of the clearing system. The Bank is prohibited by statute from advancing funds to the banking system.

The Bank's approach to managing liquidity risk is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

The investment management function considers the cash flows historically observed in the deposit accounts of both the government and the commercial banks. From this information, decisions are made that determine the size of the physical cash holdings held in Timor-Leste, the amount of cash to be maintained in correspondent bank accounts, and the nature of the investments to be made in short-term United States Treasury Bills, for which a deep and liquid market exists, such that there will always be bills close to maturity that may be sold if necessary, without incurring the risk of suffering a material market loss.

The following are the remaining contractual maturities of financial liabilities at the reporting date. The amounts are gross and undiscounted and include contractual interest payments and exclude the impact of netting arrangements.

	2021 Carrying amounts US$ '000	"Contractual Cash Flow" 6 months or less	Over 6 months
Cash and Cash equivalents	665,600	665,600	-
Financial assets at fair value through other comprehensive income	249,372	169,982	79,390
IMF related assets and liabilities	68,827	-	68,827
Total assets (Excluding PPE)	**983,799**	**835,582**	**148,217**
Government deposits	504,420	504,420	-
Other deposits	365,484	296,657	68,827
Other liabilities	22,521	22,521	-
Currency issued	25,805	25,805	-
Total liabilities	**918,230**	**849,403**	**68,827**

	2020 Carrying amounts US$ '000	"Contractual Cash Flow" 6 months or less	Over 6 months
Cash and Cash equivalents	731,717	731,717	-
Financial assets at fair value through other comprehensive income	-	-	-
IMF related assets and liabilities	35,488	-	35,488
Total assets (Excluding PPE)	**767,205**	**731,717**	**35,488**
Government deposits	497,486	497,486	-
Other deposits	167,446	131,934	35,512
Other liabilities	11,905	11,905	-
Currency issued	23,446	23,446	-
Total liabilities	**700,283**	**664,771**	**35,512**

e) Market Risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's/issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Bank's approach to the management of market risks is strongly guided by its legislative framework that requires investments to be in high quality financial instruments.

The Bank measures and manages its exposure to market risk in terms of interest rate risk and foreign currency risk, and information on these two risks is provided in the following sections.

i) Interest Rate Risk

Interest rate risk is the risk of loss arising from changes in interest rates.

The Bank's management of interest rate risk is partially governed by the legal framework outlined above, and partly by a management policy of closely matching the re-pricing periods of its assets and liabilities.

The assets and liabilities of the Bank will mature or re-price within the following periods:

	Total Carrying Amount 2021 US$ '000	Non-Interest Sensitive	6 month or less
Cash and cash equivalents	665,600	98,628	566,972
Financial assets at fair value through other comprehensive income	249,372	-	249,372
IMF related assets and liabilities	68,827	68,827	-
Other assets	4,647	4,647	-
Total assets (Excluding PPE)	**988,446**	**172,102**	**816,344**
Government deposits	504,420	-	504,420
Other deposits	365,484	68,827	296,657
Other liabilities	22,521	22,521	-
Currency issued	25,805	25,805	-
Total liabilities	**918,230**	**117,153**	**801,077**
Interest Rate Sensitivity Gap	**70,216**	**54,949**	**15,267**

	Total Carrying Amount 2020 US$ '000	Non-Interest Sensitive	6 month or less
Cash and cash equivalents	731,717	62,432	669,285
Financial assets at fair value through other comprehensive income	-	-	-
IMF related assets and liabilities	35,488	35,488	-
Other assets	3,217	3,217	-
Total assets (Excluding PPE)	**770,422**	**101,137**	**669,285**
Government deposits	497,468	-	497,486
Other deposits	167,446	35,512	131,934
Other liabilities	11,905	11,905	-
Currency issued	23,446	23,446	-
Total liabilities	**700,863**	**70,863**	**629,420**
Interest Rate Sensitivity Gap	**70,139**	**30,274**	**39,865**

ii) Sensitivity Analysis – Interest risk

In managing interest rate risk the Bank aims to reduce the impact of short-term fluctuations on its net income. At 31 December 2021, it is estimated that a general increase/decrease of one percentage point in interest rates would increase/decrease the Bank's profit by approximately $153 thousand (2020 - $399 thousand).

iii) Foreign Currency Risk

Foreign currency risk is the risk of loss arising from changes in exchange rates.

The management of the Bank maintains a low exposure to foreign currencies, which are maintained at levels sufficient to meet operational settlement obligations. The Bank does not engage in foreign currency intervention activities.

As at 31 December 2021, the Bank's net exposure to major currencies was as follows:

	Total 2021 US$ "000	United States Dollars	Australian Dollars	SDR	Euro
Cash and cash equivalents	665,600	661,703	97	-	3,800
Financial assets at fair value through other comprehensive income	249,372	249,372	-	-	-
IMF related assets and liabilities	68,827	-	-	68,827	-
Other assets	4,647	4,647	-	-	-
Total assets (Excluding PPE)	**988,446**	**915,722**	**97**	**68,827**	**3,800**
Government deposits	504,420	504,420	-	-	-
Other deposits	365,484	296,657	-	68,827	-
Other liabilities	22,521	22,521	-	-	-
Currency issued	25,805	25,805	-	-	-
Total liabilities	**918,230**	**849,403**	**-**	**68,827**	**-**
Net Foreign Currency Exposure	**70,216**	**66,319**	**97**	**-**	**3,800**

	Total 2020 US$ "000	United States Dollars	Australian Dollars	SDR	Euro
Cash and cash equivalents	731,717	731,689	7	-	21
Financial assets at fair value through other comprehensive income	-	-	-	-	-
IMF related assets and liabilities	35,488	-	-	35,488	-
Other assets	3,217	3,217	-	-	-
Total assets (Excluding PPE)	**770,422**	**734,906**	**7**	**35,488**	**21**
Government deposits	497,486	497,486	-	-	-
Other deposits	167,446	296,657	-	35,512	-
Other liabilities	11,905	11,905	-	-	-
Currency issued	23,446	23,446	-	-	-
Total liabilities	**700,283**	**664,771**	**-**	**35,512**	**-**
Net Foreign Currency Exposure	**70,139**	**70,135**	**7**	**24**	**21**

iv) Sensitivity analysis - Currency exchange risk

In managing currency exchange risk, the Bank only hold small net positions in foreign currency and therefore it's not materially exposed to changes in foreign exchange rate.

f) Operational Risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks, such as those arising from legal requirements or adverse events in the community at large. Operational risks arise from all the Bank's operations and are faced by all business entities.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management in each business area. This responsibility is supported by the development of standards for the management of operational risk in the following areas:

- Requirements for the appropriate segregation of duties, including independent authorisation of transactions;
- Requirements for the timely reconciliation and monitoring of transactions;
- Compliance with regulatory and other legal requirements;
- Written documentation of all major operating procedures;
- Requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- Requirements for the reporting of operational losses and development of proposed remedial actions;
- Development of contingency plans;
- Ongoing capacity building and professional development;
- Establishment of ethical standards of behaviour; and
- Risk mitigation, including insurance for high risk operations.

Compliance with these standards is supported by a programme of risk-based periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the business area in which they relate, with all findings submitted monthly to the Governor, and a summary of work undertaken submitted quarterly to the Governing Board.

g) Capital Management

The management of the capital of the Bank is subject to organic Law No 5/2011 on the Banco Central de Timor-Leste. In particular, the following requirements are stipulated in the law:

- The capital of the Bank must at least be $20,000,000, fully subscribed and paid-up.
- The capital of the Bank may be increased on the recommendation of the Governing Board and approved by the Government.
- A general reserve account may be established to hold the paid-up capital up to the difference between ten percent of the total financial assets of the Bank.
- The capital of the Bank may not be transferable or subject to encumbrance of any kind.

There have been no material changes in the Bank’s management of capital during the period.

The allocation of capital between specific operations and activities is, to a large extent, driven by the need to provide liquidity to the financial and economic systems of Timor-Leste. Accordingly, a significant proportion of capital is allocated to maintaining physical holdings of currency in Timor-Leste, which earn no interest, and cash balances in current accounts at correspondent banks.

5. Critical Accounting Judgements in applying the Bank's Accounting Policies

Critical accounting judgements made in applying the Bank's accounting policies include:

- Although article 39 of the Organic Law no. 5/2011 states that the Bank is authorised to manage and maintain special funds on its books, the assets and liabilities of which shall be segregated from the other assets and liabilities of the Bank, the management of the Bank, having taken advice concerning the provisions of the Petroleum Fund Law and IFRS, has determined that the liabilities and assets of the Petroleum Fund managed and registered in the name of the Bank should for reporting purposes not be presented on the face of the Bank's balance sheet.
- Management has recognised the classification of the debt instruments at Fair value through other comprehensive income (FVOCI). The bank holds financial assets in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets.

6. Segment Reportings

The Bank's primary function is to act as the central bank of a single geographical area – Timor-Leste. The shares of the Bank are not tradable. Accordingly, the Bank is not required to present segment information.

7. Cash and Cash Equivalents

Cash and Cash Equivalents	2021 US$ "000	2020 US$ "000
Cash	98,628	62,432
Deposits at central banks	530,400	575,399
Resident banks	21,506	86,303
Non-resident banks	15,066	7,583
Total	**665,600**	**731,717**

8. Financial Assets at fair value through other comprehensive income

Designated as fair value through other comprehensive income	2021 US$ "000	2020 US$ "000
US Government Treasury Bills	100,000	-
US Government Treasury Notes	79,390	-
Investment in Fixbis	69,982	-
Total	**249,372**	-

9. Financial Assets and Liabilities

The table below sets out the Bank's classification of each class of its assets and liabilities, identifying the nature and amounts of financial assets and liabilities, with their fair values (excluding accrued interest).

	Fair Value through Profit or Loss		Amortised Cost		Fair Value through Other Comprehensive Income	
Financial Assets	2021 US$ "000	2020 US$ "000	2021 US$ "000	2020 US$ "000	2021 US$ "000	2020 US$ "000
Cash and cash equivalents	-	-	665,600	731,717	-	-
Financial assets at fair value through other comprehensive income	-	-	-	-	249,372	-
IMF related assets and liabilities	-	-	68,827	35,488	-	-
Other assets	-	-	4,647	3,217	-	-
Total assets (Excluding PPE)	-	-	**739,074**	**770,422**	**249,372**	-
Financial liabilities						
Government deposits	-	-	504,420	497,486	-	-
Other deposits	-	-	365,484	167,446	-	-
Other liabilities	-	-	22,521	11,905	-	-
Currency issued	-	-	25,805	23,446	-	-
Total liabilities	-	-	**918,230**	**700,283**	-	-

10. IMF related assets and liabilities

a. International Monetary Fund

The Democratic Republic of Timor-Leste became a member of the International Monetary Fund (IMF) on 23 July 2002. The Bank was designated as the official depository under Article XIII of the IMF Articles of Association. In accordance with article 19 (f) of Organic Law no. 5/2011 the Bank holds the Timor-Leste reserve position subscription in the IMF.

The IMF Securities Account reflects the value of a Promissory Note payable by the Ministry of Finance as the fiscal agent of the IMF in Timor-Leste held by the Bank in favour of the IMF.

The Bank recognises an asset and a liability account in relation to the IMF Securities. The underlying balances of the IMF are denominated as follows:

	2021		2020	
	in SDR '000	in US$ '000	in SDR '000	in US$ '000
IMF Holdings of Currency	21.250	29,742	21,250	30,606
IMF SDR Holdings	27,926	39,085	3,389	4,882
Total	**49,176**	**68,827**	**24,639**	**34,488**

b. The World Bank Group

The Democratic Republic of Timor-Leste became a member of three institutions within the World Bank Group on 23 July 2002. Under the relevant Articles of Association, the Bank was designated as the official depository. In accordance with general practice, the Bank records the outstanding balances with the members of the World Bank Group on a net liability basis. The amounts subscribed are in US dollars, as follows:

International Bank for Reconstruction and Development
The Bank records the outstanding balance with IBRD on a net liability basis.

International Development Association
Timor-Leste has subscribed for $314,858, of which $314,858 has been paid in the form of a Promissory Note held at the Bank.

Multilateral Investment Guarantee Agency
Timor-Leste has subscribed to 50 shares with a total value of $54,100, of which $54,100 has been paid on the form of a Promissory Note held at the Bank.

11. Property, Plant and Equipment

	Buildings US$ '000	Plant US$ '000	Office equipment US$ '000	Computer equipment US$ '000	Vehicles US$ '000	Work in progress US$ '000	Total US$ '000
Cost							
Balance at 1 January 2020	1,317	415	1,068	4,000	593	67	7,460
Acquisitions	-	11	281	32	152	-	476
Adjustment	68	-	-	68	-	-	-
Work in Progress	-	-	-	-	-	216	216
Balance at 31 December 2020	1,385	426	1,349	3,964	745	283	8,152
Acquisitions	-	1	107	341	113	-	562
Adjustment	-	-	-	-	-	-	-
Work in Progress	-	-	-	-	-	193	193
Balance at 31 December 2021	**1,385**	**427**	**1,456**	**4,305**	**858**	**476**	**8,907**
Accumulated depreciation							
Balance at 1 January 2020	822	397	817	2,818	568	-	5,422
Depreciation for the year	65	9	121	355	16	-	566
Adjustment	-	-	-	-	-	-	-
Balance at 31 December 2020	887	406	938	3,173	584	-	5,988
Depreciation for the year	63	8	87	421	54	-	633
Adjustment	19	-	-	1	-	-	20
Balance at 31 December 2021	**931**	**414**	**1,025**	**3,593**	**638**	**-**	**6,601**
Nett carrying amounts							
As at 31 December 2021	**454**	**13**	**431**	**712**	**220**	**476**	**2,306**
As at 31 December 2020	498	20	411	791	161	283	2,164

Pending the establishment of a land and property registration system in Timor-Leste, and the commencement of a property market in which the valuation of commercial and other property can be established by reference to observable transactions, the Governing Board of the Bank has been unable to establish a fair value for the head office land and buildings occupied by the Bank. Work in progress includes costs incurred in relation to the refurbishment of Board meeting room and acquisition of sachet machine. There were subsequently capitalised and transferred to property, plant, and equipment in 2022.

There were no impairment losses at balance date.

12. Other Assets

Other assets comprise the following:

	2021 US$ "000	2020 US$ "000
Other Assets		
Accounts receivable	3,699	2,296
Advance, security & prepayment	314	79
Inventories	634	842
Total	**4,647**	**3,217**

Inventories comprise the cost of unissued centavos coins held for circulation. There were no impairment losses at balance date.

13. Government deposits

Government deposits	2021 US$ "000	2020 US$ "000
Consolidated fund	251,712	305,215
Infrastructure fund	33,030	7,086
Human Development Capital fund	1,724	552
Autonomous agency accounts	96,260	49,340
Municípalities accounts	16,692	1,422
Social security fund	105,002	133,871
Total	**504,420**	**497,486**

14. Other deposits

Other deposits	2021 US$ "000	2020 US$ "000
Domestic financial institutions	296,657	131,934
International financial institutions (Note 10a)	68,827	35,512
Total	**365,484**	**167,446**

15. Other Liabilities

Other Liabilities	2021 US$ "000	2020 US$ "000
Accounts payable	3,862	2,437
Withholding tax payable	59	104
Provision for Long service account	552	375
Letters of Credit	10,733	269
Operating accounts	7,315	8,720
Total	**22,521**	**11,905**

16. Capital and Reserves

The capital of the Bank is maintained at $70,000,000 (2019 - $70,000,000).
The following reserves are established by article 10.1 of the organic law:

- An amount equivalent to at least 50 percent of distributable earnings shall be credited to the general reserve account until the capital and general reserves equal 10 percent of the total financial assets of the Bank.
- A part of the remaining distributable earnings may, on the proposal of the Governing Board, approved by the Government, be credited to special reserve accounts that may be established by the Bank pursuant to paragraph 4 of Article 8 until such reserve accounts reach a sum that the Governing Board deems appropriate.
- After deduction of the amounts referred to in the previous sub-paragraphs (a) and (b), the remaining distributable earnings shall be used to redeem any securities issued by the Bank, the remainder being transferred to the Treasury as revenue for the general budget of the State.

17. Provision for Transfer of Surplus to Government of Timor-Leste

Article 9 of the organic law no. 5/2011 on the Banco Central de Timor-Leste requires that the net profit of the Bank, after statutory deductions to the General Reserve Account and the Supplementary Reserve Account shall be transferred to the Government of Timor-Leste.

Furthermore article 10.1 (a) of the organic law no. 5/2011 stated that an amount equivalent to 50 percent of distributable earnings shall be credited to the general reserve account until the capital and general reserves equal 10 percent of the total financial assets of the Bank, a transfer to the Government will be made as follows:

	2021 US$ "000	2020 US$ "000
Transfer to Government		
Balance of General Reserve Account	0	0
Net profit for the year ended 31 December 2021	2,126	1,541
Transfer to General Reserve Account	0	0
Total	**2,126**	**1,541**

Since 2020, the Bank has not transferred 50% of the distributable earning to reserve account on the basis of the Government's commitment to increase the Bank's capital to $100 million. The Bank will transfer the profit for the year 2021 (2020 – transferred to Government in early May 2020) to Government, when the Governing Board approved the distribution of earnings.

18. Contingent Liabilities

There were no contingent liabilities as at 31 December 2021.

19. Net Interest Income

	2021 US$ "000	2020 US$ "000
Interest income from Financial Assets		
Interest on deposits at foreign central banks	173	1,313
Interest on deposits at domestic banks	11	74
Total interest income	184	1,387
Interest paid on Financial Liabilities		
Interest paid on Government accounts	9	512
Interest paid to commercial banks	-	2
Total interest expenses	**9**	**514**
Net Interest Income	**175**	**873**

20. Interest on financial assets at fair value through other comprehensive income

	2021 US$ "000	2020 US$ "000
Interest on financial assets at fair value through other comprehensive income		
Interest on financial assets at fair value through other comprehensive income	144	-
Total interest	**144**	**-**

There is no impairment on the financial assets at fair value through other comprehensive income during the year (2020 – nil).

21. Fee and Commission Income

	2021 US$ "000	2020 US$ "000
Fees and commissions		
Currency withdrawal fees	7	8
Licensing and supervision fees	152	158
Government account management fees	500	500
Total fees and commissions	**659**	**666**

22. Petroleum Fund Management Fee

In accordance with the provisions of the Petroleum Fund Law No 9/2005 the Bank is entitled to charge a management fee for the operational management of the Petroleum Fund of Timor-Leste that reasonably represents the cost of managing the Petroleum Fund. The balance of Petroleum Fund on 31 December 2021 (unaudited) was $19,651 million (2020 – $18,991 million).

Ministry of Finance agreed to cover internal management fee of BCTL up to 4 basis points on an annual basis. The management fee received from the Petroleum Fund account for the period ended 31 December 2021 amounted to $16,549 thousand (2020 – $14,531 thousand or 8 basis points) or represented 8 basis points of the average balance of the funds. The fees cover expenses for custody services and external managers, Investment Advisory Board, and the fees for BCTL internal management. Presented below is the petroleum fund management fee income by nature:

	2021 US$ "000	2020 US$ "000
Total Petroleum fund management fee income	**16,549**	**14,531**
External managers & custody mgmt services	-9,103	-7,814
Investment Advisory management expenses	-92	-162
Others	0	-582
Net fee and commission income	**7,354**	**5,973**

The BCTL internal fees receipts from the management of the fund was $6.4 million (2020 - $5.9 million) which allocated to expenses as shown below.

	2021 US$ "000	2020 US$ "000
Salary, capacity building and Other personnel related costs	1,287	1,195
IT services, systems and data	2,060	1,911
Research, consulting and legal fees	1,609	1,493
Allocated common costs BCTL	1,159	1,075
Other costs	322	299
Total BCTL operational expenses	**6,437**	**5,973**

23. Personnel Expenses

	2021 US$ "000	2020 US$ "000
Personnel Expenses		
Salaries and related payments	1,988	1,863
Staff welfare payments	48	185
Capacity building and staff development	3	11
Representation at conferences and meetings	-	2
Total personnel expenses	**2,039**	**2,034**

24. Administration Expenses

	2021 US$ "000	2020 US$ "000
Administration Expenses		
Asset maintenance	29	89
Communications	72	125
Information systems	1,426	1,664
General expenses	43	45
Office Expenses	244	226
Professional fees	593	619
Other Assets management expenses	166	216
Total Administration Expenses	**2,573**	**2,984**

25. Petroleum Fund of Timor-Leste

The Bank is responsible for the operational management of the Petroleum Fund of Timor-Leste in accordance with Law number 9/2005 on the Petroleum Fund Timor-Leste and an Operational Management Agreement signed between the Bank and the Minister of Finance.

Under those arrangements, the following mechanisms have been established by the Bank:

- An "earmarked receipts account" has been opened by the Bank in its own name at the Federal Reserve Bank of New York into which all payments made as petroleum receipts must be made.
- The investments of the Petroleum Fund and related custodial arrangements are made in the name of the Bank.
- The Bank is not liable for losses arising from the operations of the Petroleum Fund unless such losses arise from the negligence of the Bank or its employees.

Taking into account the recognition tests set out in international accounting standards, the assets and liabilities of the Petroleum Fund are not shown on the face of the Bank's balance sheet.

The assets and liabilities of the Petroleum at 31 December 2021* were as follows:

	2021 US$ "000	2020 US$ "000
Petroleum Fund Assets		
Cash and Cash Equivalents	1,379,487	1,361,477
Other receivables	4,730	17,247
Financial assets at fair value through profit or loss	18,280,950	16,943,356
Financial assets at Amortised Cost	0	701,350
Less: Pending Purchase of Securities	-14,490	-32,849
& Account payables	**19,650,677**	**18,990,581**
Capital	19,650,677	18,990,681
Capital	**19,650,677**	**18,990,581**

Notes: **) the PF balance sheet is unaudited*

26. Related Party transactions

Ultimate Controlling Party

The capital of the Bank is held by the Democratic Republic of Timor-Leste and carries no voting or other rights of control. The Bank is established as a distinct autonomous public legal entity, endowed with administrative and financial autonomy and of its own capital. Article 3.2 of Central Bank law no. 5/2011 gives the Bank complete legal, operational, administrative, and financial autonomy from any other person or entity, including the government and any of its agencies, and subsidiary organs or entities.

Governing Board

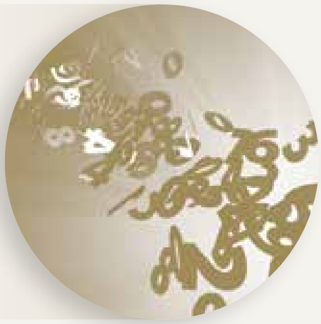
There were three members of the Governing Board who were the executive management personnel. The compensation is determined by the Government through Government Decree No. 3/2015 of 21 January, which is disclosed below.

	2021 US$ "000	2020 US$ "000
Executive Board members Compensation		
(Included in personnel expenses)		
Short-term employee benefits	242	260
Long-term benefits	17	17
Total	**259**	**277**

Non-Executive Governing Board

There were four members of the Governing Board who were not one of the key management personnel, whose compensation is disclosed below.

	2021 US$ "000	2020 US$ "000
Non-Executive Board members Compensation		
Sitting allowance		
(Included in personnel expenses)	77	68
Total	**77**	**68**



Key Management Personnel

The management of the Bank is undertaken by a Management Committee comprising the three-senior staff.

	2021 US$ "000	2020 US$ "000
Key Management Personnel Compensation		
(Included in personnel expenses)		
Short-term employee benefits	71	72
Long-term benefits	5	6
Total	**76**	**78**

Government-Related Entities

The Bank provides banking services on an arm's-length basis to the Ministry of Finance and other public entities which are exempt from the disclosure requirements of paragraph 18 of IAS 24 – "Related Party Disclosures" in relation to related party transactions and outstanding balances, including commitments. The nature and amount of each individually significant transaction with Government related entities are disclosed in Notes 13, 15, 23 and 26.

27. Authorisation and approval of the financial statements

As stated in the basis of preparation - Statement of compliance, these financial statements were authorised for issue by the Governing Board of the Bank on 31 March 2022.

28. Subsequent Events

The COVID-19 pandemic developed rapidly in 2020, with a significant number of cases. Measures taken by the governments to contain the virus have affected economic activity. The Bank have taken a few measures to monitor and mitigate the effects of COVID-19, such as safety and health measures for our people (such as social distancing and working from home).

At this stage, the impact on the business and results has not been significant. The bank will continue to follow the government policies and advice and, in parallel, the bank will do to continue operations in the best and safety way possible without jeopardising the health of the people.

At this moment, there were no subsequent events have occurred after the reporting date and the date of the issuance of the financial statements.

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INDEPENDENT AUDITOR'S REPORT

To the Governing Board of Banco Central de Timor-Leste (the Bank)

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Banco Central de Timor-Leste (the Bank), which comprise the statement of financial position as at 31 December 2021, the statement of profit or loss and other comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion the accompanying financial statements of the Bank:

(i) Give a true and fair view of the Bank's financial position as at 31 December 2021 and of its financial performance and its cash flows for the year ended on that date; and

(ii) Complies with the International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with the ethical requirements of the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Timor Leste. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of the Bank's Governing Board for the Financial Statements

The Bank's Governing Board is responsible for the preparation of the financial statements that gives a true and fair view in accordance with the IFRSs and for such internal control as the Governing Board determines is necessary to enable the preparation of the financial statements that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Governing Board is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Governing Board either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional skepticism throughout the planning and performance of the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control;

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

We are required to communicate with the Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

BDO

BDO Australia Ltd

Clive Garland
Audit Partner

Darwin, 13 April 2022