



2016 Article IV Consultation Outreach Seminar

IMF Timor-Leste Team
Dili, Timor-Leste
February 11, 2016

Outline

- World Economic Outlook
- Key Recommendations of 2016 Article IV Consultation
- Cross-cutting Issues
 - Financial Inclusion
 - Economic Diversification

World Economic Outlook

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Subdued demand, diminished prospects

Continuing uneven recovery, with a more gradual pick-up in activity in 2016

- AEs asynchronous monetary policy (U.S. tightening; EA and Japan loosening)
- Continuing weaker prospects in EMs (rebalancing in China; low commodity prices)

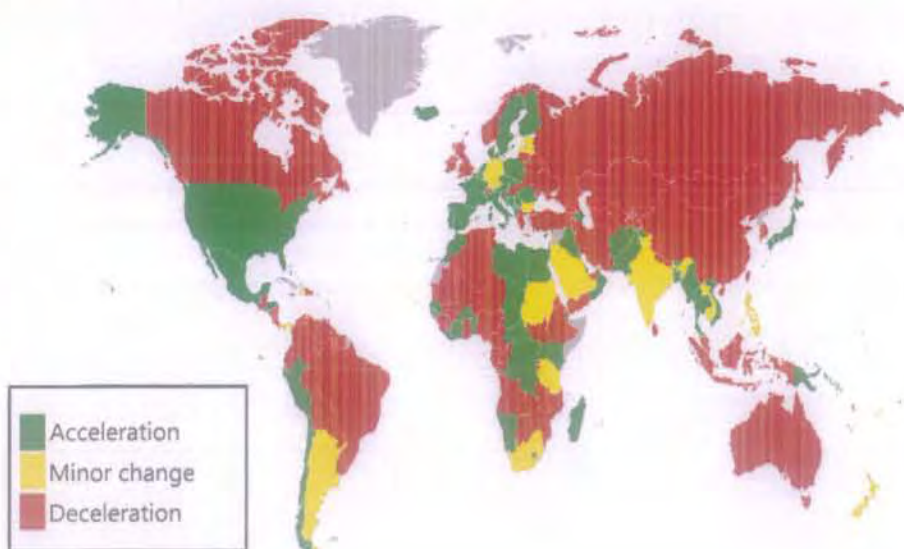
Risks

- Increasing financial market volatility (capital flows reversals; liquidity shortages)
- Sharper slowdown in China
- Secular stagnation risks still present
- Geopolitical risks remain very relevant

A difficult challenge. Short and medium term policy action needed!

- More aggregate demand needed despite limited policy space
- Infrastructure investment
- Structural reforms

Growth 2015













Future growth downgraded



Projections and Country Evolution 1

Advanced Economies Real GDP Growth Projections
(percent change from a year earlier)

										
	World	AEs.	U.S.	EA	Japan	U.K.	Germany	France	Italy	Spain
2016 (Jan 2016)	3.4	2.1	2.6	1.7	1.0	2.2	1.7	1.3	1.3	2.7
2016 (Oct 2015)	3.6	2.2	2.8	1.6	1.0	2.2	1.6	1.5	1.3	2.5
2017 (Jan 2016)	3.6	2.1	2.6	1.7	0.3	2.2	1.7	1.5	1.2	2.3
2017 (Oct 2015)	3.8	2.2	2.8	1.7	0.4	2.2	1.5	1.6	1.2	2.2

Source: IMF, World Economic Outlook.

Projections and Country Evolution 2

Emerging Market and Developing Economies Real GDP Growth Projections
(percent change from a year earlier)

								
	EMDEs	China	India	Russia	LAC	Brazil	Mexico	LIDCs
2016 (Jan 2016)	4.3	6.3	7.5	-1.0	-0.3	-3.5	2.6	5.6
2016 (Oct 2015)	4.5	6.3	7.5	-0.6	0.8	-1.0	2.8	5.8
2017 (Jan 2016)	4.7	6.0	7.5	1.0	1.6	0.0	2.9	5.9
2017 (Oct 2015)	4.9	6.0	7.5	1.0	2.3	2.3	3.1	6.1

Source: IMF, World Economic Outlook.

Global Risks and Spillovers

➤ Sharp growth slowdown in China:

- ☐ Insufficient progress with reforms leads to a continued buildup of vulnerabilities
- ☐ Sharp slowdown in 2016-17

➤ Sharper-than-expected global growth slowdown:

- ☐ Significant slowdown in other large EMs/frontier economies
- ☐ Structurally weak growth in key advanced and emerging economies

➤ Tighter or more volatile global financial conditions:

- ☐ Sharp asset price decline and decompression of credit spreads
- ☐ Surge in the US dollar

➤ A sudden rise in global risk aversion could generate a broader contagion effects

➤ An escalation of ongoing geopolitical tensions affecting confidence and disrupting global trade, financial, and tourism flows

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Policy Recommendations

Advanced economies

- Deal with legacies
- Continue with monetary accommodation where output gaps are negative and inflation too low (Euro area, Japan); smooth normalization (US)
- Absorb and integrate refugees
- Utilize fiscal space (Euro area)

Emerging market and developing economies





- Improve business climate/diversify export base
- Continue to use exchange rates as shock absorber as much as possible
- Evaluate tradeoffs before loosening monetary and/or fiscal policies
- Output gaps might be small despite growth slowdown
- Strengthen supervision and macroprudential frameworks

All countries

- Increase potential output – How?
- The case for infrastructure investment
- Which structural reforms to choose?

Role of the IMF

Support members facing a changing world

 Ensure quick delivery of financial assistance	Agility	Improve provision of capacity building	
 Better integrate policy advice across sectors	Integration	Synergies between surveillance and capacity building	
 Deepen engagement with members	Member-Focused	Strengthen knowledge management and timely feedback	

Key Recommendations of Timor-Leste 2016 Article IV Consultation

Recent Developments and Outlook

- Stable non-oil GDP growth
- Low inflationary pressure
- Fiscal and external balances deteriorated due to falling oil prices
- Petroleum Fund balance: first decline in value
- Oil prices remain low in the medium term

Crude Oil Price Assumptions

(US Dollars per Barrel)

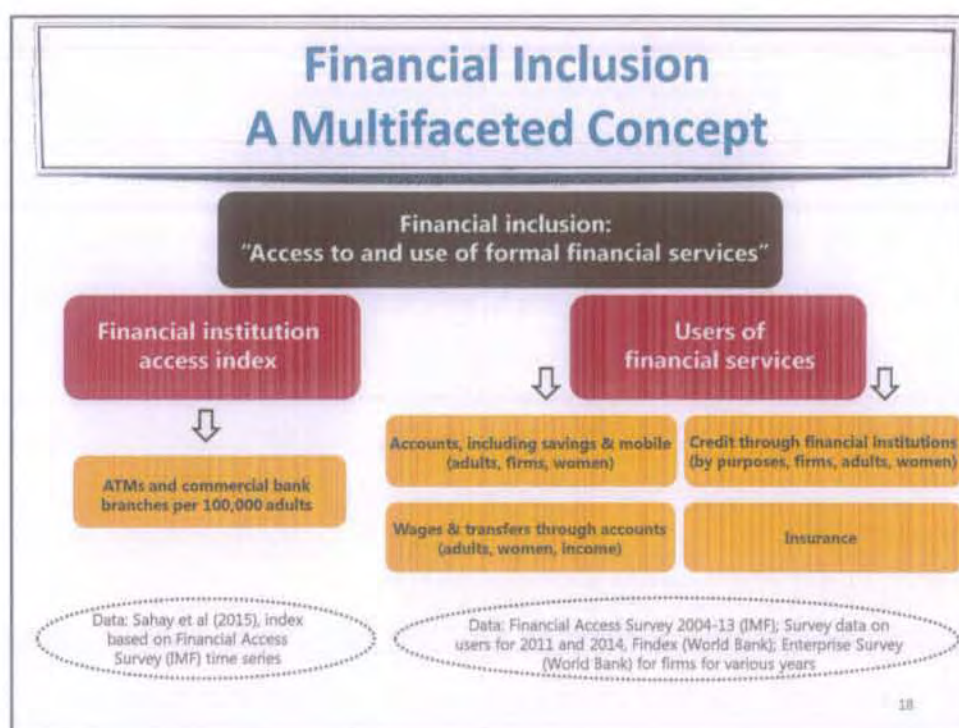


Source: IMF WEO Database.

Policy Recommendations

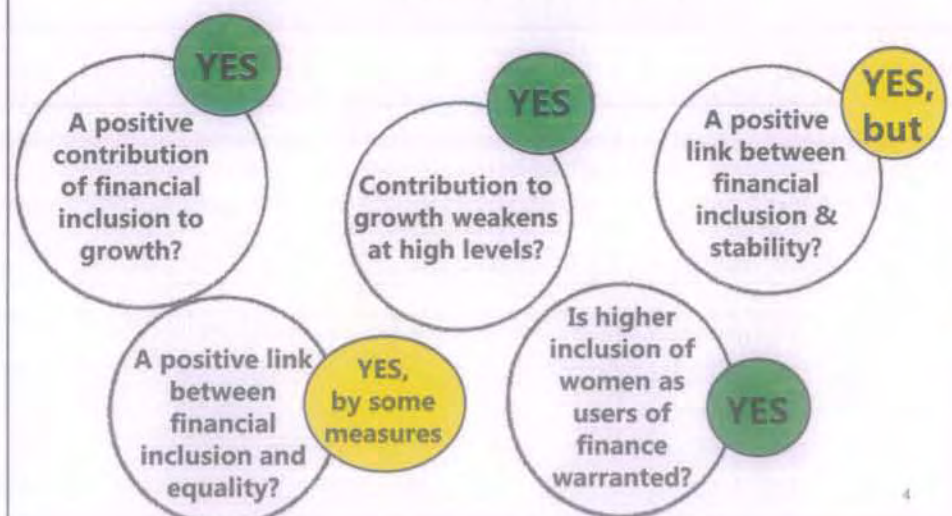
- Preserve fiscal sustainability
 - Scale back ambitious plan to front-load public investment
 - Rationalize recurrent spending
 - Strengthen non-oil revenues
 - Commit to a medium-term fiscal consolidation plan
- Maintain an appropriate balance between promoting financial inclusion and safeguarding financial stability
- Facilitate economic diversification
 - Catalyzing private sector development

Cross-cutting Issues Financial Inclusion



Our Key Contributions and Findings

Specific Questions We Ask



Financial Inclusion → Growth?

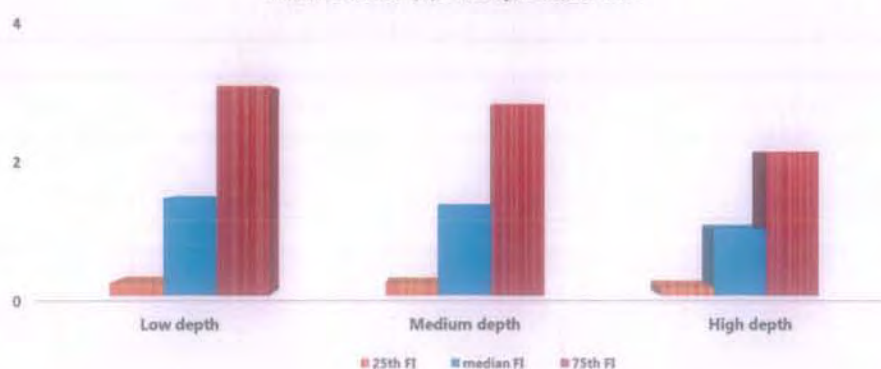
Channels Similar to Financial Development



Financial Inclusion: Positive but Effect on Growth Falls at High Levels of Financial Depth

Marginal Effects on Growth

Financial Inclusion (FI) = ATMs per 100,000 adults

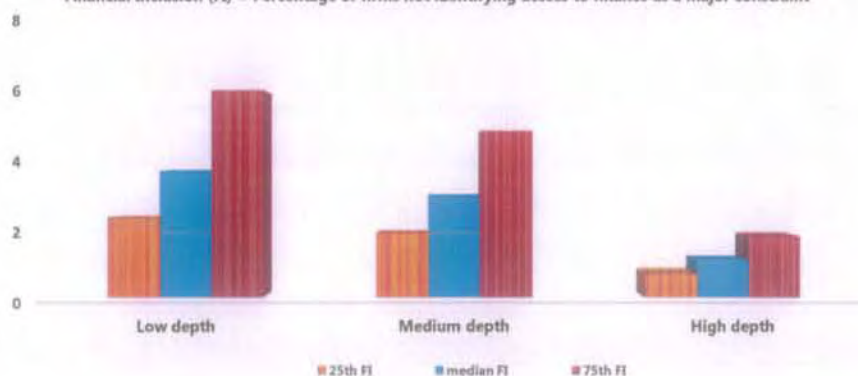


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Financial Inclusion: Positive but Effect on Growth Falls at High Levels of Financial Depth

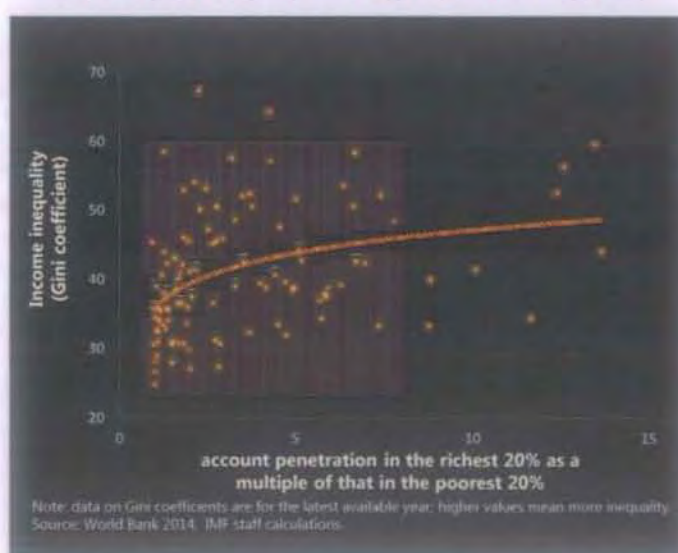
Marginal Effects on Growth

Financial Inclusion (FI) = Percentage of firms not identifying access to finance as a major constraint



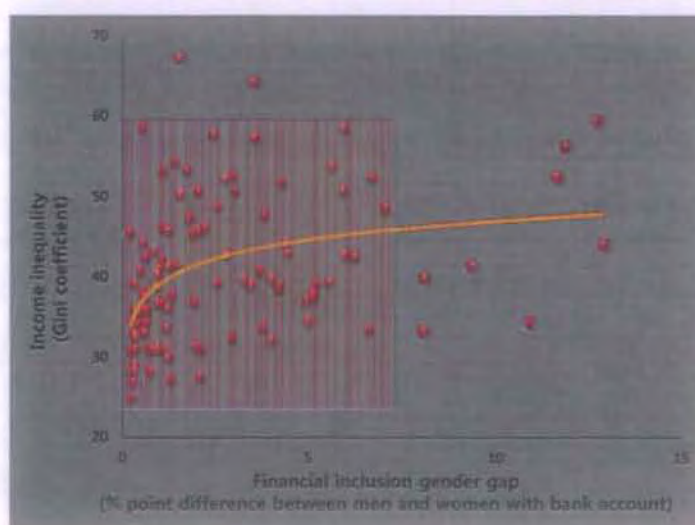
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Inequality in Access to Banks and in Income Go Hand-in-Hand



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Gender Gap in Bank Accounts Coexists with Income Inequality



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Financial Inclusion → Stability?

Trade-Offs and Synergies

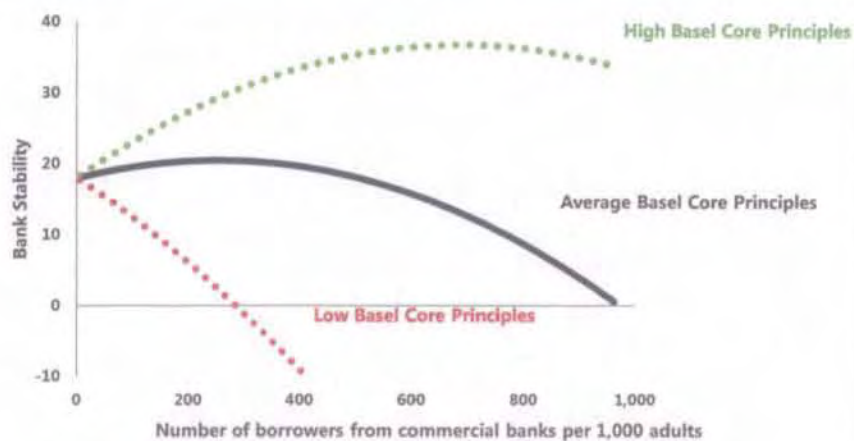
Systemic
Risk

Deposits as
Stable
Funding
Base during
Crisis

Risk Mitigation
Tools

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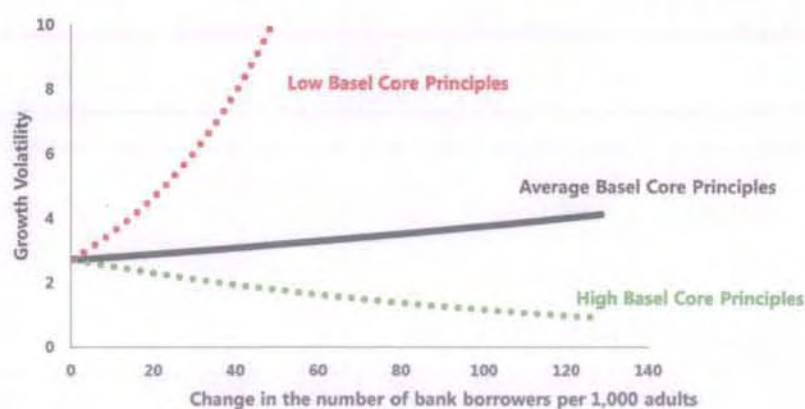
Financial Stability: Risks with Broadening Credit Access Rise as Supervisory Quality Falls



Source: IMF staff calculations.
Note: Bank stability is approximated by bank z-score, which captures banks' distance-to-distress (the amount of buffers banks have against shocks to earnings).

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Output Stability: Risks with Broadening Credit Access Rise as Supervisory Quality Falls



Source: IMF staff calculations.

Note: Growth volatility is approximated by the 3-year rolling standard deviation of GDP growth.

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Cross-cutting Issues Diversification

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International experience suggests:

Diversification depends on country circumstances

- ▶ There is no one-fits-all answer

Diversifying away from oil is very difficult

- ▶ Success or failure appears to depend on the implementation of appropriate policies ahead of the decline in oil revenues

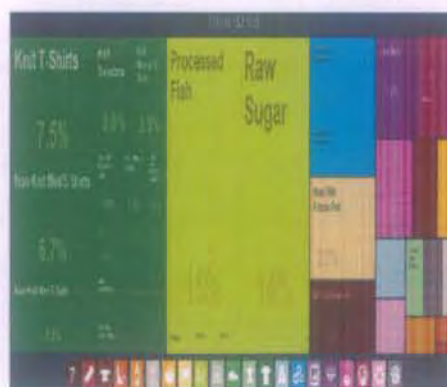
Based on IMF (2014) "Economic Diversification in GCC: Past, Present, and Future."

The case of Mauritius: Focus on comparative advantage areas...

Mauritius: Export Products (1970)



Mauritius: Export Products (2013)



Source: The Observatory of Economic Complexity, MIT.

...and move up the product ladder

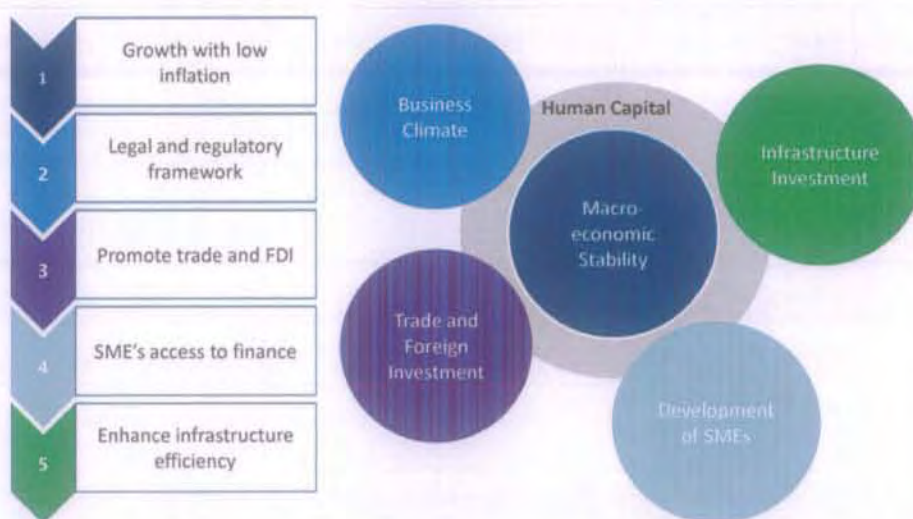
Mauritius: Export Product Space (2013)



Note: Network shows the relatedness between products (See Hidalgo, Hausmann et al. (2007)).

Source: The Observatory of Economic Complexity, MIT.

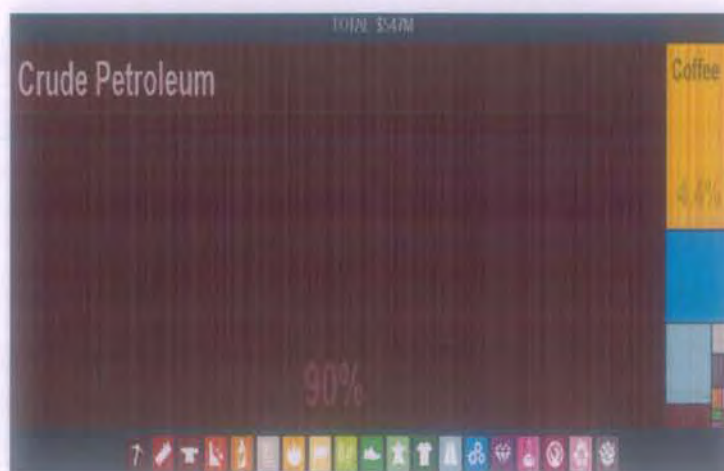
Policies to support diversification



Based on IMF (2014) "Economic Diversification in GCC: Past, Present, and Future."

Landscape of Timor-Leste's export products

Timor-Leste: Export Products (2013)



Source: The Observatory of Economic Complexity, MET.

What are the comparative advantages of Timor-Leste?

Young labor force has potential

- Invest in education and vocational training
- Exploit opportunity to work abroad and bring capital, skill and know-how

Agriculture & tourism with branding and marketing

- Coffee, spices, candlenuts...
- Access to market, product innovation



Role of the Government?

- ✓ Enabling business environment
- ✓ Serve as a facilitator
- ✓ Establish an effective dialogue with the private sector for better partnership

e.g. legal frameworks, regulatory rules,
labor training services, market access, access to
finance, and infrastructure