International Monetary Fund

IMF Concludes 2016 Article IV Consultation Mission to Timor-Leste

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An International Monetary Fund (IMF) team led by Ms. Yu Ching Wong visited Timor-Leste from February 1–12 to hold Article IV consultation discussions. The team met with Minister of State, Coordinator of Economic Affairs and Minister of Agriculture and Fisheries Estanislau da Silva, Minister of Public Works, Transport and Communications Gastão de Sousa, Minister of Petroleum and Mineral Resources Alfredo Pires, Central Bank Governor Abraão de Vasconselos, Deputy Minister of Finance Helder Lopes, members of Parliament, and other senior officials. The team also held discussions with development partners as well as representatives of the private sector and civil society.

At the conclusion of the mission, Ms. Wong made the following statement:

"Although the recent fall in global oil prices has weakened overall macroeconomic prospects of oil exporters, Timor-Leste has been cushioned by the prudent saving of its oil wealth in the Petroleum Fund. Non-oil GDP growth is estimated to have moderated to 4.3 percent in 2015 from 5.5 percent in 2014, due to weaker government spending. CPI inflation eased to around 1 percent in 2014 and 2015 from double-digit increases in previous years, reflecting lower commodity prices, a stronger U.S. dollar, and an improvement in supply bottlenecks. Preliminary indicators point to the fiscal position slipping into an overall deficit of around 6 percent of GDP in 2015 due to lower global oil prices, declining oil production, and lower returns on the Petroleum Fund's investment portfolio amid global financial market uncertainties. The external current account surplus was halved to 24.4 percent of GDP in 2014 and is estimated to have shrunk further to 4.3 percent of GDP in 2015 due to declining oil and gas receipts and lower investment returns. Private credit growth picked up to 10.5 percent in 2015. Average non-oil real GDP growth in the medium term is projected at around 6 percent, supported in part by an increase in foreign direct investment.

"The mission welcomes the authorities' continued commitment to a transparent and accountable fiscal framework that has allowed oil revenues to be saved through the Petroleum Fund which is a source of confidence for the economy. However, fiscal consolidation measures are needed to safeguard long-term fiscal and debt sustainability and the assets of the Petroleum Fund should be preserved to provide an adequate stream of investment incomes for future generations. Achieving fiscal sustainability requires prioritization of public investment through rigorous investment appraisal and taking into account existing bottlenecks and absorptive capacity constraints, rationalizing recurrent spending, strengthening non-oil revenues, and adhering to a medium-term fiscal consolidation plan.

"The mission supports the government's intention to tap more concessional borrowing to finance large infrastructure projects if the borrowing cost is lower than the opportunity cost of tapping into the Petroleum Fund. Such borrowing would come with the discipline of debt sustainability monitoring by creditors and the transfer of knowledge by these multilateral or bilateral institutions.

"In the same vein, domestic revenues need to be mobilized to reduce the reliance on excess withdrawals from the Petroleum Fund. Ongoing work by the Fiscal Reform Commission on tax reforms is a step in the right direction to achieve the government's domestic revenue target of 15 percent of non-oil GDP by 2020.

"The mission welcomes the progress in promoting financial inclusion, including through the introduction of branchless banking facilities. However, efforts to enhance financial inclusion will need to strike a balance with safeguarding financial stability. Recent milestones in the installation of the Automatic Payment System constitute major steps toward more efficient and secure interbank payments. Overall, commercial banks' operations are sound and the central bank is strengthening its capacity in banking supervision, supported by development partners. Banco Central de Timor-Leste's plan to enhance its role of lender of last resort with clear protocol and appropriate legal framework is commendable. Steps have also been taken to implement the Financial Action Task Force's guideline to safeguard anti-money laundering and combating the financing of terrorism (AML/CFT).

"Medium-term growth will depend crucially on economic diversification, and this has gained added urgency in light of falling oil production in existing fields and the associated reduction of fiscal resources. Continuing efforts to improve human capital formation through investment in health and education, including strengthening vocational education would also help to lift potential growth. An enabling business environment and measures to boost competitiveness are also needed to catalyze private sector development. Timor-Leste, with its young labor force, is well-placed to take advantage of global and regional integration trends including its application to ASEAN membership. To maximize benefits from these opportunities, the private sector should leverage comparative advantages in line with Timor-Leste's fundamentals, by expanding labor-intensive sectors such as agriculture and tourism.

"The team thanks the authorities and other counterparts for their hospitality, strong engagement, and candid exchange of views."

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