INTERNATIONAL MONETARY FUND

IMF Country Report No. 19/310

BRUNEI DARUSSALAM

October 2019

2019 ARTICLE IV CONSULTATION—PRESS RELEASE AND STAFF REPORT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2019 Article IV consultation with Brunei Darussalam, the following documents have been released and are included in this package:

- A **Press Release.**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse of time basis following discussions that ended on July 8, 2019, with the officials of Brunei Darussalam on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on August 26, 2019.
- An **Informational Annex** prepared by the IMF staff.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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October 10, 2019

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IMF Executive Board Concludes 2019 Article IV Consultation with Brunei Darussalam

On September 10, 2019, the Executive Board of the International Monetary Fund (IMF) concluded the 2019 Article IV consultation[1] with Brunei Darussalam and considered and endorsed the staff appraisal without a meeting on a lapse-of-time basis.[2]

Brunei Darussalam's economy has been adjusting to lower oil and gas (O&G) prices since 2014, with the authorities undertaking wide-ranging reforms. The decline in O&G prices led to large budget deficits and narrower current account surpluses. In response, the authorities in 2015 launched a comprehensive reform program aimed at: (i) ensuring long-term fiscal sustainability and intergenerational equity, and (ii) fostering economic diversification by improving the business climate, developing the financial sector, attracting FDI in priority business clusters, and supporting micro, small and medium-sized enterprises (MSMEs).

Growth in 2018 was lower than expected, slowing down to 0.1 percent. Unscheduled maintenance of O&G fields hampered both crude oil and liquified natural gas (LNG) production. Non-O&G growth continued to improve, underpinned by ongoing construction projects. In expenditure terms, lower public spending and net exports—reflecting fiscal consolidation and large infrastructure related imports—offset higher private investment. Average inflation moved into positive territory in 2018, at 0.1 percent, but has turned negative again this year. Current

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

account surplus decreased to 7.9 percent of GDP in 2018, due to higher imports linked to large infrastructure projects. The fiscal balance was better than expected, recording a surplus in FY2018/19 for the first time since the 2014 oil price shock.

Growth is expected to pick up in 2019 to 1.8 percent, with the outlook improving further over the medium term, driven by stronger O&G activities from asset rejuvenation and large FDI projects. The ramp-up of capital spending under the 11th National Development Plan (RKN11) would also support the non-O&G growth. The start of operations of large downstream investment projects—the Hengyi refinery and Brunei Fertilizer Industries—and stronger O&G activities will further improve the outlook from 2020 onward. Inflation would remain low. The current account surplus would increase over the medium term, reflecting stronger exports of O&G and downstream products. The fiscal position would deteriorate owing to lower O&G prices this year, while it is expected to recover over the medium term. Risks to the near-term outlook are tilted to the downside. Lower-than-expected O&G prices or production would reduce fiscal revenues and exports, with significant spillovers to the non-O&G sector.

The authorities have made substantial progress in fiscal consolidation, improving the business climate, and developing the financial sector. The fiscal consolidation initiatives include corporatization and privatization, public-private partnership, evaluation of subsidies against targets, fiscal management enhancement, revenue diversification, and amalgamation of the government's asset management system. From 2015 to 2019, Brunei made strides in improving the World Bank Doing Business scores, with strong progress in access to credit and starting a business. Brunei has attracted sizable FDI in its five priority business clusters, mainly in the downstream O&G sector. The authorities have also set up centers and programs, such as JobCenter Brunei, I-Ready, and the Center for Capacity Building, to foster job opportunities and increase job matching. Finally, they have taken wide-ranging measures in developing the financial sector, while strengthening macroprudential framework and supervisory system.

Executive Board Assessment

In concluding the 2019 Article IV consultation with Brunei Darussalam, Executive Directors endorsed staff's appraisal, as follows:

Brunei Darussalam's economy has been adjusting to the lower O&G prices since 2014, with the authorities undertaking wide-ranging reforms. Brunei has made significant progress in consolidating the fiscal position, improving the business climate, attracting FDI, developing the financial sector, and strengthening regulation. Growth is expected to pick up in 2019, with the outlook improving further over the medium term, driven by a pickup in the O&G sector and large investment projects. Nevertheless, Brunei faces challenges and risks. Future oil production and prices remain uncertain. Against this backdrop, the reforms should continue to ensure long-term sustainability and intergenerational equity, increase productivity and competitiveness, diversify the sources of growth, reduce unemployment—especially youth unemployment, and build resilience to shocks.

Staff supports the authorities' fiscal consolidation program, although more ambition is called for to bring the fiscal position gradually closer to that implied by intergenerational equity considerations. Over the medium term, staff recommends: (i) continue reforms in public services and the wage bill, including streamlining civil service vacancies, (ii) reform fuel subsidies, (iii) rebalance further budget spending toward growth-enhancing activities, and (iv) increase non-O&G revenues. Adopting a formal medium-term fiscal framework would help control spending and delink it from O&G revenue fluctuations. Digitalization can help improve public financial management.

The peg to the Singapore dollar remains appropriate, providing a credible nominal anchor and stability to the financial system. The external position is assessed to be weaker in 2018 than fundamentals. However, the current account balance, on current policies, is expected to rebound, closing the gap over the medium term as new downstream exports rise.

The authorities' initiatives toward economic diversification are commendable. Brunei has made strides in improving business environment, while attracting sizable FDI in the priority business clusters, mainly in the downstream O&G sector. Going forward, continued efforts are needed to further improve the business environment, attract quality FDI, enhance human capital, and reform labor market to foster private sector led-growth and reduce unemployment.

Staff supports the authorities' initiatives to develop the financial sector, while safeguarding financial stability and integrity. The initiatives include steps to broaden the investor base, establish a secondary bond market, develop the required infrastructure and rules for establishing a stock exchange, and put all the three pillars of Basel II in place. Given the size of banking assets placed offshore, the AMBD should closely monitor the potential risks emanating from external shocks. Staff supports the recent progress in strengthening the AML/CFT framework and the additional measures planned for the upcoming mutual evaluation.

The authorities should address the remaining data gaps. Staff welcomes the authorities' commitment to publishing the NSDP in line with the recent IMF TA on e-GDDS, as well as the authorities' plan to request further TA from the IMF to improve data collection and dissemination.

Brunei Darussalam: Selected Economic and Financial Indicators, 2014–24

Area: 5,765 sq. kilometers
Population (2018): 442,400
Nominal GDP per capita (2018): US$30,668
Main export destinations (2018): Japan (34.7), Thailand (10.1), Australia (8.8), Korea (8.6)
Unemployment rate (2017): 9.3%
Labor force participation rate (2017): total 62.7%; male 68.9%; female 56.5%

	2014	2015	2016	2017	2018	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Output and prices											
Nominal GDP (millions of Brunei dollars)	21,664	17,778	15,748	16,747	18,301	16,907	17,281	17,498	17,879	18,213	18,575
Nominal non-oil and gas GDP (millions of Brunei dollars)	7,733	7,658	7,463	7,521	7,595	7,653	8,048	8,302	8,554	8,709	8,877
Real GDP (percentage change) 1/	-2.5	-0.4	-2.5	1.3	0.1	1.8	4.7	3.6	3.5	2.4	2.1
Oil and gas sector GDP	-3.7	-0.2	-2.8	1.2	-1.1	2.4	3.2	3.3	3.5	2.9	2.6
Non-oil and gas sector GDP	-0.8	-0.6	-1.9	1.5	1.7	1.0	6.8	4.0	3.6	1.8	1.5
Oil production ('000 barrels/day)	126	127	121	113	112	115	118	122	126	129	132
Natural gas output (millions cu. ft./day)	1,170	1,228	1,205	1,234	1,184	1,205	1,246	1,291	1,342	1,382	1,421
Average Brunei oil price (U.S. dollars per barrel)	104.4	53.9	44.6	55.9	73.2	65.5	61.9	59.8	59.0	59.0	59.3
Average Brunei gas price (U.S. dollars per million BTU)	16.6	10.6	7.3	8.3	10.5	6.5	7.3	7.3	7.3	7.3	7.3
Consumer prices (period average, percentage change)	-0.2	-0.4	-0.7	-0.2	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Consumer prices (end of period, percent change)	1.2	-1.0	-1.6	0.0	0.0	0.1	0.2	0.2	0.2	0.2	0.2
					(In percent of GDP)						
Public finances: budgetary central government											
Total revenue	37.7	24.2	17.7	26.0	28.6	23.9	24.1	23.8	23.6	24.2	24.9
Oil and gas	32.9	18.4	12.3	17.4	23.4	17.9	18.1	17.6	17.4	18.0	18.8
Other	4.7	5.8	5.4	8.6	5.2	6.0	6.1	6.2	6.2	6.1	6.1
Total expenditure	34.1	38.7	39.4	36.6	32.2	35.4	35.5	34.9	34.1	33.5	32.9
Current	25.3	29.6	30.6	30.7	28.9	31.5	30.8	30.4	29.7	29.2	28.6
Capital	8.8	9.1	8.7	5.9	3.3	3.8	4.6	4.6	4.5	4.4	4.3
Overall balance 2/	3.6	-14.5	-21.7	-10.6	-3.6	-11.5	-11.3	-11.1	-10.5	-9.4	-8.0
Non-oil and gas overall deficit	-71.5	-68.9	-67.7	-57.1	-58.6	-60.0	-58.2	-55.8	-53.6	-52.5	-51.3
(In percent of non-oil and gas GDP)											
					(12-month percent change)						
Money and banking											
Private sector credit	1.8	2.6	-6.2	-5.3	-3.1	0.4	1.0	1.6	1.5	1.2	1.0
Narrow money	-1.5	6.4	-0.1	-5.7	-3.0	1.9	3.1	3.7	3.6	2.7	2.0
Broad money	3.2	-1.8	1.5	-0.4	2.8	3.9	3.3	3.1	2.7	2.3	2.2
					(In millions of U.S. dollars, unless otherwise indicated)						
Balance of payments											
Goods	7,479	2,910	2,154	2,403	2,364	1,605	2,157	2,424	2,764	3,094	3,502
Exports	11,149	6,127	4,813	5,475	6,470	4,952	7,180	8,098	8,474	8,723	8,868
Of which: oil and gas	9,604	5,909	4,321	5,021	6,114	4,775	4,801	4,724	4,876	5,015	5,148
Imports	3,670	3,217	2,659	3,072	4,105	3,347	5,022	5,674	5,710	5,629	5,366
Services (net)	-955	-1,007	-1,114	-698	-1,005	-709	-745	-770	-792	-818	-832
Primary income (net)	-20	650	835	721	215	614	593	634	636	643	629
Secondary income (net)	-1,045	-397	-404	-442	-506	-451	-466	-474	-464	-468	-469
Current account balance	5,459	2,157	1,470	1,985	1,068	1,060	1,539	1,814	2,144	2,452	2,831
Current account balance (in percent of GDP)	31.9	16.7	12.9	16.4	7.9	8.5	12.0	13.8	15.9	17.6	19.8
Gross official reserves 3/	3,471	3,211	3,322	3,300	3,221	3,327	3,435	3,543	3,654	3,764	3,876
In months of next year's imports of goods and services	8.6	9.0	9.2	7.0	8.3	6.3	5.9	6.0	6.2	6.6	…
Brunei dollars per U.S. dollar (period average)	1.27	1.37	1.38	1.38	1.35	…	…	…	…	…	…
Brunei dollar per U.S. dollar (end of period)	1.32	1.41	1.44	1.35	1.37	…	…	…	…	…	…

Sources: Data provided by the Brunei authorities; and Fund staff estimates and projections.
1/ Non-oil and gas GDP includes the downstream sector.
2/ In absence of government debt and interest payments, this is also primary balance.
3/ Comprises foreign exchange assets of Autoriti Monetari Brunei Darussalam, SDR holdings, and reserve position in the Fund.

INTERNATIONAL MONETARY FUND

BRUNEI DARUSSALAM

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION

August 26, 2019

KEY ISSUES

Context. Brunei Darussalam's economy has been adjusting to the lower oil and gas (O&G) prices since 2014, with the authorities undertaking wide-ranging reforms. The reforms aim to ensure long-term fiscal sustainability and intergenerational equity, and to foster economic diversification.

Outlook and risks. Growth is expected to pick up in 2019, with the outlook improving further over the medium term, driven by expansion in the O&G sector and large investment projects. Nonetheless, lower-than-expected O&G prices or production would reduce fiscal revenues and exports, with significant spillovers to the non-O&G sector.

Policy Recommendations:

- **Fiscal policy.** Continue fiscal consolidation to ensure long-term sustainability and intergenerational equity, by enhancing the revenue and expenditure strategy, reforming subsidies, and continuing public financial management reforms;

- **Structural reforms.** Step up structural reforms to encourage private sector-led growth, by continuing to improve the business climate, enhance human capital, attract FDI, and boost integration with the global economy, while leveraging digital innovations;

- **Financial sector.** Develop the financial sector while safeguarding financial stability and integrity, by strengthening micro- and macroprudential policies and supervision;

- **External sector**. The peg to the Singapore dollar remains appropriate, providing a credible nominal anchor and stability to the financial system; and

- **Data issues.** Continue to improve data compilation and dissemination.

Approved By
Odd Per Brekk and Edward Gemayel

Discussions took place in Bandar Seri Begawan during June 26–July 8, 2019. The mission team comprised Tahsin Saadi Sedik (head), Kyung-Seol Min, Md Shah Naoaj, and Qianqian Zhang (all APD). The mission met with the Minister at the Prime Ministers' Office and Minister of Finance and Economy II Hon. Dato Dr. Amin Abdullah, and other senior officials from the ministries, Autoriti Monetari Brunei Darussalam (AMBD), Anti-Corruption Bureau, and private sector representatives. Ms. Mahasandana (Executive Director) and Mr. Mahyuddin (OED Senior Advisor) also participated in the discussions. Justin Flinner and Claudia Marchini (both APD) assisted in preparing this report.

CONTENTS

CONTEXT

1. **Brunei's economy has been adjusting to declining oil production since 2010 and lower oil and gas (O&G) prices since 2014, with the authorities undertaking wide-ranging reforms.** The decline in O&G prices led to large budget deficits and narrower current account surpluses. In response, the authorities in 2015 launched a comprehensive reform program aimed at: (i) ensuring long-term fiscal sustainability and intergenerational equity, and (ii) fostering economic diversification by improving the business climate, developing the financial sector, attracting FDI in priority business clusters, and supporting micro, small and medium-sized enterprises (MSMEs).

2. **Brunei faces challenges and risks (Appendix I).** Its economy remains dependent on the O&G sector, which in 2018 accounted for 58 percent of GDP, 81 percent of government revenues, and 95 percent of exports. Future oil production and prices remain uncertain. Subdued oil production or prices would take a toll on fiscal balances, requiring a drawdown of Brunei's asset funds, undermining long-term sustainability and intergenerational equity. While non-O&G growth prospects have recently improved, unemployment remains high.

3. **Sizable sovereign wealth buffers accumulated through prudent policies allow Brunei to face its challenges from a position of strength.** Virtually no public debt and ample international reserves underpin Brunei's resilience to shocks and provide scope for gradual adjustment.

4. **Economic reforms have been broadly in line with Fund policy advice.** The authorities have made progress in consolidating the fiscal position, improving the business climate, and developing the financial sector while strengthening regulation and supervision, in line with Fund advice. However, progress on non-O&G revenue measures, energy subsidy reforms, and improvements in data compilation and dissemination could be accelerated (Appendix II).

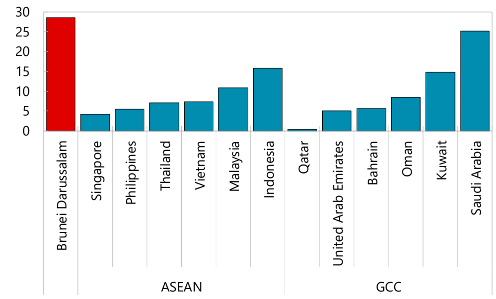
RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

5. **Growth in 2018 was lower than expected, slowing to 0.1 percent.** Unscheduled maintenance of O&G fields hampered both crude oil and liquified natural gas (LNG) production. Non-O&G growth continued to improve, underpinned by construction projects. In expenditure terms, lower public spending and net exports—reflecting fiscal consolidation and large infrastructure related imports—offset higher private investment. The latest quarterly data show a continued recovery in the non-O&G sector, growing at 2.5 percent year-on-year in the first quarter of 2019, while the overall growth declined to -0.5 percent due to scheduled maintenance of O&G fields. Average inflation moved into positive territory in 2018, at 0.1 percent, but has turned negative again this year, at -0.2 percent in May.

6. **Unemployment remains high (Appendix III).** The unemployment rate increased to 9.3 percent in 2017 from 6.9 percent in 2014, owing to the slowdown in the economy following the 2014 oil price shock. The youth unemployment rate increased to 28.9 percent from 25.3 percent,

higher than ASEAN and Gulf Cooperation Council (GCC) countries. The unemployment rate of locals increased to 11.5 percent and youth unemployment rate of locals reached 31.7 percent in 2017. While the female labor force participation rate declined to 56.5 percent, the corresponding gender gap narrowed.

Youth Unemployment, Latest
(Percent)



Source: International Labor Organization estimates.

7. The authorities have made significant progress in fiscal consolidation in the wake of the 2014 oil price shock. The overall fiscal balance recorded a surplus in FY2018/19 for the first time since the oil price shock in 2014, owing mostly to higher O&G revenues, reflecting a rebound in O&G prices, and lower expenditure, mainly capital spending due to the gradual implementation of the 11th National Development Plan (RKN11). The non-O&G deficit—an indicator of underlying fiscal effort and long-term sustainability—narrowed from 61.3 percent of non-O&G GDP in FY2017/18 to 54.9 percent in FY2018/19 (Text Table 1).

Text Table 1. Brunei Darussalam: Fiscal Development 1/

	2014/15	2015/16	2016/17	2017/18	2018/19
			(Percent of GDP)		
Revenue	34.4	21.7	22.5	22.7	32.6
Oil & Gas	29.4	15.9	13.4	16.2	25.1
Non-Oil & Gas	5.0	5.9	9.2	6.5	7.4
Expenditure	35.4	37.1	39.3	35.6	32.3
Current	26.6	29.2	31.2	30.4	29.6
Capital	8.8	8.0	8.1	5.2	2.7
Overall Balance 2/	-1.0	-15.4	-16.8	-12.9	0.3
Non-O&G Balance (% of Non-O&G GDP)	-70.5	-65.1	-59.6	-61.3	-54.9
			(millions of BND)		
Nominal GDP	20,581	17,063	15,905	17,048	18,440
Nominal non-O&G GDP	7,735	7,600	7,449	7,508	7,636

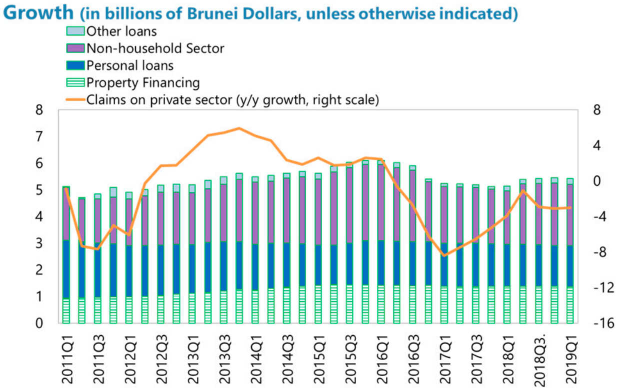
Source: Brunei authorities, IMF staff estimates
1/ Fiscal year: April-March
2/ In absence of government debt and interest payments, this is also primary balance.

8. Brunei's external position is assessed to have been weaker than fundamentals in 2018 (Appendix IV). The current account surplus narrowed to 7.9 percent of GDP in 2018, due to higher temporary imports linked to the construction phase of large infrastructure projects. However, the surplus is expected to rebound on current policies, closing the gap over the medium term as new downstream exports rise and the temporary imports fade.

9. The peg to the Singapore dollar remains appropriate, providing a credible nominal anchor and stability to the financial system. The currency board has helped keep the inflation rate and its volatility low, suggesting that the credibility of the peg anchors inflation and preserves macroeconomic stability. The peg also helps Brunei benefit from Singapore's deep financial markets in managing its large external assets without incurring exchange rate risks. Official reserves are assessed to remain above the adequacy benchmarks.

10. The banking sector remains sound, with solid capital and liquidity buffers. Indications are that banks are well capitalized—the capital adequacy ratio increased from 18.6 percent in 2018Q1 to 20.7 percent in 2019Q1, well above the regulatory minimum requirement of 10 percent. Banks hold considerable excess liquidity, with the overall liquid asset ratio hovering around 50 percent. Gross non-performing loans and financing ratio remained stable at 5.1 percent. Banks are profitable—the return on assets increased to 1.5 percent from 1.2 percent, and the return on equity increased to 10.4 percent from 8.6 percent. The pickup in the non-O&G growth has attenuated the decline in private sector credit, recovering from -3.9 percent to -3.0 percent, while total banking sector loans, which include loans to the government-linked companies (GLCs), increased from -2.0 percent to 5.4 percent.

Brunei Darussalam: Direction of Loans and Private Sector Credit Growth (in billions of Brunei Dollars, unless otherwise indicated)



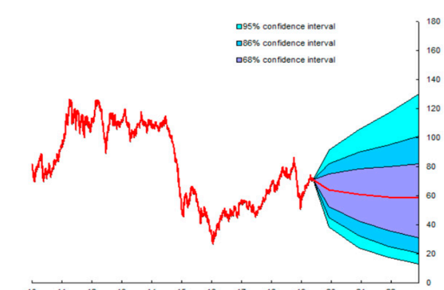
Sources: Brunei authorities; and IMF staff estimates

11. **Growth is expected to pick up in 2019, with the outlook improving further over the medium term, driven by expansion in the O&G sector and large investment projects.** Growth is projected to accelerate to 1.8 percent in 2019, reflecting stronger O&G activities from asset rejuvenation and planned investment. The ramp-up of capital spending related to the RKN11 would also support the non-O&G growth. The fiscal position would deteriorate this year owing to lower O&G prices and higher capital spending. In the medium-term, however, the fiscal position is expected to recover. The start of operations of the large downstream investment projects—the Hengyi refinery and Brunei Fertilizer Industries—and stronger O&G activities would further improve the outlook from 2020 onward. Inflation would remain low, but positive, over the medium term. The current account surplus would increase, reflecting stronger exports of O&G and downstream products, and fading temporary imports related to large investment projects. Private sector credit growth would recover in line with the non-O&G growth.

12. **Risks to the near-term outlook are tilted to the downside (Appendix I).** Lower-than-expected energy prices would reduce fiscal revenues and exports, with significant spillovers to the non-O&G sector. Disruption in domestic O&G production caused by aging fields and lower than expected production from new projects are also important risks to the outlook, as are possible delays in large downstream FDI projects. A sharp tightening of global financial conditions and rising protectionism may slow global growth and dampen energy demand. On the upside, geopolitical tensions may push O&G prices higher than expected. In addition, the ongoing asset rejuvenation and planned exploration could deliver higher-than-expected O&G production over the medium term.

Brent Crude Oil

(U.S. dollars a barrel)

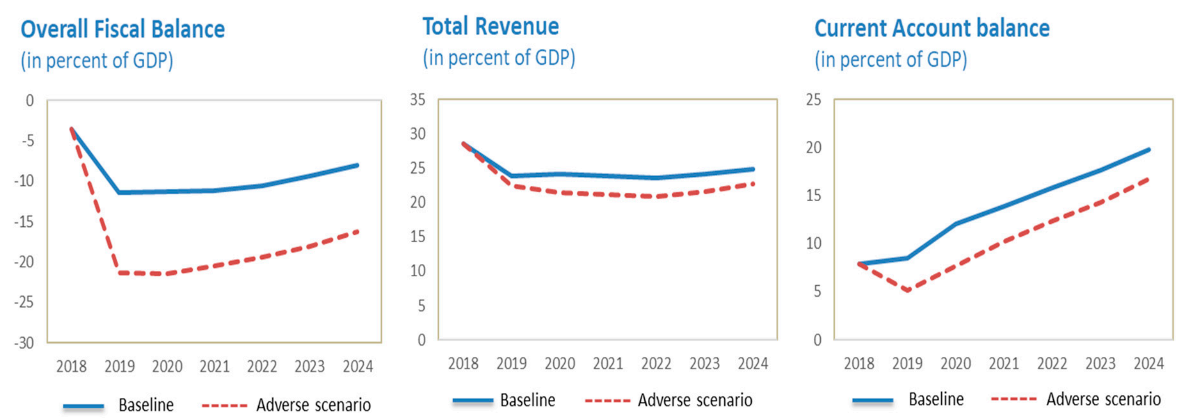


Sources: Bloomberg L.P.; and IMF staff calculations.

13. **A sharp decline in O&G prices would have large impacts on macroeconomic balances.** To illustrate the impact of lower O&G prices on fiscal position and current account, in an adverse scenario staff assumes medium-term Brunei O&G prices to fall back to the lowest levels observed in 2016 (oil price at US$34.4 and gas price at US$6.4) and remain there. In this low probability scenario,

the fiscal deficit is projected to be lower by about 10 percentage points over 2019-2024, compared to the baseline scenario, requiring the use of the sovereign asset funds and undermining intergenerational equity. Staff sees this as a tail risk, given the authorities' capacity for fiscal consolidation, demonstrated over the past years, and the available policy options such as raising tax and non-tax revenues.

Brunei Darussalam: Baseline vs. Adverse Scenario



Authorities' Views

14. The authorities broadly agreed with the assessment of recent developments. While acknowledging the risks and challenges faced by the Brunei's economy, they are more optimistic about the short-to-medium-term outlook, given new investment in the upstream O&G sector and scheduled asset rejuvenation, which could generate higher O&G production than staff's baseline scenario. They noted the continued recovery in the non-O&G growth due to large investment in infrastructure projects and ramp-up of capital spending related to RKN11. The Hengyi refinery may start operations this year, further boosting spin-off activities in both the O&G and non-O&G sectors. While the authorities acknowledged that the unemployment rate is high, efforts are ongoing to significantly reduce it over the next few years, through active labor market programs, including the Bruneianization and the start of operations of the large downstream investment projects.

MACROECONOMIC POLICIES

A. Continuing Fiscal Consolidation and Reducing the Procyclicality of Fiscal Policy

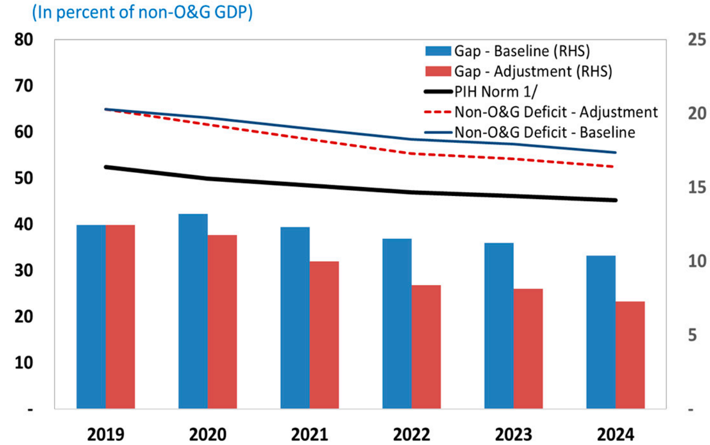
15. The authorities formulated the FY2019/20 budget based on more realistic expenditure assumptions. In recent years, spending outturns have been on average about 10 percent higher than budgeted. As part of strengthening the budget framework, the authorities seek to enhance the credibility of the fiscal framework by aligning the budget with actual spending and reinforcing accountability.

16. The authorities introduced a medium-term fiscal consolidation program. The program aims to help each ministry formulate its own fiscal consolidation plan and reassess government revenue and expenditures to rebalance the budget toward growth-promoting activities. To monitor implementation of the program, line ministries are required to communicate regularly with the Ministry of Finance and Economy (MOFE) on its progress. The consolidation initiatives include corporatization and privatization, public-private partnership, evaluation of subsidies against targets, fiscal management enhancement, revenue diversification, and amalgamation of the government's asset management system.

17. Staff supports the authorities' fiscal consolidation program, although more ambition is called for to ensure long-term sustainability and to bring the fiscal position gradually closer to that implied by intergenerational equity considerations. Sustainable long-term expenditures—under the permanent income hypothesis (PIH) commonly used for oil-exporting economies—point to a need for continued fiscal consolidation and making the budget less reliant on O&G revenues. The gap between the non-O&G balance and that consistent with the intergenerational equity level is estimated at about 10 percent of non-O&G GDP in 2024. Brunei's sizable fiscal buffers and virtually no public debt provide fiscal space to carry out the needed adjustment in a gradual manner and limit the adverse effects on growth and employment.

Brunei Darussalam: Non-O&G Fiscal Deficit vs. PIH Norm

(In percent of non-O&G GDP)



Source: IMF staff estimates.

1/ Using a constant real per-capita annuity

18. To ensure long-term fiscal sustainability and intergenerational equity, staff recommends the following medium-term reforms:

- **Continue reforming public services and the wage bill.** Reforms should be designed to foster public sector productivity and incentivize Bruneians to seek more job opportunities in the private sector. The wage bill could be further contained by streamlining civil service vacancies.

- **Reform fuel subsidies in line with the IMF technical assistance (TA).** In addition to being costly, subsidies encourage excessive consumption and inefficient allocation of capital. The TA estimated the fiscal cost of fuel subsidies at 1-1.5 percent of GDP. Furthermore, subsidies benefit the wealthier group more than the vulnerable. International experience suggests that a well thought-out and comprehensive reform strategy is key to ensuring success, which includes a clear communication strategy and compensatory measures to protect the vulnerable.

- **Rebalance further budget spending toward growth-enhancing activities**. Measures could include reducing untargeted subsidies (for example, on housing and food) and promoting more efficient use of energy and water. Priority spending should concentrate on physical infrastructure (public transportation system), human capital (high quality education and training), institutional frameworks, MSME support, active labor market programs, and digitalization.

- **Increase non-O&G revenue.** Additional revenue mobilization can be achieved by recalibrating property taxes, expanding further excise taxes, and adopting a Goods and Services Tax (GST).

19. These reforms would contribute to economic diversification and development of the private sector, while achieving long-term fiscal sustainability earlier than under the baseline scenario. Relative to the baseline scenario, which reflects the authorities' planned efforts over the medium term, the adjustment scenario, comprising gradual reform of fuel subsidies and a lower wage bill, would lead to an additional reduction in the deficit path by 1.4 percent of GDP on average annually (Text Table 2). Such an adjustment scenario would reduce the gap between the non-O&G balance and that consistent with the intergenerational equity to 7 percent of non-O&G GDP in 2024. The adjustments would help achieve the sustainable long-term non-O&G deficit level gradually, reaching the level consistent with intergenerational equity considerations in 10 years, instead of 15 years in the baseline scenario.

Text Table 2. Brunei Darussalam: Medium-Term Fiscal Balances Under Different Scenarios

	2019	2020	2021	2022	2023	2024	cumulative 2019-2024
	(Calendar year basis, percent of GDP)						
Fiscal balance under:							
Baseline scenario	-11.5	-11.3	-11.1	-10.5	-9.4	-8.0	-61.9
Policy adjustments 1/	-11.5	-10.7	-10.1	-9.1	-8.0	-6.6	-55.9

Source: IMF Staff calculations

1/ Policy adjustments relative to the baseline: containing wage bill (0.2 percent of GDP) and fuel subsidy reform (1.2 percent of GDP) gradually from 2020 to 2022, and sustained in the medium term.

20. Adopting a formal medium-term fiscal framework (MTFF) would help control spending and delink it from O&G revenue fluctuations (Appendix V). The authorities have taken steps toward establishing an MTFF, by establishing a fiscal forecasting unit and requesting that line ministries prepare three-year spending plans. Despite this progress, Brunei's MTFF is still in an early stage. The MTFF should be incorporated into a fiscal strategy that includes aggregate and sectoral ceilings and fiscal risk analysis. Adopting a medium-term budget framework focused on strategic prioritization of expenditure by ministries and programs would help insulate spending from volatile O&G prices and reduce the procyclicality of fiscal policy. The annual budget process would be further enhanced by strengthening fiscal transparency, for instance, by publishing more detailed budget execution data and reconciling budget projections with outcomes. Implementing a treasury single account and a well-functioning financial management information system would enhance budget control and monitoring.

21. Digitalization can help improve public financial management. For example, integrated beneficiary databases for social safety nets can reduce inclusion and exclusion errors. E-procurement can generate budgetary savings by promoting competition among contractors, increase transparency, and reduce vulnerabilities to corruption. Staff welcomes the newly introduced e-invoice procurement system and supports the efforts to create a National Centralized Database—a centralized database for welfare assistance programs, while emphasizing the need to ensure privacy and cyber security.

Authorities' Views

22. The authorities agreed on the need for further fiscal consolidation in a gradual manner. The authorities underscored that the FY2019/20 budget does not entail an easing of fiscal policy—the budget is based on more realistic spending assumptions, by aligning the budget with actual spending. They emphasized that fiscal consolidation efforts will continue in line with their medium-term fiscal consolidation program. To achieve a balanced budget, fiscal consolidation policy requires a "whole of government" approach. To operationalize the consolidation program, the government is assessing fiscal consolidation plans formulated by each ministry, which includes three program components namely Policy Review, Sector Reform Plan, and Fiscal Consolidation Plan. The consolidation initiatives include further corporatization—building on the successful corporatization of Muara port. Any subsidy reform will be assessed thoroughly and will be implemented gradually to protect the most vulnerable. As a first step, the authorities' efforts focus on minimizing leakages by introducing a smart metering system for electricity and water. Plans are also underway to introduce initiatives which will reduce fuel subsidies without affecting the vulnerable. To support budget execution, the monitoring system has been strengthened by introducing the e-invoice system for procurements. They are currently reviewing the current tax policy and structure, and the feasibility to further broaden the current tax base. Efforts are underway to implement a medium-term expenditure framework and to improve budget presentation. They also plan to focus more on the non-oil balance to delink fiscal policy from oil price volatilities.

B. Structural Reforms to Support Diversification, Inclusive Growth, and Job Creation

23. The authorities' initiatives toward economic diversification are commendable, but challenges remain. To support the Wawasan Brunei 2035 development plan, the authorities have focused on five priority business clusters: Downstream O&G, Food, Tourism, Services, and ICT. Brunei's characteristics, however, pose challenges. Its small size makes it difficult to exploit economies of scale. Like other oil exporters, private sector activity remains weak, while the preference for public sector employment limits private sector growth.

24. The efforts to enhance the business environment need to be sustained. Brunei has made important progress in improving the business climate. For example, from 2016 to 2019, Brunei made strides in improving the World Bank Doing Business scores, with strong progress in access to credit and starting a business (Figure 6). More reforms, however, are needed to further improve the ease of doing business scores, in particular, in registering property and trading across borders. Making the regulatory framework more consultative, transparent and predictable would also help improve the business environment. A better business environment is paramount to support private sector-led growth and reduce unemployment, including youth unemployment.

25. Brunei should continue efforts to attract quality FDI, while deepening its global integration. Brunei has attracted sizable FDI in the five business clusters, mainly in the downstream O&G sector. The expansion and modernization of the Muara Port, and trade agreements (for example, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, CPTPP) may further enhance Brunei's attractiveness for FDI and help global integration. More efforts are needed to generate stronger positive spillovers from FDI to the domestic economy, including by integrating local MSMEs into the supply chains. Brunei would also benefit from further improving trade facilitation, such as advance rulings, information availability, and formalities (for example, promoting more automated process for Customs). In this regard, staff welcomes the introduction of the common online platform (the National Single Window), which will reduce face-to-face interactions and increase economic efficiency. Linking the National Single Window and the ports' Equipment Interchange Receipts would further enhance trade facilitation. The authorities are also making progress in advance rulings as part of the preparation to ratify the CPTPP.

26. The government's focus on human capital development and private sector employment is welcome but incentive structures could be further improved. The authorities have set up centers and programs, such as JobCenter Brunei, I-Ready, and the Center for Capacity Building, to foster job opportunities and increase job matching. These steps need to be accompanied by reforms to remove structural rigidities. For example, labor market and civil service reforms should continue to encourage Bruneians to create and seek private sector jobs and ensure that talent is directed to its most productive uses. This will require incentives for private sector employment—by aligning public and private sector wages and benefits, lowering reservation wages by signaling that government employment will be limited, and supporting entrepreneurship and private sector competitiveness. Policies should aim at building expertise in the five priority business clusters, while investment in human capital should target the specific skills needed in these clusters. Policies should also aim at boosting sectors, rather than specific firms, and preserving competition. The authorities should continue to support MSME development, while holding the recipients accountable. In this regard, encouraging start-ups and established firms to compete in international markets will provide discipline and valuable market signals to gauge performance.

27. Digitalization can support diversification efforts, given Brunei's young and tech-savvy population. The authorities have identified digitalization as one of the five priority business clusters. To maximize the benefit of digitalization, policies should focus on upgrading physical and soft infrastructure, and improving the quality of education. Digitalization brings innovation and new opportunities, generating potentials for new jobs that give young people comparative advantages. For example, e-commerce could overcome challenges stemming from Brunei's small market size. Moreover, initiatives such as coding bootcamps could help tackle youth unemployment.

Authorities' Views

28. The authorities emphasized the progress made in economic diversification, while recognizing that more efforts are needed to reach the objectives of the Wawasan Brunei 2035. While Brunei's small size poses challenges, they have a comprehensive strategy and government agencies are working coherently toward the same goals. The government is tackling the diversification reforms from a position of strength, given Brunei's strong external and fiscal buffers. The authorities agreed on the need to better integrate and generate stronger positive spillovers from the FDI sector to the rest of domestic economy. They plan to leverage these large projects to develop further downstream activities, which would support MSMEs and create high-quality jobs for Bruneians. In addition, to achieve private sector-led growth, the government strategy encompasses corporatization, public-private partnership, and privatization. The government also continues to introduce and implement reforms under the Ease of Doing Business initiatives. Furthermore, the authorities remained committed to promote and facilitate cross border trade and investment, among others, through participation in various free trade agreements such as ASEAN and its Plus One FTAs and economic cooperation at bilateral, regional and international forums which are aimed at increasing market access/outreach for regional and international markets for local products. They highlighted that the government has undertaken various initiatives in encouraging Bruneians to pursue jobs in the private sector, including the creation of the Manpower Planning Council to strategize and coordinate efforts in increasing employment, while leveraging the programs such as I-Ready and Center for Capacity Building. To harness the benefits of digitalization, the authorities have taken many initiatives, including establishing the Digital Economy Council and the Unified National Networks.

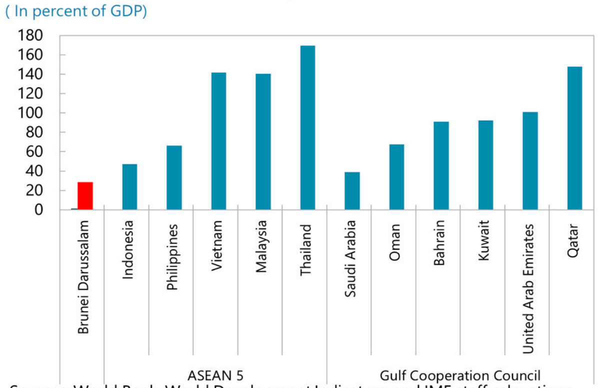
C. Developing the Financial Sector while Preserving Financial Stability and Integrity

29. While sound overall, the financial system is bank dominated and shallow (Appendix VI). The banking sector accounts for 83.3 percent of total financial sector assets, equivalent to about 100 percent of GDP. Islamic banks account for 65.6 percent of banking assets. The banks' offshore assets represent 53 percent—consequently, total domestic credit provided by the financial sector stands at about 30 percent of GDP, the lowest compared to peers.

30. Staff supports the authorities' reforms to foster financial sector development as laid out in the Financial Sector Blueprint 2016–25:

- Steps to broaden the investor base, establish a secondary bond market, and develop the required infrastructure and rules for establishing a stock exchange are commendable. The authorities' plans to develop Brunei as one of the international Islamic finance hubs in niche areas as part of the economic diversification strategy are

Domestic Credit Provided by Financial Sector, Latest
(In percent of GDP)



Sources: World Bank, World Development Indicators; and IMF staff calcuations.

also welcome. Progress in issuing sukuks at longer maturities would help build a yield curve and develop the private sector.

- The authorities have introduced conventional and Sharia-compliant overnight standing facilities, which will support liquidity management and facilitate smooth functioning of the financial system. The recent implementation of the Bureau Credit Score will improve access to credit, increase transparency in lending, and ensure discipline in the financial sector.
- As part of modernizing its financial infrastructure, the Autoriti Monetari Brunei Darussalam (AMBD) published the Digital Payment Roadmap 2019-25 and issued a fintech regulatory sandbox.

31. Strengthening banking supervision and regulation, and building a macroprudential framework are vital to preserve financial stability and integrity:

- The authorities have taken a range of measures to develop the macroprudential framework and supervisory system. Staff welcomes the recent implementation of International Financial Reporting Standard (IFRS) 9 by financial institutions. Implementation of all the three pillars of Basel II is an important milestone in increasing the resilience of the banking system. The AMBD has made progress in developing the Domestic Systemically Important Banks framework. The authorities are also developing a top-down stress testing framework and have planned to introduce the Counter-Cyclical Capital Buffer for the banking sector. Given the size of banking assets placed offshore, the AMBD should closely monitor the potential risks emanating from external shocks. The planned publication of the first financial stability report would be an important communication tool.
- Continued efforts are needed to put in place a bank resolution framework and contingency planning for crisis management. As a first step, the authorities have set up a working group to develop the framework, including the requirement for banks to submit their own recovery plans.
- Staff supports the recent progress in strengthening the AML/CFT framework and the additional measures planned for the upcoming mutual evaluation, including measures to support anti-corruption efforts, while underscoring the need of coordination among concerned agencies.

Authorities' Views

32. The authorities are mindful to progress financial sector development while preserving financial stability and integrity. The authorities remain committed to strengthening and improving financial infrastructures including through digitalization to foster financial sector development, drive new financial linkages internationally, and potentially develop Brunei as one of the Islamic finance hubs. They welcomed staff's acknowledgement on the ongoing efforts to strengthen banking supervision and regulation. The authorities will continue to advance the efforts in developing a crisis management framework, strengthening the financial sector through developments in liquidity management and upgrading macroprudential framework for effective financial sector oversight. In this regard, they welcomed the recommendations of the IMF TA on building a macroprudential framework. Regarding AML/CFT, the authorities highlighted that they are implementing the third cycle of national strategy, focusing on the upcoming mutual evaluation.

D. Data Issues and Capacity Building

33. Further progress in data compilation and dissemination is needed. Staff supports the authorities' commitment to international data standards and best practices, including the adoption of IFRS 9. The authorities should address delays in releasing national account and balance of payments data and increase data quality. Staff welcomes the authorities' commitment to publish the National Summary Data Page (NSDP), in line with the recent IMF TA on e-GDDS. Publishing data through the NSDP would help reduce data gaps and increase transparency. The authorities should strengthen capacity on gross external debt reporting. In that regard, staff welcomes the authorities' plan to request TA from the IMF, including on balance of payments and national account.

Authorities' Views

34. The authorities agreed on the need for further progress in data compilation and publication. The authorities will improve data dissemination through the e-GDDS in line with the recent IMF TA. They also expressed strong interest in IMF TA and trainings on data compilation and quality. The authorities acknowledged the various IMF TA and capacity building trainings. In this regard, they called for IMF's flexibilities on the conditions for the provision of these programs for Brunei Darussalam.

STAFF APPRAISAL

35. Brunei Darussalam's economy has been adjusting to the lower O&G prices since 2014, with the authorities undertaking wide-ranging reforms. Brunei has made significant progress in consolidating the fiscal position, improving the business climate, attracting FDI, developing the financial sector, and strengthening regulation. Growth is expected to pick up in 2019, with the outlook improving further over the medium term, driven by a pickup in the O&G sector and large investment projects. Nevertheless, Brunei faces challenges and risks. Future oil production and prices remain uncertain. Against this backdrop, the reforms should continue to ensure long-term sustainability and intergenerational equity, increase productivity and competitiveness, diversify the sources of growth, reduce unemployment—especially youth unemployment, and build resilience to shocks.

36. Staff supports the authorities' fiscal consolidation program, although more ambition is called for to bring the fiscal position gradually closer to that implied by intergenerational equity considerations. Over the medium term, staff recommends: (i) continue reforms in public services and the wage bill, including streamlining civil service vacancies, (ii) reform fuel subsidies, (iii) rebalance further budget spending toward growth-enhancing activities, and (iv) increase non-O&G revenues. Adopting a formal medium-term fiscal framework would help control spending and delink it from O&G revenue fluctuations. Digitalization can help improve public financial management.

37. The peg to the Singapore dollar remains appropriate, providing a credible nominal anchor and stability to the financial system. The external position is assessed to be weaker in 2018 than fundamentals. However, the current account balance, on current policies, is expected to rebound, closing the gap over the medium term as new downstream exports rise.

38. The authorities' initiatives toward economic diversification are commendable. Brunei has made strides in improving business environment, while attracting sizable FDI in the priority business clusters, mainly in the downstream O&G sector. Going forward, continued efforts are needed to further improve the business environment, attract quality FDI, enhance human capital, and reform labor market to foster private sector led-growth and reduce unemployment.

39. Staff supports the authorities' initiatives to develop the financial sector, while safeguarding financial stability and integrity. The initiatives include steps to broaden the investor base, establish a secondary bond market, develop the required infrastructure and rules for establishing a stock exchange, and put all the three pillars of Basel II in place. Given the size of banking assets placed offshore, the AMBD should closely monitor the potential risks emanating from external shocks. Staff supports the recent progress in strengthening the AML/CFT framework and the additional measures planned for the upcoming mutual evaluation.

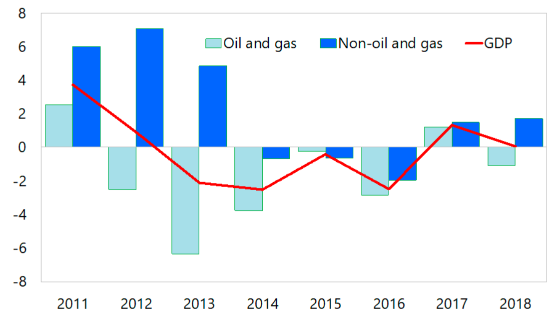
40. The authorities should address the remaining data gaps. Staff welcomes the authorities' commitment to publishing the NSDP in line with the recent IMF TA on e-GDDS, as well as the authorities' plan to request further TA from the IMF to improve data collection and dissemination.

41. It is expected that the next Article IV consultation with Brunei Darussalam will be held on the standard 12-month cycle.

Figure 1. Brunei Darussalam: Real and Fiscal Indicators

Real GDP growth was lower than expected, with the recovery in the non-O&G sector offset by a decline in the O&G sector…

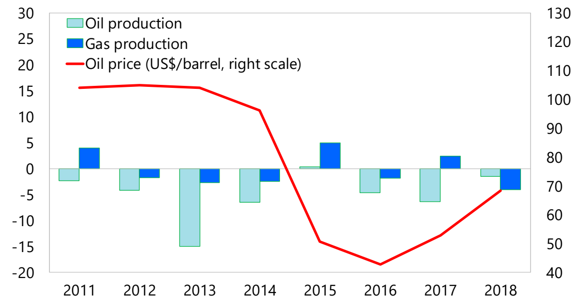
Real GDP Growth
(In percent)



Sources: Brunei authorities; and IMF staff estimates.

…as both crude oil and LNG production declined despite higher oil prices.

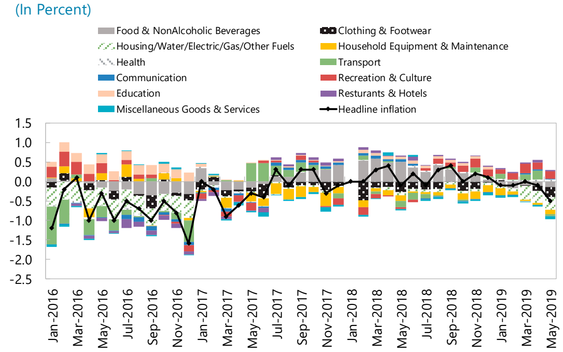
Energy Sector Production and Oil Price
(Year-on-year percent change)



Sources: Brunei authorities; CEIC Data Co. Ltd; IMF, *World Economic Outlook*; and IMF staff estimates.

Inflation was higher in 2018 but turned negative again this year.

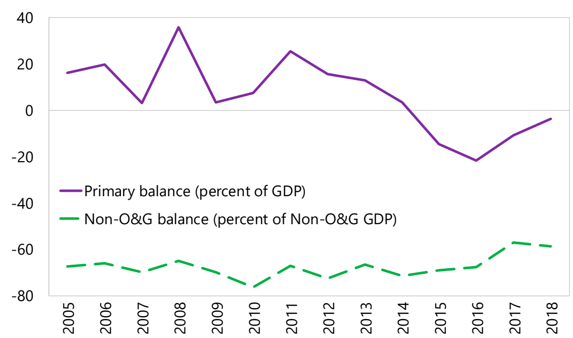
Inflation Decomposition
(In Percent)



Sources: Brunei authorities data; and IMF staff calculations.

The fiscal balance improved significantly…

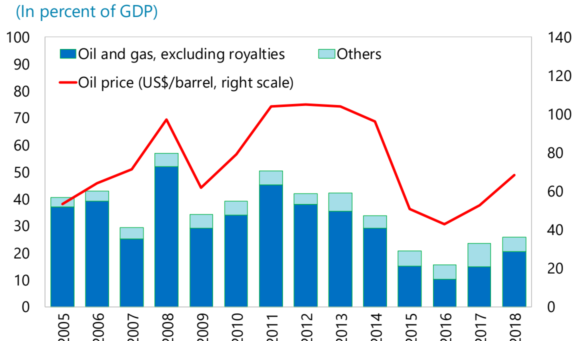
Fiscal Balance



Sources: Brunei authorities; and IMF staff estimates.

…driven by higher O&G prices…

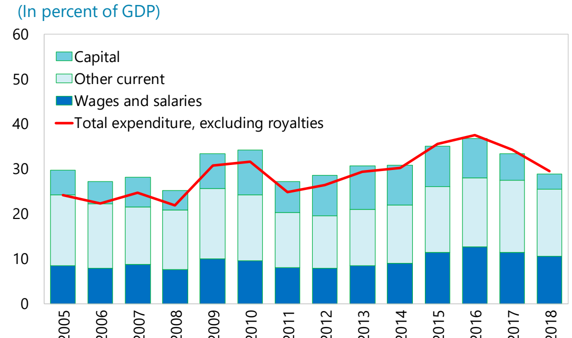
Fiscal Revenues
(In percent of GDP)



Sources: Brunei authorities; and IMF staff estimates.

…and compressed government spending.

Fiscal Expenditure
(In percent of GDP)



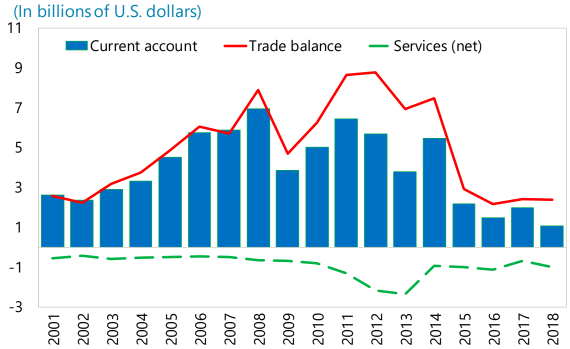
Sources: Brunei authorities; and IMF staff estimates.

Figure 2. Brunei Darussalam: External and Financial Indicators

The current account surplus narrowed in 2018…

External Balances

(In billions of U.S. dollars)

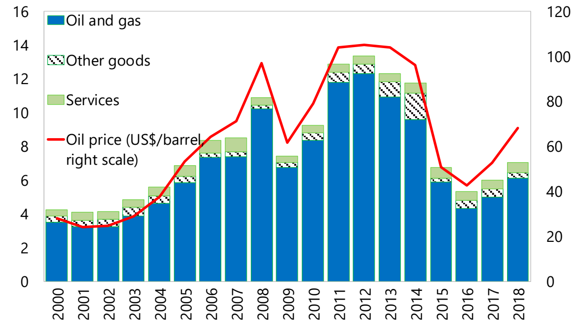


Sources: Brunei authorities; and IMF staff estimates.

…as higher O&G exports…

Export Composition

(In billions of U.S. dollars)

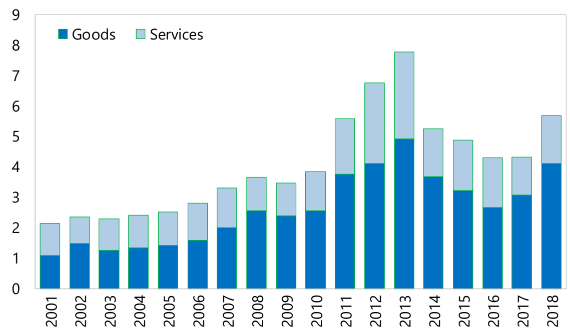


Sources: Brunei authorities; and IMF staff estimates.

…were more than offset by higher imports linked to infrastructure projects.

Import Composition

(In billions of U.S. dollars)

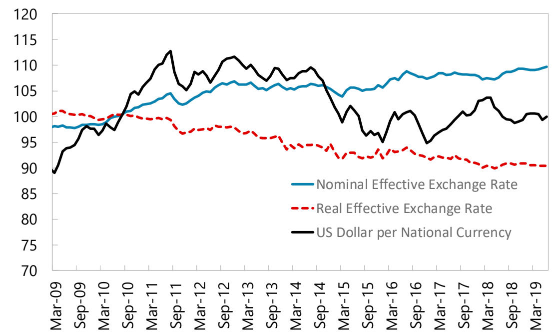


Sources: Brunei authorities; and IMF staff estimates.

The peg to the Singapore dollar has resulted in a stable real effective exchange rate.

Exchange Rates

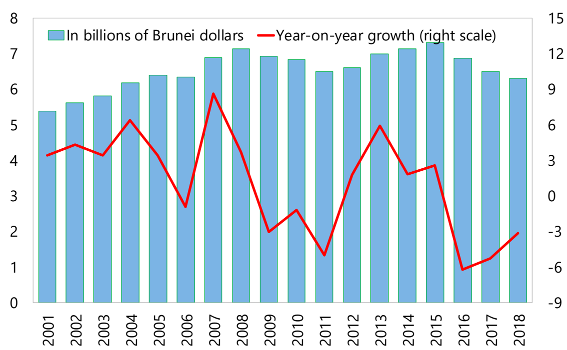
(Index, 2010=100)



Sources: IMF, *International Financial Statistics*.

The decline in credit growth to the private sector slowed in 2018 …

Credit to Private Sector

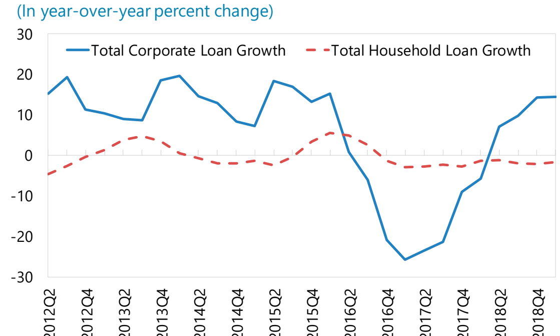


Sources: IMF, *International Financial Statistics*.

…mainly due to a rebound in corporate credit growth.

Brunei Darussalam: Loan Growth, 2012–2019

(In year-over-year percent change)



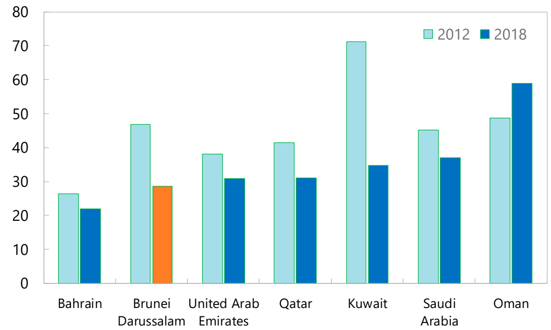
Sources: Autoriti Monetari Brunei Darussalam; and IMF staff estimates.
Note: Latest observation is 2019Q1.

Figure 3. Brunei Darussalam: Fiscal Indicators in Comparison with GCC Countries

Brunei's fiscal revenue since 2012 has reflected O&G shocks…

General Government Revenue

(In Percent of GDP)

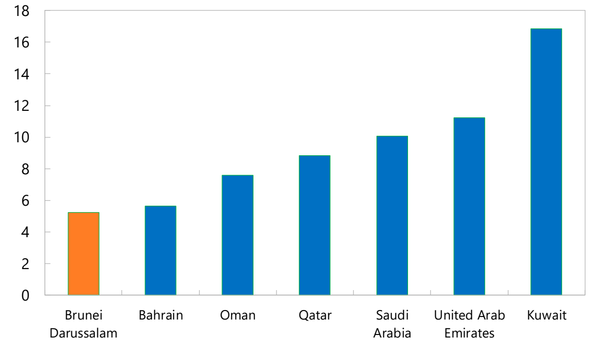


Sources: IMF, World Economic Outlook.

…given its small non-O&G revenue.

Non-oil and gas Revenue

(In Percent of GDP)

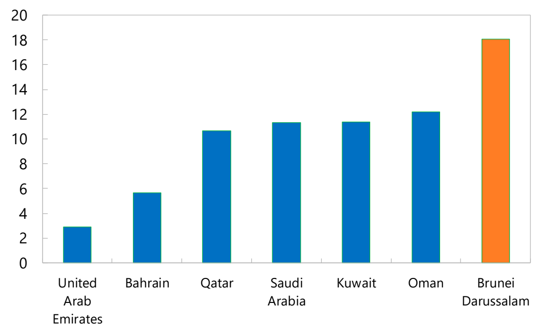


Sources: Bruneian Authorities; IMF Staff calculations.

Brunei has made significant progress in fiscal consolidation.

Fiscal Consolidation, 2016-18

(In Percent of GDP)



Sources: IMF, World Economic Outlook; IMF Staff calculations.

Brunei's hydrocarbon generating capacity appears relatively modest compared to GCC countries.

Oil and Gas Production in GCC Countries and Brunei (2018)

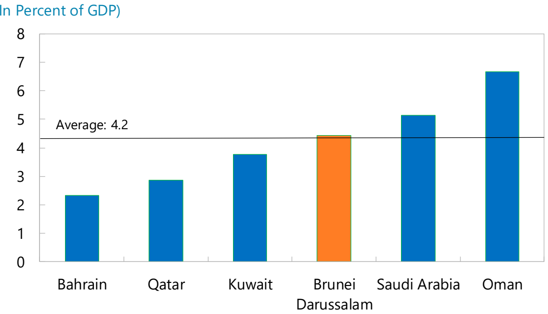
	Oil [1]	Natural gas [2]	Population (Millions)
Saudi Arabia	12,287.0	96.4	33.4
United Arab Emirates	3,942.0	55.6	9.3
Kuwait	3,049.0	15.0	4.6
Qatar	1,879.0	150.9	2.8
Oman	978.0	30.9	4.6
Bahrain		12.8	1.5
Brunei Darussalam	112.0	10.8	0.4

Source: BP Statistical Review of World Energy, 2019; IMF, WEO; International Energy Agency.
1/ In thousands of barrels per day. Includes crude oil, shale oil, oil sands and natural gas liquids.
2/ In million tonnes oil equivalent.

Brunei's public education expenditures are in line with its peers…

Public Education Expenditure, latest year available

(In Percent of GDP)

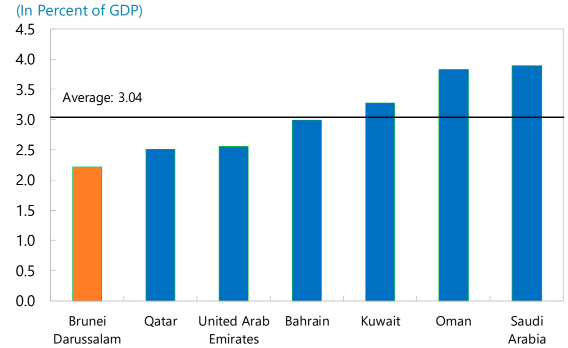


Sources: IMF, World Economic Outlook; World Bank; IMF Staff Calculations.
Note: Data for Brunei are as of 2016, while data for the other economies range between 2006 and 2017 depending on availability.

…while health expenditure lags somewhat that of peers.

Public Health Expenditure, 2016

(In Percent of GDP)

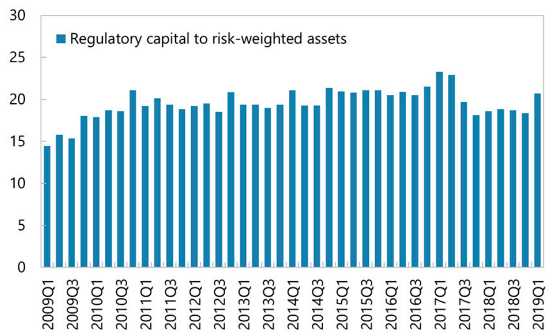


Sources: IMF, World Economic Outlook; World Bank; IMF Staff Calculations.

Figure 4. Brunei Darussalam: Financial Stability Indicators

The banking sector is well capitalized…

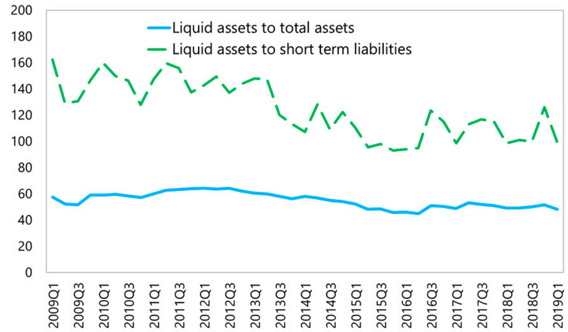
Capital Adequacy
(In Percent)



Sources: Brunei Authorities; and IMF staff estimates.

…and maintains ample liquidity…

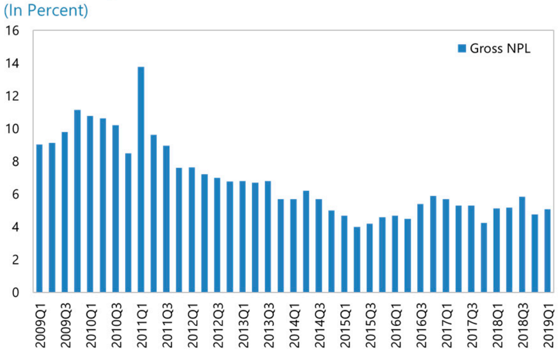
Liquidity
(In Percent)



Sources: Brunei Authorities; and IMF staff estimates.

…while non-performing loans remained stable…

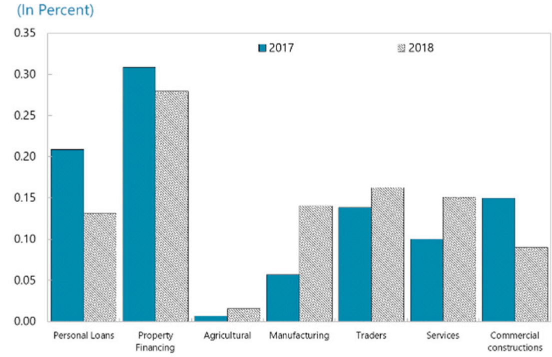
Asset Quality
(In Percent)



Sources: Brunei Authorities; and IMF staff estimates.

…mainly explained by the housing sector.

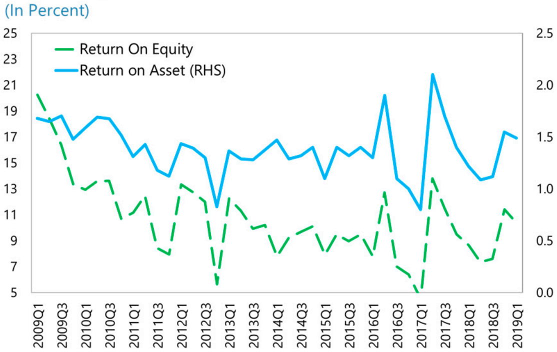
Sectoral Non Performing Loans Contributions
(In Percent)



Sources: Brunei authorities; and IMF staff estimates.

Banks remained profitable…

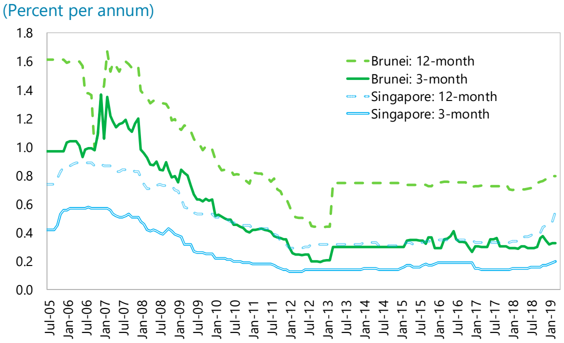
Profitability
(In Percent)



Sources: Brunei Authorities; and IMF staff estimates.

…and deposit rates remained broadly unchanged.

Deposit Rates
(Percent per annum)



Sources: IMF, *International Financial Statistics*; and CEIC Data Co. Ltd.

Figure 5. Brunei Darussalam: Socioeconomic Developments

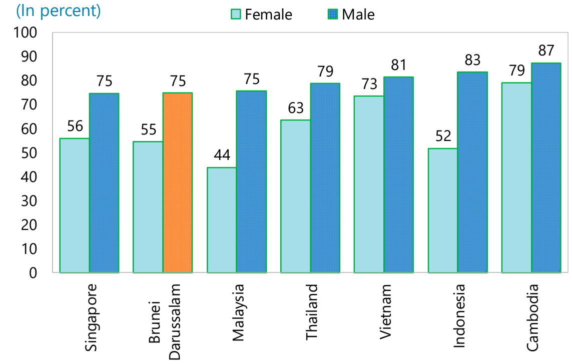
Bruneians enjoy a high level of per-capita income, but in contrast to Asian peers, it has contracted in recent years reflecting low oil price and production.

Per Capita GDP, 2013 and 2018
(In U.S. dollars)

Source: IMF, *World Economic Outlook*.

Brunei's labor force participation is low both for male and female compared to regional peers.

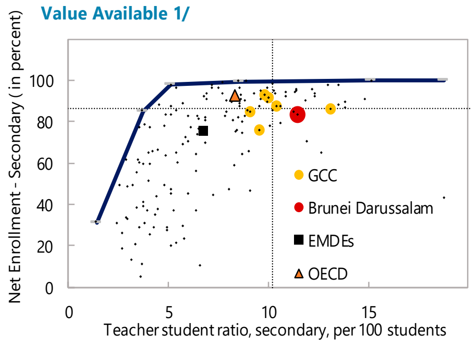
Labor Force Participation Rates, 2018
(In percent)



Source: International Labor Organization, *Labor Statistics*.

There is room to increase Brunei's social spending efficiency both for education…

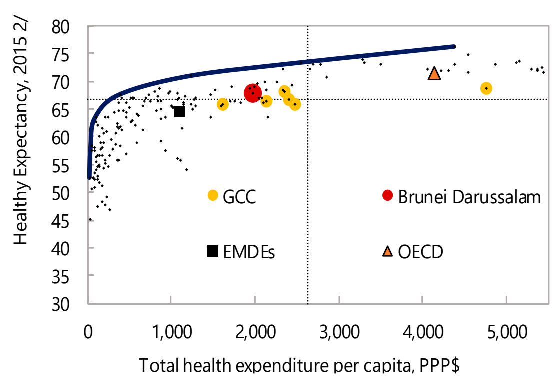
Teachers and Outcome, secondary, Latest Value Available 1/



Source: IMF FAD Expenditure Assessment Tool (EAT), World Bank
1/ Dashed lines are the average of GCC.

…and for healthcare.

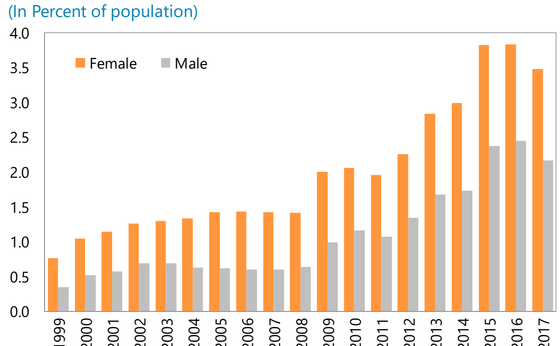
Health Efficiency Frontier, Latest Value Available 1/



Source: IMF FAD Expenditure Assessment Tool (EAT), World Bank
1/ Dashed lines are the average of GCC.
2/ Healthy life expectancy is the number of years expected in full health.

University enrollment is low, particularly for males.

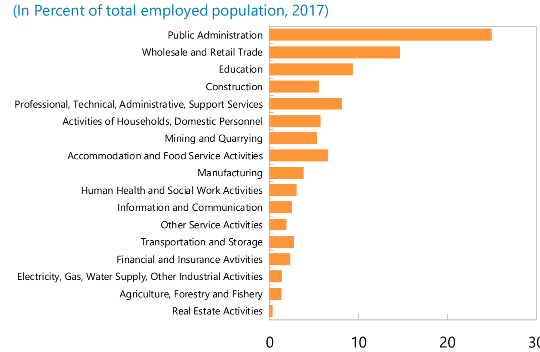
University Enrollment
(In Percent of population)



Sources: CEIC Data Co. Ltd.; and IMF staff estimates.

The public sector employs the largest share of the labor force.

Distribution of Employed Population by Industry
(In Percent of total employed population, 2017)

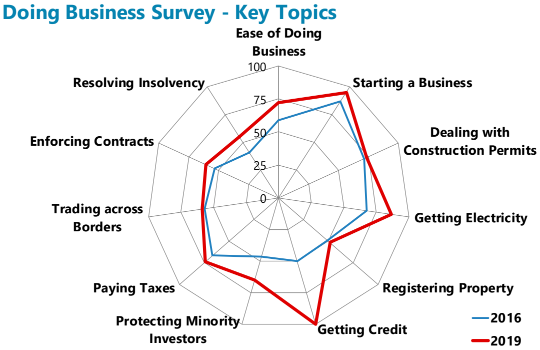


Source: Brunei Department of Statistics, Labor Force Survey 2017.

Figure 6. Brunei Darussalam: Doing Business and Governance Indicators

Brunei has made progress in improving its business climate…

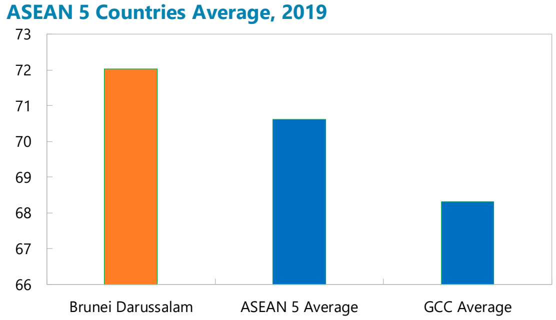
Doing Business Survey - Key Topics



Sources: The World Bank Group, *Doing Business*; and IMF staff calculations.
Note: Scores further away from the center indicate better performance.

…and, as a result, Brunei scores well compared with its peers…

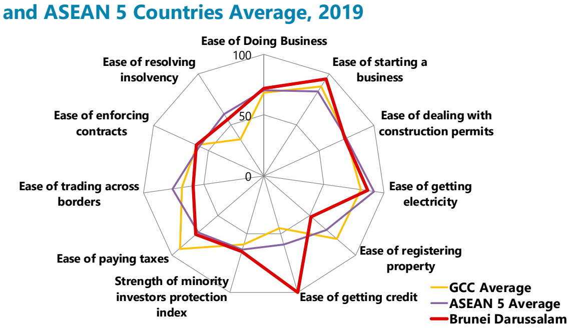
Ease of Doing Business Global Scores for Brunei, GCC and ASEAN 5 Countries Average, 2019



Sources: The World Bank Group, *Doing Business*; and IMF staff calculations.
Note: Higher is better. ASEAN 5 include Indonesia, Malaysia, Philippines, Singapore, and Thailand.

…in particular, it stands out in areas such as starting a business and getting credit, while it needs to improve registering property and trading across borders.

Doing Business Survey - Key Topic Scores for Brunei, GCC and ASEAN 5 Countries Average, 2019

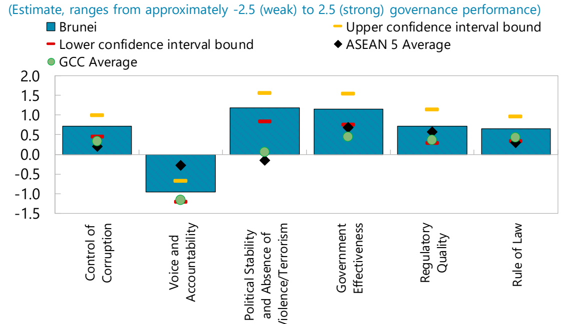


Sources: The World Bank Group, *Doing Business*; and IMF staff calculations.
Note: Scores further away from the center indicate better performance. ASEAN 5 include Indonesia, Malaysia, Philippines, Singapore, and Thailand.

Brunei performs well in many governance indicators.

Worldwide Governance Indicators, 2017

(Estimate, ranges from approximately -2.5 (weak) to 2.5 (strong) governance performance)

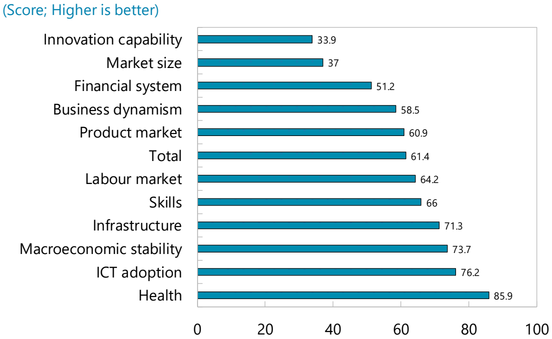


Sources: Worldwide Governance Indicators (2017); and IMF staff calculations. ASEAN 5 include Indonesia, Malaysia, Philippines, Singapore, and Thailand.
Note: WGI is a perception-based indicator, summarizing views of enterprises, citizens and expert survey respondents on the quality of governance in a country.

Competitiveness indicators show that Brunei stands out in health, technology, and infrastructure, but its small market size poses challenges.

Global Competitiveness Indicators by Category, 2018

(Score; Higher is better)

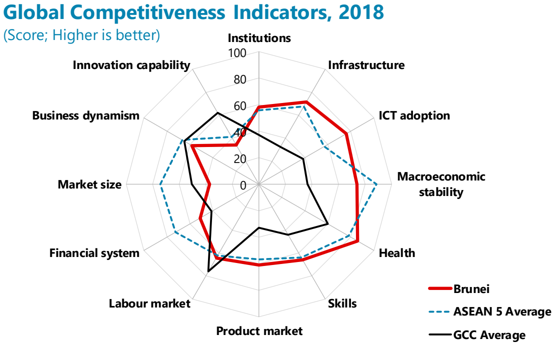


Sources: World Economic Forum, The Global Competitiveness Report 2018, and IMF staff calculations.

Compared with its peers, Brunei's competitiveness can benefit from improvement of its financial system and business dynamism.

Global Competitiveness Indicators, 2018

(Score; Higher is better)



Sources: World Economic Forum, The Global Competitiveness Report 2018, and IMF staff calculations. ASEAN 5 include Indonesia, Malaysia, Philippines, Singapore, and Thailand.

Table 1. Brunei Darussalam: Selected Economic and Financial Indicators, 2014-24

Area: 5,765 sq. kilometers
Population (2018): 442,400
Nominal GDP per capita (2018): US$30,668
Main export destinations (2018): Japan (34.7), Thailand (10.1), Australia (8.8), Korea (8.6)
Unemployment rate (2017): 9.3%
Labor force participation rate (2017): total 62.7%; male 68.9%; female 56.5%

	2014	2015	2016	2017	2018	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Output and prices											
Nominal GDP (millions of Brunei dollars)	21,664	17,778	15,748	16,747	18,301	16,907	17,281	17,498	17,879	18,213	18,575
Nominal non-oil and gas GDP (millions of Brunei dollars)	7,733	7,658	7,463	7,521	7,595	7,653	8,048	8,302	8,554	8,709	8,877
Real GDP (percentage change) 1/	-2.5	-0.4	-2.5	1.3	0.1	1.8	4.7	3.6	3.5	2.4	2.1
Oil and gas sector GDP	-3.7	-0.2	-2.8	1.2	-1.1	2.4	3.2	3.3	3.5	2.9	2.6
Non-oil and gas sector GDP	-0.8	-0.6	-1.9	1.5	1.7	1.0	6.8	4.0	3.6	1.8	1.5
Oil production ('000 barrels/day)	126	127	121	113	112	115	118	122	126	129	132
Natural gas output (millions cu. ft./day)	1,170	1,228	1,205	1,234	1,184	1,205	1,246	1,291	1,342	1,382	1,421
Average Brunei oil price (U.S. dollars per barrel)	104.4	53.9	44.6	55.9	73.2	65.5	61.9	59.8	59.0	59.0	59.3
Average Brunei gas price (U.S. dollars per million BTU)	16.6	10.6	7.3	8.3	10.5	6.5	7.3	7.3	7.3	7.3	7.3
Consumer prices (period average, percentage change)	-0.2	-0.4	-0.7	-0.2	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Consumer prices (end of period, percent change)	1.2	-1.0	-1.6	0.0	0.0	0.1	0.2	0.2	0.2	0.2	0.2
				(In percent of GDP)							
Public finances: budgetary central government											
Total revenue	37.7	24.2	17.7	26.0	28.6	23.9	24.1	23.8	23.6	24.2	24.9
Oil and gas	32.9	18.4	12.3	17.4	23.4	17.9	18.1	17.6	17.4	18.0	18.8
Other	4.7	5.8	5.4	8.6	5.2	6.0	6.1	6.2	6.2	6.1	6.1
Total expenditure	34.1	38.7	39.4	36.6	32.2	35.4	35.5	34.9	34.1	33.5	32.9
Current	25.3	29.6	30.6	30.7	28.9	31.5	30.8	30.4	29.7	29.2	28.6
Capital	8.8	9.1	8.7	5.9	3.3	3.8	4.6	4.6	4.5	4.4	4.3
Overall balance 2/	3.6	-14.5	-21.7	-10.6	-3.6	-11.5	-11.3	-11.1	-10.5	-9.4	-8.0
Non-oil and gas overall deficit (In percent of non-oil and gas GDP)	-71.5	-68.9	-67.7	-57.1	-58.6	-60.0	-58.2	-55.8	-53.6	-52.5	-51.3
				(12-month percent change)							
Money and banking											
Private sector credit	1.8	2.6	-6.2	-5.3	-3.1	0.4	1.0	1.6	1.5	1.2	1.0
Narrow money	-1.5	6.4	-0.1	-5.7	-3.0	1.9	3.1	3.7	3.6	2.7	2.0
Broad money	3.2	-1.8	1.5	-0.4	2.8	3.9	3.3	3.1	2.7	2.3	2.2
				(In millions of U.S. dollars, unless otherwise indicated)							
Balance of payments											
Goods	7,479	2,910	2,154	2,403	2,364	1,605	2,157	2,424	2,764	3,094	3,502
Exports	11,149	6,127	4,813	5,475	6,470	4,952	7,180	8,098	8,474	8,723	8,868
Of which: oil and gas	9,604	5,909	4,321	5,021	6,114	4,775	4,801	4,724	4,876	5,015	5,148
Imports	3,670	3,217	2,659	3,072	4,105	3,347	5,022	5,674	5,710	5,629	5,366
Services (net)	-955	-1,007	-1,114	-698	-1,005	-709	-745	-770	-792	-818	-832
Primary income (net)	-20	650	835	721	215	614	593	634	636	643	629
Secondary income (net)	-1,045	-397	-404	-442	-506	-451	-466	-474	-464	-468	-469
Current account balance	5,459	2,157	1,470	1,985	1,068	1,060	1,539	1,814	2,144	2,452	2,831
Current account balance (in percent of GDP)	31.9	16.7	12.9	16.4	7.9	8.5	12.0	13.8	15.9	17.6	19.8
Gross official reserves 3/	3,471	3,211	3,322	3,300	3,221	3,327	3,435	3,543	3,654	3,764	3,876
In months of next year's imports of goods and services	8.6	9.0	9.2	7.0	8.3	6.3	5.9	6.0	6.2	6.6	...
Brunei dollars per U.S. dollar (period average)	1.27	1.37	1.38	1.38	1.35	...	...	...	...	...	...
Brunei dollar per U.S. dollar (end of period)	1.32	1.41	1.44	1.35	1.37	...	...	...	...	...	...

Sources: Data provided by the Brunei authorities; and Fund staff estimates and projections.

1/ Non-oil and gas GDP includes the downstream sector.
2/ In absence of government debt and interest payments, this is also primary balance.
3/ Comprises foreign exchange assets of Autoriti Monetari Brunei Darussalam, SDR holdings, and reserve position in the Fund.

Table 2. Brunei Darussalam: Budgetary Central Government Developments, 2014/15–2024/25[1]

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20 Proj.	2020/21 Proj.	2021/22 Proj.	2022/23 Proj.	2023/24 Proj.	2024/25 Proj.
					(In millions of Brunei dollars)						
Revenue	7,076	3,709	3,583	3,873	6,006	4,077	4,171	4,178	4,263	4,453	4,616
Tax	4,856	2,115	1,934	1,508	3,352	2,069	2,132	2,118	2,167	2,325	2,463
Oil and gas	4,444	1,692	1,595	1,162	3,004	1,711	1,758	1,733	1,772	1,922	2,055
Other	412	423	339	347	348	358	374	385	395	402	408
Nontax revenue	2,220	1,593	1,649	2,365	2,654	2,007	2,039	2,060	2,096	2,129	2,153
Oil and gas 2/	1,599	1,029	698	1,662	1,737	1,339	1,353	1,359	1,383	1,410	1,430
Other	621	564	951	703	917	669	686	700	713	719	723
Revenue excluding royalties	6,339	3,216	3,197	3,451	5,523	3,671	3,749	3,750	3,826	4,008	4,278
Expenditure	7,290	6,339	6,250	6,077	5,951	6,020	6,127	6,111	6,104	6,109	6,106
Current	5,471	4,981	4,964	5,190	5,455	5,333	5,327	5,311	5,304	5,309	5,306
Wages and salaries	1,984	1,985	1,977	1,859	1,953	1,952	1,955	1,959	1,963	1,965	1,960
Other	3,487	2,996	2,987	3,331	3,502	3,381	3,371	3,352	3,341	3,344	3,346
Of which: Royalty payments	779	391	350	356	384	381	397	402	411	419	425
Capital	1,819	1,358	1,286	887	495	688	800	800	800	800	800
Of which: Development expenditure	1,079	791	684	887	495	688	800	800	800	800	800
Expenditure excluding royalties	6,511	5,948	5,900	5,721	5,566	5,639	5,730	5,709	5,693	5,690	5,681
Overall balance 3/	-215	-2,630	-2,667	-2,204	55	-1,944	-1,956	-1,933	-1,842	-1,656	-1,490
Overall balance excluding royalties 4/	-173	-2,732	-2,703	-2,270	-121	-1,968	-1,981	-1,959	-1,868	-1,682	-1,404
Non-oil and gas overall deficit 4/	-5,450	-4,947	-4,443	-4,604	-4,195	-4,613	-4,669	-4,624	-4,585	-4,569	-4,550
Investment income 5/	1,124	1,064	1,125	1,376	1,458	1,220	1,196	1,230	1,232	1,234	1,220
Balance including investment income 5/	909	-1,566	-1,542	-828	1,514	-724	-760	-703	-610	-422	-270
					(In percent of GDP)						
Revenue	34.4	21.7	22.5	22.7	32.6	24.0	24.1	23.7	23.7	24.3	24.9
Tax	23.6	12.4	12.2	8.8	18.2	12.2	12.3	12.0	12.1	12.7	13.3
Oil and gas	21.6	9.9	10.0	6.8	16.3	10.1	10.1	9.9	9.9	10.5	11.1
Other	2.0	2.5	2.1	2.0	1.9	2.1	2.2	2.2	2.2	2.2	2.2
Nontax revenue	10.8	9.3	10.4	13.9	14.4	11.8	11.8	11.7	11.7	11.6	11.6
Oil and gas 2/	7.8	6.0	4.4	9.7	9.4	7.9	7.8	7.7	7.7	7.7	7.7
Other	3.0	3.3	6.0	4.1	5.0	3.9	4.0	4.0	4.0	3.9	3.9
Revenue excluding royalties	30.8	18.8	20.1	20.2	30.0	21.6	21.6	21.3	21.3	21.9	23.0
Total expenditure	35.4	37.2	39.3	35.6	32.3	35.4	35.3	34.7	34.0	33.4	32.9
Current	26.6	29.2	31.2	30.4	29.6	31.4	30.7	30.2	29.5	29.0	28.6
Wages and salaries	9.6	11.6	12.4	10.9	10.6	11.5	11.3	11.1	10.9	10.7	10.6
Other	16.9	17.6	18.8	19.5	19.0	19.9	19.4	19.1	18.6	18.3	18.0
Capital	8.8	8.0	8.1	5.2	2.7	4.0	4.6	4.5	4.5	4.4	4.3
Of which: Development expenditure	5.2	4.6	4.3	5.2	2.7	4.0	4.6	4.5	4.5	4.4	4.3
Expenditure excluding royalties	31.6	34.9	37.1	33.6	30.2	33.2	33.1	32.4	31.7	31.1	30.6
Overall balance 3/	-1.0	-15.4	-16.8	-12.9	0.3	-11.4	-11.3	-11.0	-10.3	-9.0	-8.0
Non-oil and gas overall deficit 4/	-26.5	-29.0	-27.9	-27.0	-22.7	-27.1	-26.9	-26.3	-25.5	-25.0	-24.5
In percent of non-oil and gas GDP	-70.5	-65.1	-59.6	-61.3	-54.9	-59.5	-57.6	-55.3	-53.4	-52.2	-51.3
Memorandum items:											
Nominal GDP (in millions of Brunei dollars)	20,581	17,063	15,905	17,048	18,440	17,000	17,335	17,593	17,963	18,303	18,575
Non-oil and gas GDP (in millions of Brunei dollars)	7,735	7,600	7,449	7,508	7,636	7,752	8,112	8,365	8,593	8,751	8,877
Investment income (percent of GDP) 5/	5.5	6.2	7.1	8.1	7.9	7.2	6.9	7.0	6.9	6.7	6.6
Balance including investment income (percent of GDP) 5/	4.4	-9.2	-9.7	-4.9	8.2	-4.3	-4.4	-4.0	-3.4	-2.3	-1.5

Sources: Data provided by the Brunei authorities; and Fund staff estimates and projections.

1/ *GFSM 1986* Presentation (cash-based); fiscal year ends March 31.
2/ Includes energy sector royalties and dividends.
3/ In absence of government debt and interest payments, this is also primary balance.
4/ Excludes collection and disbursement of royalties and capital transfers.
5/ Includes Fund staff estimates of investment income.

Table 3. Brunei Darussalam: Balance of Payments, 2014–24[1]

	2014	2015	2016	2017	2018	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
	(In millions of U.S. dollars; unless otherwise indicated)										
Current account	5,459	2,157	1,470	1,985	1,068	1,060	1,539	1,814	2,144	2,452	2,831
In percent of GDP	31.9	16.7	12.9	16.4	7.9	8.5	12.0	13.8	15.9	17.6	19.8
Goods	7,479	2,910	2,154	2,403	2,364	1,605	2,157	2,424	2,764	3,094	3,502
Exports	11,149	6,127	4,813	5,475	6,470	4,952	7,180	8,098	8,474	8,723	8,868
Oil and gas	9,604	5,909	4,321	5,021	6,114	4,775	4,801	4,724	4,876	5,015	5,148
Other 2/	1,545	218	492	454	356	178	2,379	3,374	3,598	3,708	3,721
Imports	3,670	3,217	2,659	3,072	4,105	3,347	5,022	5,674	5,710	5,629	5,366
Services	-955	-1,007	-1,114	-698	-1,005	-709	-745	-770	-792	-818	-832
Receipts	618	648	530	552	570	576	571	579	590	599	620
Payments	1,573	1,654	1,645	1,249	1,575	1,285	1,316	1,349	1,382	1,416	1,451
Primary income	-20	650	835	721	215	614	593	634	636	643	629
Receipts	1,012	1,097	1,077	1,061	1,114	879	855	896	904	920	915
Payments	1,032	447	243	339	899	265	262	262	267	276	286
Secondary income	-1045	-397	-404	-442	-506	-451	-466	-474	-464	-468	-469
Receipts	40	71	53	40	32	42	38	37	39	38	38
Payments	1085	468	457	482	538	492	504	512	503	506	507
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account											
Net lending (+) / net borrowing (-)	4,377	4,543	6,394	1,441	212	4,168	3,824	3,501	3,109	3,311	3,595
Net acquisition of financial assets	5,187	4,275	6,066	2,047	863	4,795	4,596	4,224	3,829	4,055	4,344
Net incurrence of liabilities	810	-268	-328	607	651	627	772	724	721	744	748
Direct investment											
of which: Direct investment in Brunei	575	171	-150	468	512	473	541	517	523	532	542
Portfolio investment											
of which: Portfolio investment assets	771	336	625	-60	-1349	418	428	433	442	451	460
Other investment 3/											
of which: Other investment assets	4,416	3,939	5,441	2,107	2,212	4,377	4,168	3,792	3,387	3,605	3,884
of which: Other investment liabilities	235	-439	-178	138	139	154	230	207	198	212	206
Errors and omissions	-835	-2,352	-5,065	-814	-866	0	0	0	0	0	0
Reserve assets	246	-34	141	-270	-10	107	107	108	110	110	112
Gross official reserves 4/	3,471	3,211	3,322	3,300	3,221	3,327	3,435	3,543	3,654	3,764	3,876
In months of next year's imports of goods and services	8.6	9.0	9.2	7.0	8.3	6.3	5.9	6.0	6.2	…	…
Memorandum items:											
Exchange rates											
Brunei dollars per U.S. dollar (period average)	1.27	1.37	1.38	1.38	1.35	…	…	…	…	…	…
Nominal effective exchange rates (2010=100)	105.8	105.1	107.5	108.2	108.2	…	…	…	…	…	…
Real effective exchange rates (2010=100)	97.1	97.3	97.0	95.9	94.6	…	…	…	…	…	…
Nominal GDP (in millions of U.S. dollars)	17,098	12,931	11,399	12,128	13,568	12,455	12,812	13,096	13,511	13,903	14,328

Sources: Data provided by the Brunei authorities; and Fund staff estimates and projections.

1/ Reflects BPM6 presentation adopted by the authorities. Includes official revisions in March 2014, which improved data coverage and methodology, but lack of comprehensive balance of payments data remains.

2/ Projections for 2020–24 include an increase in petrochemical exports with the start of operations of the Heng Yi refinery.

3/ Includes changes in banks' foreign assets and liabilities and in estimated BIA investments.

4/ Comprises foreign exchange assets of Autoriti Monetari Brunei Darussalam, SDR holdings, and reserve position in the Fund.

Table 4. Brunei Darussalam: Monetary Developments, 2012–20

	2012	2013	2014	2015	2016	2017	2018	2019 Proj.	2020 Proj.
	(In millions of Brunei dollars; end of period)								
Central Bank Survey									
External assets (net) 1/	3,632	3,875	3,957	4,141	4,354	4,028	4,012	4,111	4,218
Foreign exchange holdings	3,587	3,864	4,146	4,090	4,025	4,051	3,917	3,895	3,889
Other assets	359	159	146	108	112	36	63	63	63
Currency issued	1,627	1,220	1,272	1,322	1,381	1,263	1,249	1,256	1,255
Reserve money excluding currency outside ODCs	1,961	1,993	1,984	2,089	2,162	1,793	1,705	1,745	1,882
Other liabilities	1,230	1,128	1,161	1,148	1,237	1,255	1,235	1,286	1,286
Depository Corporations Survey									
Foreign assets (net)	14,860	14,048	13,071	11,212	13,405	13,250	13,600	14,166	14,780
Net claims on government	-3,987	-3,158	-1,868	-685	-1,546	-1,953	-1,871	-1,871	-1,871
Claims on nonfinancial public sector	194	320	269	457	194	175	575	579	609
Claims on private sector	6,610	7,000	7,129	7,314	6,861	6,499	6,296	6,319	6,383
Claims on other financial corporations	60	220	386	441	371	180	72	73	77
Capital accounts	3,344	3,419	3,524	3,637	3,840	3,372	3,416	3,442	3,620
Other items (net)	-419	-832	-827	-715	-849	-251	-314	-320	-342
Broad money	13,962	14,166	14,623	14,365	14,582	14,518	14,930	15,505	16,016
Money	4,293	4,465	4,396	4,680	4,675	4,408	4,274	4,357	4,494
Of which: currency outside depository corps	926	978	1,021	1,073	1,135	1,091	1,084	1,143	1,113
Quasi-money	9,668	9,702	10,227	9,686	9,907	10,110	10,656	11,148	11,523
	(12-month percent change)								
Depository Corporations Survey									
Foreign assets (net)	-4.7	-5.5	-7.0	-14.2	19.6	-1.2	2.6	4.2	4.3
Claims on private sector	1.8	5.9	1.8	2.6	-6.2	-5.3	-3.1	0.4	1.0
Memorandum items:									
Central bank net external asset ratio 2/	2.2	3.2	3.3	3.1	2.9	3.2	3.1	3.1	3.1
Brunei dollars per U.S. dollar (end of period)	1.2	1.3	1.3	1.4	1.4	1.4	1.3	…	…

Sources: Data provided by the Brunei authorities; and Fund staff estimates and projections.

1/ Comprises central bank's foreign exchange assets, SDR holdings, and reserve position in the Fund.

2/ Ratio of foreign exchange holding to currency.

Table 5. Brunei Darussalam: Financial Soundness Indicators and Other Indicators of Vulnerability, 2012–19

	2012	2013	2014	2015	2016	2017	2018	2019 Proj.
Financial sector indicators 1/								
Broad money (M2, percent change, y/y)	0.9	1.5	3.2	-1.8	1.5	-0.4	2.8	3.9
Private sector credit (percent change, y/y)	1.8	5.9	1.8	2.6	-6.2	-5.3	-3.1	0.4
NPL to total loans	6.8	5.7	5.0	4.6	5.9	4.2	4.8	...
NPL net of provisions to total loans	1.6	1.6	2.3	1.7	3.3	1.4	2.4	...
NPL net of provisions to capital	4.3	4.5	6.1	4.8	7.8	3.7	6.4	...
Regulatory capital to risk-weighted assets	20.9	19.4	21.4	21.1	21.5	18.1	18.4	...
External indicators								
Exports of goods and services (percent change, in U.S. dollars)	3.8	-7.8	-4.5	-42.4	-21.1	12.8	16.8	-21.5
Imports of goods and services (percent change, in U.S. dollars)	21.2	15.0	-32.5	-7.1	-11.6	0.4	31.5	-18.5
Current account balance (in millions of U.S. dollars)	5,683	3,778	5,459	2,157	1,470	1,985	1,068	1,060
(In percent of GDP)	29.8	20.9	31.9	16.7	12.9	16.4	7.9	8.5
Gross official reserves (in millions of U.S. dollars)	3,285	3,399	3,471	3,211	3,322	3,300	3,221	3,327
(In months of next year's imports of goods and services)	5.1	7.8	8.6	9.0	9.2	7.0	8.3	6.3
Real effective exchange rate (end of period, 2010=100)	98.4	98.8	97.1	97.3	97.0	95.9	94.6	...

Sources: Data provided by the Brunei authorities; and Fund staff estimates and projections.

1/ The calculation of Financial Soundness Indicators is based on the IMF's *Financial Soundness Indicators: Compilation Guide.*

Appendix I. Risk Assessment Matrix 1/

Source of Risks (Time Horizon; Likelihood)	Expected Impacts	Recommended Policy Responses
Disruption in domestic O&G production caused by aging fields and lower than expected production from new projects (short- to medium-term; high).	**High** Fiscal revenues and exports are susceptible to O&G production declines, with potential spillovers to the non-O&G sector.	Despite substantial fiscal buffers, further re-prioritize current expenditure, including reforming subsidies, and raising non-O&G revenues to ensure long-term sustainability. To mitigate the social impact of these reforms—notably subsidy reforms—implement targeted mitigation measures and a communication strategy that raises awareness of the benefits. In addition, accelerate diversification initiatives.
Large swings in energy prices. Risks to prices are broadly balanced, reflecting offsetting—but large and uncertain—supply and demand shocks. In the near term, uncertainty surrounding the shocks translates to elevated price volatility, complicating economic management and adversely affecting investment in the energy sector. As shocks materialize, they may cause large and persistent price swings (short- to medium-term; medium).	**High** **Lower energy prices:** This would worsen fiscal and external balances, complicating the fiscal consolidation strategy. In addition, long-term plans to increase O&G production could become commercially unviable. Spillovers to the financial sector could rise, weakening banks' balance sheets.	
	High **Higher energy prices:** Higher exports and fiscal revenues, with potential spillovers to the non-O&G sector.	Keeping the consolidating fiscal trajectory is prudent to rebuild buffers; avoid procyclical fiscal policy.
Higher O&G production stemming from the ongoing O&G asset rejuvenation program (short- to medium-term; low).	**High** Higher exports and fiscal revenues, with potential spillovers to the non-O&G sector.	
Delays in reforms and FDI project implementation in the non-O&G sector (short- to medium-term; high).	**High** Continued delays, particularly in large FDI downstream projects, could further hamper growth in the non-O&G sector and slow down diversification.	Continue investment climate reforms that facilitate project execution. Improve public financial management and ensure the quality of public investment.
Weaker-than-expected global growth. Idiosyncratic factors in the U.S., Europe, China, and stressed emerging markets feed off each other to result in a synchronized and prolonged growth slowdown (medium term, short- to medium-term, short- to medium-term, short-term; low, high, high, medium).	**Medium-High** Weak global demand could further suppress O&G prices, worsening fiscal and external balances. In addition, long-term plans to increase O&G production could become commercially unviable. A significant slowdown of the Chinese economy could also slow down important Chinese FDI inflows coming into Brunei.	Despite substantial fiscal buffers, further re-prioritize current expenditure, including reforming subsidies, and raising non-O&G revenues to ensure long-term sustainability.
Rising protectionism and retreat from multilateralism. Escalating and unpredictable trade actions and a WTO dispute settlement system under threat imperil the global trade system and international cooperation (short- to medium-term; high).	**Medium** Reduced global and regional policy collaboration with negative consequences for trade, capital and labor flows, sentiment, and domestic and global growth.	Press ahead with international trade liberalization efforts such as the CPTPP to expand markets and continue improving the business environment to attract further investments and diversify the economy.
Sharp rise in risk premia. An abrupt deterioration in market sentiment (e.g., prompted by policy surprises, renewed stresses in emerging markets, or a disorderly Brexit) could trigger risk-off events (short-term; high).	**Low-Medium** U.S. dollar appreciation if unhedged and higher rates could have valuation losses on sovereign holdings of foreign assets in other currencies.	Continue to manage sovereign asset holdings prudently, including strategic hedging when appropriate.

1/ The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Appendix II. Status of Staff Advice Made During the 2018 Article IV Consultation

Staff Advice	Policy Actions
Fiscal Policy	
Continuing fiscal consolidation. Deepening fiscal reforms, including enhancing the revenue and expenditure strategy, reforming subsidies, and continuing public financial management reforms.	The authorities have made significant progress in fiscal consolidation. The consolidation efforts included: (i) corporatizing public services, (ii) introducing a smart metering system to minimize leakages in utilities, and (iii) taking steps to introduce an MTFF. The FY2019/20 budget has been formulated based on more realistic expenditure assumptions to enhance the credibility of the fiscal framework. However, progress on non-O&G revenue measures and energy subsidy reforms could be accelerated.
Financial Sector Policies	
Developing the financial sector while safeguarding financial stability, by strengthening micro-and macroprudential policies and supervision.	The authorities have taken wide-ranging measures in developing the financial sector, while strengthening macroprudential framework and supervisory system. The measures include steps to broaden the investor base, establish a secondary bond market, develop the required infrastructure and rules for establishing a stock exchange, implement International Financial Reporting Standard 9 by financial institutions, and put all the three pillars of Basel II in place. The authorities have also made progress in developing the Domestic Systemically Important Banks framework. The authorities are also developing a top-down stress testing framework and has planned to introduce the Counter-Cyclical Capital Buffer for the banking sector.
Structural Policies	
Stepping up structural reforms to develop the non-O&G sector and promote private sector development, by continuing to improve the business climate, enhance human capital, attract FDI, and boost integration with the global economy, while leveraging the latest technological innovations.	Significant progress has been made in improving the World Bank Doing Business scores, especially in access to credit and starting a business. Brunei has attracted sizable FDI. Initiatives has been taken to enhance human capital, including the creation of the Manpower Planning Council, while fostering job opportunities and increasing job matching through JobCenter Brunei, I-Ready, and the Center for Capacity Building. Muara Port has been expanded and modernized; Brunei continues to participate in free trade agreements, including the CPTPP, and improve trade facilitation, by introducing the National Single Window.
Data Issues	
Making further progress in data compilation and dissemination.	The authorities have committed to publishing the National Summary Data Page (NSDP), following the recent IMF TA on e-GDDS. The AMBD is preparing its first financial stability report, which is planned to be published this year. However, further improvements in data compilation and dissemination could be accelerated.

Appendix III. Youth Unemployment in Brunei

According to the latest Labor Force Survey, youth unemployment has increased to 28.9 percent, the highest among ASEAN and GCC countries. International experience shows that youth unemployment has significant economic and social consequences. To address youth unemployment, strong growth is essential, while structural labor market reforms can also help. Leveraging technology and digitalization could help turn Brunei's young and tech-savvy population into an asset.

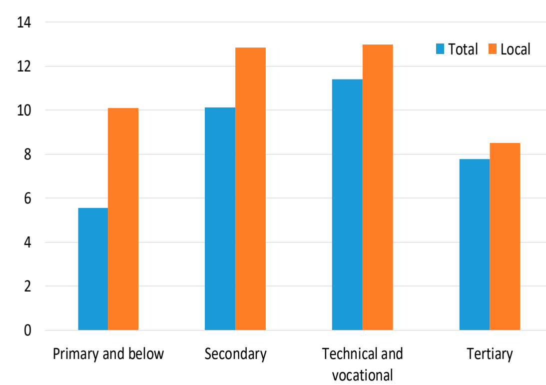
1. **Youth unemployment is high in Brunei.** The recent Labor Force Survey shows that the unemployment rate increased to 9.3 percent in 2017 from 6.9 percent in 2014, when the survey was last conducted. The youth unemployment rate increased from 25.3 percent to 28.9 percent, the highest among ASEAN and GCC countries. Unemployment for locals[1] increased to 11.5 percent from 9.0 percent, with youth unemployment of locals rising to 31.7 percent from 29.9 percent. While unemployment rates for all levels of education is high, those with vocational background have the highest unemployment, underscoring the need for enhancing the quality of vocational training and reducing skill mismatches. Unemployment for those with tertiary education is the lowest, suggesting that education pays off. Both male and female unemployment rates rose, though the gender gap in unemployment narrowed. While female labor force participation rate declined to 56.5 percent from 58.3 percent, the corresponding gender gap narrowed to 12.4 percentage points from 14.1 percentage points as male participation rate declined even more.

Brunei Labor Market Indicators
(In percent, local)

	2014	2017
Unemployment rate	9.0	11.5
Youth unemployment rate	29.9	31.7
Unemployment Rate:		
By Education Attainment		
Primary and below	7.4	10.1
Secondary	10.4	12.9
Tertiary	6.2	8.5
Technical and vocational	7.8	13.0

Sources: Brunei Labor Force Survey and IMF staff calculations.

Unemployment By Education Attainment in 2017
(In percent of labor force with that education attainment)



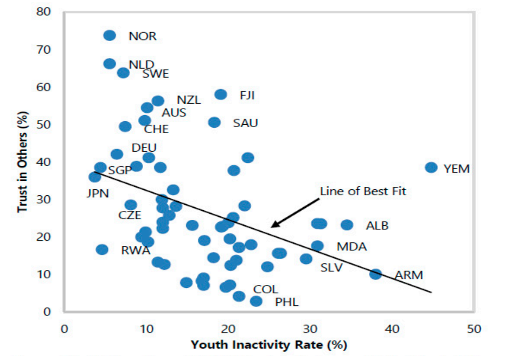
Sources: Brunei Labor Force Survei and IMF staff calculations.

2. **International experience shows that youth unemployment has significant economic and social consequences.** Large and persistent unemployment rates lead to skill attrition, depreciated human capital, outward migration of skilled labor, and an increase in social and political resistance to reforms. Long-term youth unemployment can even erode social cohesion and institutions. For example, experience from other countries shows that there is a negative relationship between youth unemployment and trust in society (Ruble et al, 2003; Urdal, 2006; Fox et al, 2013;

[1] Local persons are the persons in relation to the immigration laws of the country that include Brunei citizens and permanent residents. Non-local persons are those that are temporary residents and others.

Filmer and Fox, 2014). Youth unemployment may also affect medium-term growth prospects by creating a more fragile employment condition with lower wages and sentiment of a lower probability of future employment. Therefore, early experience in the labor market for the young people can affect job aspects later in their lives as well as the overall social environment.

Figure 2. Trust in Society and Youth Labor Markets

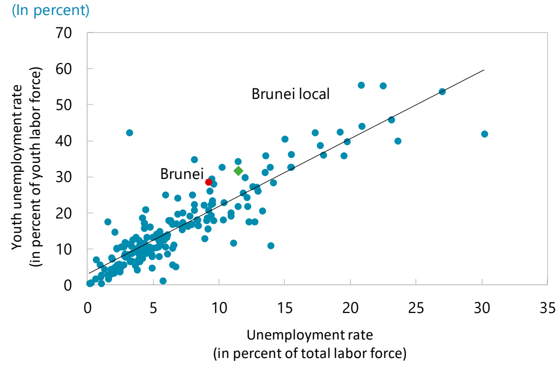


Source: World Values Survey; ILOSTAT Yearly Indicators; and IMF staff calculations.
Note: Respondents of the survey are asked: "Generally speaking, would you say that most people can be trusted or that you need to be very careful in dealing with people?" Possible answers include "Most people can be trusted", "Don't know" and "Can't be too careful". Figures reported here are "Most people can be trusted" as a share of all answers. Slope of the line of best fit is -0.8 with an R^2 of 0.17. ISO 3-letter country codes are indicated for some data points. Youth inactivity rate is the youth NEET rate. Latest available data are shown.

3. Strong growth is essential to reduce youth unemployment, which is usually twice as sensitive or more to economic growth than adult unemployment (IMF, 2014; and IMF, 2019). The sensitivity may be due to the concentration of youth unemployment in cyclically sensitive industries, such as manufacturing, wholesale and retail trade, and hotels and restaurants, and SMEs, which employ a big share of the labor force. In 2014-17, Brunei youth unemployment increased by 3.6 percentage points while total unemployment increased by 2.4 percentage points.

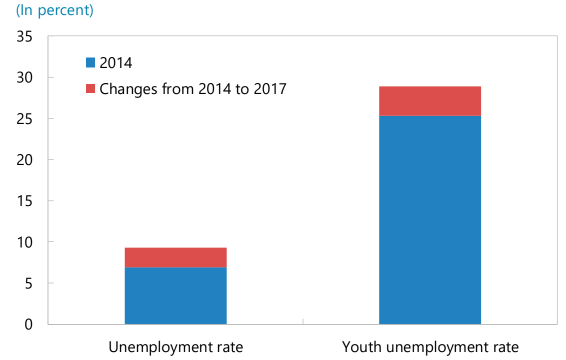
4. Structural labor market reforms are also needed to significantly reduce youth unemployment. Growth alone may not solve the youth unemployment problem. Labor market institutions become the center of forces in addressing youth unemployment issues when economic recovery stabilizes and when unemployment rate returns to historical averages. In Brunei, the 2014 youth unemployment, before the impact of the oil price shock, which can be regarded as a proxy for structural unemployment, was still high.

Unemployment Rates
(In percent)



Sources: World Bank *World Development Indicators*.

Unemployment Rates
(In percent)

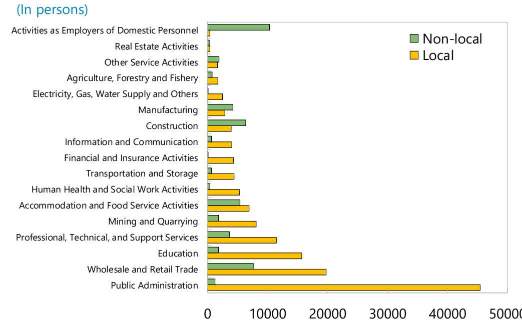


Source: Brunei Labor Force Survey.

5. Diversifying the economy, supporting entrepreneurship, attracting more FDIs, and developing private sector growth are critical. Improving the business climate and fostering competition will be essential in reducing unemployment in the medium term and raising potential growth over the longer term. Policies should also focus on MSME development including capacity development and entrepreneurial training. Efforts are also needed to better integrate and generate stronger positive spillovers from the FDI sector to the rest of domestic economy.

6. The authorities' efforts should also focus on improving the flexibility of labor market, streamlining the public sector, scaling up quality training programs, and reducing skill mismatches. Well-designed labor market institutions can enhance job prospects for both youth and adult Bruneians. Large government sectors may crowd out private investment and disincentivize employment for the private sector. A large public sector may also inflate wage expectations and contribute to skill mismatches by influencing employment choices. If combined with higher public sector wages and better benefits, it may increase reservation wages. The authorities have taken many welcome initiatives to foster job opportunities and increasing job matching, including JobCenter Brunei, I-Ready, and the Center for Capacity Building. Efforts should continue scaling up training programs to address skill mismatch problems and better prepare people for future employment. These initiatives should be evaluated regularly to assess their effectiveness.

Distribution of Labor Force by Economic Activity
(In persons)



Source: Brunei Labor Force Survey 2017.

7. Leveraging technology and digitalization could help turn Brunei's young and tech-savvy population into an asset. Automation and digital technology are taking over tasks that were once done by the human. It is therefore important for young people in this new era to be equipped with necessary skill sets to face the challenge and be more competitive in the job market. On the other hand, technology also brings innovation and new opportunities, generating potentials for new jobs that give young people comparative advantages. Initiatives such as facilitating necessary technological infrastructure and education programs can help tackle youth unemployment, including life-learning programs and increasing tertiary education enrollment. Leveraging digitalization, one of the five priority business clusters, to attract quality FDIs and build the required skills would be instrumental to make young Bruneians competitive.

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Appendix IV. External Sector Assessment

Brunei's external position is assessed to be weaker in 2018 than fundamentals. However, the current account balance, on current policies, is expected to rebound, closing the gap over the medium term as new downstream exports rise. Ample international reserves, together with the large foreign assets, provide strong buffers against adverse shocks. The peg to the Singapore dollar, which provides a credible nominal anchor and stability to the financial system, remains appropriate.

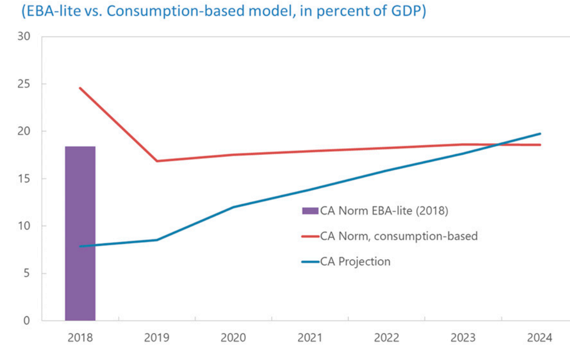
1. **The current account surplus narrowed in 2018, but it is expected to rebound over the medium term.** While exports picked up due to higher oil and gas (O&G) prices in 2018, imports increased even more driven by the ongoing construction of large downstream projects. Consequently, the current account surplus narrowed to 7.9 percent of GDP. Over the medium term, the surplus is expected to rebound as exports rise, reflecting O&G asset rejuvenation and the start of downstream productions, and the temporary imports fade. In addition, investment income from the Brunei Investment Agency (BIA) will continue supporting the external position. The rebound in the surplus is however expected to be moderate, as O&G prices and production are generally expected to remain relatively subdued. The current account balance is therefore expected to remain below the large surpluses seen over the previous decade.

2. **The current account balance is below the norm in 2018, but the gap, on current policies, is projected to be closed over the medium term:**

- ***The macrobalance (EBA-lite CA) approach suggests that the current account is below its norm, due to large temporary imports related to investment projects.*** The EBA-Lite methodology uses regression analysis to predict the equilibrium current account level consistent with a range of structural and policy factors. Norms are levels of the current account estimated based on underlying fundamentals, while gaps are deviations of observed values from norms. For Brunei, the EBA-lite model suggests a current account norm of a surplus of about 18½ percent of GDP in 2018, implying a current account gap of 10½ percent of GDP. The gap is attributed to large temporary machinery imports related to Hengyi refinery and BFI, estimated at about 13¼ percent of GDP. Excluding these temporary imports, the EBA-lite model suggests that the current account is above its norm, with a positive gap of 2.7 percent of GDP (Text table, below). The EBA-lite current account model is estimated on a wide range of countries, and it may not fully capture the features of commodity exporters such as Brunei.[1]

Brunei Darussalam: Current Account Balance and Norm

(EBA-lite vs. Consumption-based model, in percent of GDP)



Source: IMF staff estimates.

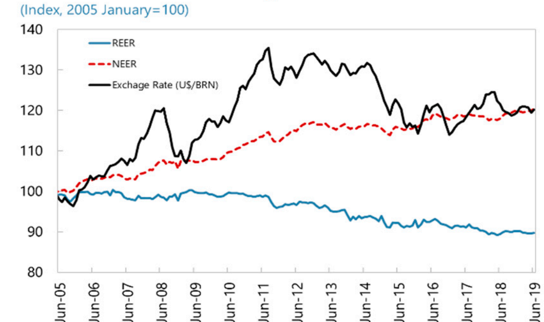
[1] The difference between the actual and fitted values of current account balances is large in Brunei. The gap for Brunei is partly driven by a strong net foreign asset position. Intuitively, the methodology predicts that countries such as Brunei with accumulated savings should be substantial net exporters of capital.

- ***The current account surplus in 2018 is also below the level needed to ensure equitable consumption for future generations, but the gap is expected to be closed over the medium term.*** As Brunei is projected to run persistent CA surpluses in the medium term, assessment of the "sustainability" of the external sector should not be guided by the need to stabilize the net foreign assets position (as in most other countries) but by the objective to save adequately for future generations. The consumption allocation rule model of the revised EBA-Lite methodology is thus the preferred method for assessing Brunei's external sector sustainability, as the CA gap reflects suboptimal saving of hydrocarbon revenues rather than traditional competitiveness issues. From this model, the current account norm as a percent of GDP is estimated to be around 24 percent in 2018, implying a gap of 16 percentage points. The gap in 2018 is mainly attributed to large temporary machinery imports related to Hengyi refinery and BFI. Excluding these temporary imports would narrow the gap to 2¾ percent of GDP (Text table, below). However, the gap is expected to be closed, on current policies, over the medium term. While the current account norm using the consumption-based model is estimated to stay at around 18-19 percent of GDP over the medium term, the actual current account surplus is projected to converge to this level as import linked to large infrastructure projects fade and new downstream exports rise.

3. **Brunei's REER remains stable.** Although the bilateral nominal exchange rate vis-à-vis the US dollar showed some volatility in recent years, the trade-weighted NEER and REER have remained stable because main trading partners showed roughly similar pattern against the U.S. dollar. Heavy reliance on hydrocarbon exports, accounting for 95 percent of exports, limits the impact of the exchange rate on the current account.

Brunei Darussalam: Exchange Rates

(Index, 2005 January=100)



Source: IMF, *International Financial Statistics*

Brunei Darussalam: Current Account Actuals and Norms (2018)

(in percent of GDP, unless otherwise specified)

	EBA-lite CA model	Consumption-based model
Current Account Actual	7.9	7.9
excl. temporary imports 1/	21.1	21.1
Current Account Norm	18.4	23.9
Policy gap	3.7	
CA-Fitted	22.1	
Current Account Gap	-10.5	-16.0
excl. temporary imports	2.7	-2.8

Source: IMF Staff calculations

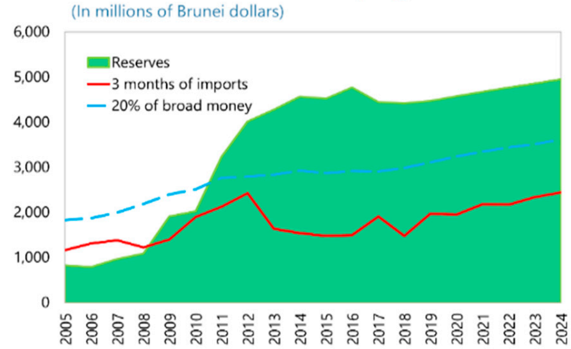
1/ Machinery imports related to Hengyi refinery and BFI.

4. **Cross-border capital flows do not pose risks to the economy.** FDI is expected to continue over the medium term driven by the funding for the ongoing downstream investment projects. Portfolio investment flows remain relatively subdued, given the current size and limited growth of the domestic capital market, which implies that vulnerabilities from global financial shocks arise mainly through Brunei's asset holdings abroad.

5. The peg to the Singapore dollar remains appropriate for Brunei, providing a credible nominal anchor and stability to the financial system. Both the inflation rate and its volatility have been low in comparison to other commodity exporters, suggesting that the credibility of the peg helps anchor inflation and preserve macroeconomic stability. The peg is also instrumental for Brunei to benefit from Singapore's deep financial markets to manage its large external assets without incurring exchange rate risks. In addition, it reduces uncertainty for trade and investment from the region. Since Singapore is a major trading partner of Brunei and a conduit to the ASEAN region and beyond, the peg can help to attract FDI for the development of the non-O&G sector and human capital, to boost productivity and help in the authorities' economic diversification efforts.

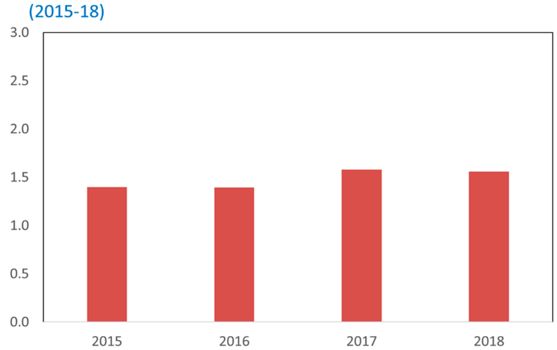
6. Official reserves remain above the adequacy benchmarks. Official reserves held by the monetary authority (Autoriti Monetari Brunei Darussalam, AMBD) continue to provide a strong buffer against adverse future shocks but are assessed to be more than adequate for precautionary purposes by various adequacy benchmarks. Brunei's international reserves in 2018 amount to 29 percent of broad money and 8.7 months of imports, although it has to be borne in mind that, in line with the currency board system in place in Brunei, international reserves should back up currency in circulation. Therefore, the size of the official reserves depends on the amount of currency in circulation. The level of official reserves was around 180 percent of the Fund's composite metric in 2018—above the recommended 100–150 percent adequacy range–and are projected to gradually increase over the medium term. Commodity-intensive economies, however, have higher precautionary liquidity needs than other economies to cope with more volatile terms of trade shocks. Indeed, Brunei's official reserves appear to be comparable to those of other energy exporters (see charts). In addition, the liquid portion of the Sustainability Fund held by the government could also provide an additional buffer against adverse shocks.

Brunei Darussalam: Reserve Adequacy, 2005–2024
(In millions of Brunei dollars)



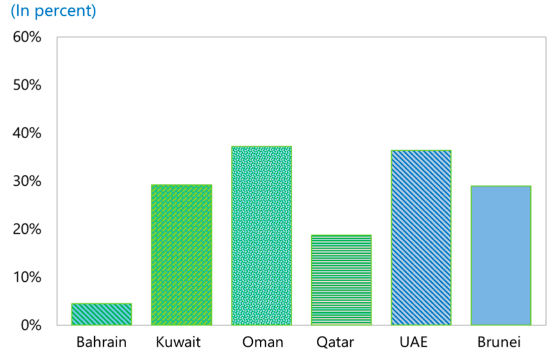
Sources: Brunei authorities; and IMF staff estimates.

Brunei Darussalam: Reserves to monetary base ratio, (2015-18)



Sources: Brunei authorities, and IMF staff calculations

Broad Money Cover: Brunei Versus GCC, 2018
(In percent)

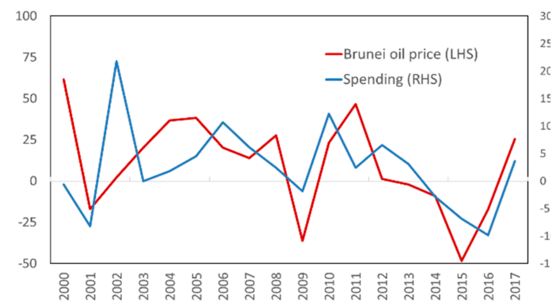


Sources: IMF, *World Economic Outlook*; IMF, *International Financial Statistics*; and staff calculations.

Appendix V. Fiscal Policy in a Medium-Term Context

Fiscal policy in Brunei takes center stage, but volatile O&G prices have led to procyclical expenditure. The authorities have taken steps toward establishing an MTFF to delink spending from short-term volatility in O&G prices, protect priority spending, and support fiscal consolidation over the medium term. Yet the MTFF is still in an early stage. A full and effective MTBF needs several prerequisites including a credible annual budget, a comprehensive top-down budget process and capacity building at each ministry. Given the volatile nature of O&G revenue, Brunei would benefit from a fiscal framework centered on a procedural fiscal rule, rather than a strict numerical target.

Brunei Oil Price vs. Total Spending, 2000-17
(Annual growth rate)



Source: IMF WEO, IMF staff calculations

1. **Fiscal policy in Brunei takes center stage in preserving macroeconomic and financial stability and supporting economic diversification.** At the same time, like in other resource-rich countries fiscal policy tends to be procyclical. Volatile oil and gas (O&G) prices and revenues lead to expenditure fluctuations, which can amplify the booms and busts in the economy and reduce the quality of government spending.

2. **Adopting a medium-term fiscal framework (MTFF[1]) could help insulate spending from volatile O&G revenues**. Delinking public spending from short-term volatility in oil revenue and ensuring that spending decisions are based on a longer-term perspective are particularly important to preserve macroeconomic and fiscal stability and support economic diversification. A medium-term budget framework (MTBF[2]), in turn, could help protect priority expenditures, maintain the strategic focus of policy plans, and support medium-term fiscal consolidation. In addition, the MTBF could improve the budget process and outcome through greater clarity of policy objectives, predictability in budget allocations, comprehensiveness of coverage, and transparency in using resources.

3. **The authorities have taken steps toward establishing an MTFF.** A fiscal forecasting unit (FFU) was established to provide the Ministry of Finance and Economy (MOFE) with revenue and expenditure forecasts using short- to medium-term models. The MOFE has asked line ministries and

[1] MTFF focuses on aggregate fiscal discipline and fiscal sustainability in a medium-term perspective. It sets multi-year macro and fiscal objectives, and develops a comprehensive statement of the medium-term fiscal strategy consistent with fiscal objectives to ensure macroeconomic stability and fiscal sustainability.

[2] MTBF (or interchangeably used Medium-Term Expenditure Framework, MTEF) is a set of institutional arrangements for prioritizing, managing and presenting budget revenue and expenditure given the medium-term fiscal objectives. It harmonizes and reconciles top-down medium-term available resource envelope with bottom-up cost estimating of policy ideas.

departments to prepare a five-year fiscal consolidation plan that will include structural reforms and policy changes. Despite this progress, Brunei's MTFF is still in a very early stage.

A. Medium-Term Budgeting: Protecting Priority Spending and Supporting Fiscal Consolidation

4. **In the absence of a well-functioning and detailed MTBF, ad hoc increases in current expenditure, which are typically difficult to unwind, tend to result in rigidities.** An MTBF is important to protect capital expenditure in the event of a need for fiscal consolidation. The MTBF could help enhance prioritization processes, and the quality of investments through the evaluation, choice, and management of projects. Thus, it could alleviate risks to long-term project viability, which could otherwise be compromised if ongoing capital projects entail significant operating and maintenance costs.

5. **An MTFF together with a fiscal strategy should be put in place ahead of a more binding MTBF**. As a first stage, a simple MTFF would provide a projection of the fiscal balance, non-O&G balance and estimates of revenues and spending at a more aggregate level. A fiscal strategy document would be the basis for annual budget preparation, translating the MTFF into a statement on fiscal policy priorities. This document could also contain fiscal risk analysis, indicating the sensitivity of fiscal plans to varying assumptions regarding the economy, the hydrocarbon sector, and contingent liabilities. In a second stage, an MTBF could provide guidelines to line ministries to prepare medium-term spending plans.

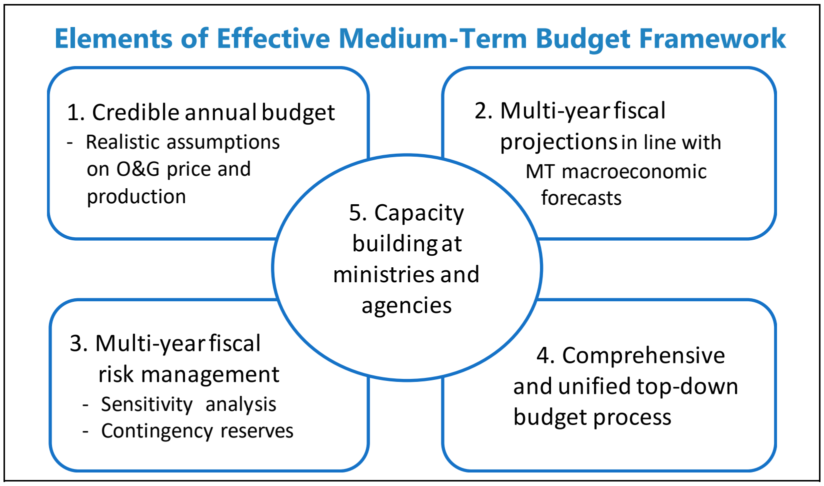
6. **A full and effective MTBF requires several critical prerequisites:**

- A credible annual budget is important to design and implement the MTBF. Using realistic hydrocarbon price and production assumptions that are based on explicit rules in the budget preparation is key to avoiding deviations of actual oil prices and production from budget. Medium-term macroeconomic projections need to be anchored in the government's multi-year projections of revenue and expenditure. The MOFE needs to further enhance its capacity in formulating medium-term macroeconomic forecasts.

- A multi-year fiscal risk management would help plan for contingencies. This highlights the need to prepare a sensitivity analysis regarding price, cost, and production, and to adequately plan for contingency reserves to smooth spending over the medium term in the face of shocks.

- A comprehensive and unified top-down budget process is also needed for medium-term budget planning to shape fiscal policy in line with the government's overall objectives.

- Capacity building at ministries and government agencies are also essential to enhance budget preparation and ensure quality of spending.



7. **For the MTBF to be successful, other public financial management (PFM) reforms should go hand in hand.** Consolidated monitoring and control of budgetary and extrabudgetary resources are key PFM issues. In this context, advancing the operation of a treasury single account (TSA) should be a priority. The TSA helps consolidate government cash resources, gives the finance ministry oversight of all government cash flows, and brings improvements in budget control and monitoring.

B. Fiscal Rules: Anchoring Fiscal Goals

8. **Brunei could consider a fiscal rule as a way of reinforcing a multiyear fiscal framework, as it would provide an anchor for medium-term ceilings and projections.** Many countries have resorted to fiscal rules of different types: expenditure, revenue, budget balance, and debt. Commodity exporters need to modify standard fiscal rules to reflect commodity price volatility, such as non-resource balance rules. For example, a structural balance rule, using long-term price forecasts of copper, has been institutionalized in Chile's fiscal responsibility law.

9. **Given the volatile nature of O&G revenues, Brunei would benefit from a framework that includes a procedural fiscal rule, rather than a permanent strict numerical target.** A procedural fiscal rule would include: (i) principles for fiscal policymaking; (ii) a requirement for the government to set a target for one or more fiscal indicators; (iii) the content of the fiscal strategy statement in which those targets are set; (iv) the arrangements for reporting performance against those targets; and (v) an escape clause to deal with exceptional circumstances which prevent the government from meeting its fiscal objectives. A procedural rule in a volatile environment would allow the authorities the flexibility to change its quantitative fiscal targets within a principle-based framework.

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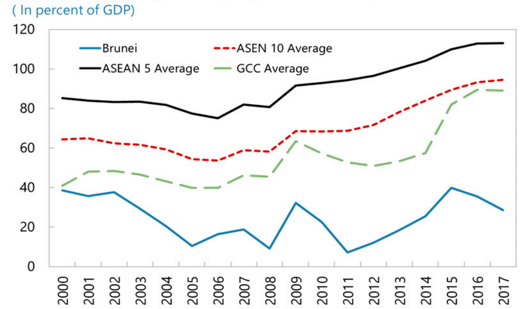
Appendix VI. Financial Deepening and Economic Diversification

Brunei's financial system is on a positive path of development supported by broad-based reforms initiatives taken in line with the ambitious Financial Sector Blueprint 2016-25. The financial system remains bank dominated, while the credit to GDP has been low compared to its peers. Brunei has no stock exchange, secondary capital and bond market, or private sector sukuk market. To further develop the financial sector, still a wide range of reforms are needed.

1. Brunei has not caught the momentum of financial sector development over the last two decades, while peers made great strides. The credit to GDP ratio was below 40 percent during 2000 to 2017, far below the average of ASEAN 5 and 10, and GCC countries.

Domestic credit provided by financial sector
(In percent of GDP)



Sources: World Bank, World Development Indicators; and IMF staff calculations.

2. The literature documents that financial development has the potential to boost economic growth, increase resilience, and promote financial stability. IMF (2015) finds sizeable impacts of improved financial intermediation on aggregate productivity and income. King and Levine (1993) and Levin (2005) also find empirical evidence that financial deepening augments economic growth while financial institutions and markets help better financial intermediation and resource allocation. The diversification and management of risk promotes financial stability to the extent that deep and liquid financial systems with diverse instruments help dampen the impact of shocks.

3. The IMF's new comprehensive financial development (FD) index (2015 and 2016) captures both financial institutions (FI) and markets (FM). To overcome the shortcomings of a single indicator—credit to GDP ratio—as a proxy for financial development, the overall financial development index and sub-indices are constructed for 183 countries on annual frequency from 1980 onward. Financial institutions include banks, insurance companies, mutual funds, and pension funds. Financial markets include stock and bond markets. Financial development is defined as a combination of depth (size and liquidity of markets), access (ability of individuals and companies to access financial services), and efficiency (ability of institutions to provide financial services at low cost and with sustainable revenues, and the level of activity of capital markets). This broad multi-dimensional approach to defining financial development follows the matrix of financial system characteristics developed (Table 1).

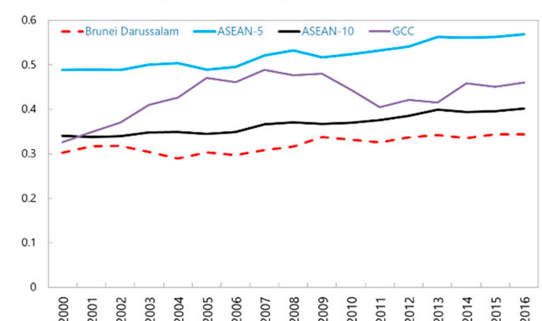
4. The index indicates that Brunei's financial sector development has improved during the last decade but remains below ASEAN and GCC Countries. The components of the FD Index reveal that for the financial institution category, Brunei's financial depth and efficiency are at its peer's level while for the financial market category the depth and efficiency are lower than its peers, owing to the minimal activity in the capital market and private sector bond issuance. However, access to financial institutions for Brunei is significantly higher than its peers because of relatively high number of bank branches and ATMs.

Table 1. Brunei Darussalam: Construction of the Financial Development Index

	FINANCIAL INSTITUTIONS	FINANCIAL MARKETS
Depth	1. Private-sector credit (% of GDP) 2. Pension fund assets (% of GDP) 3. Mutual fund assets (% of GDP) 4. Insurance premiums, life and non-life (% of GDP)	1. Stock market capitalization to GDP 2. Stocks traded to GDP 3. International debt securities government (% of GDP) 4. Total debt securities of nonfinancial corporations (% of GDP) 5. Total debt securities of financial corporations (% of GDP)
Access	1. Branches (commercial banks) per 100,000 adults 2. ATMs per 100,000 adults	1. Percent of market capitalization outside of top 10 largest companies 2. Total number of issuers of debt (domestic and external, nonfinancial corporations, and financial corporations)
Efficiency	1. Net interest margin 2. Lending-deposits spread 3. Non-interest income to total income 4. Overhead costs to total assets 5. Return on assets 6. Return on equity	1. Stock market turnover ratio (stocks traded/capitalization)

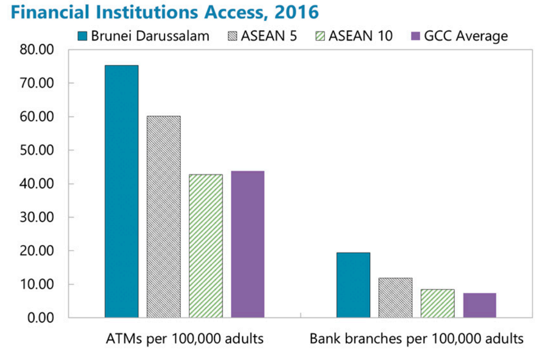
5. **Empirical analysis indicates that there is a significant, bell-shaped, relationship between financial development and economic growth.** Based on a sample of 128 countries, IMF (2015) finds that financial development increases growth, but the effects weaken at higher levels of financial development, and eventually become negative. There are several channels through which

Financial Development Index, 2000–2016



Sources: Financial Development Index, International Monetary Fund; and IMF staff calculations.

Financial Institutions Access, 2016

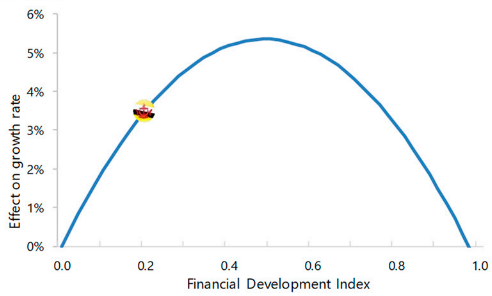


Sources: World Bank, Global Financial Development; and IMF staff calculation.

too much finance could have a negative effect on growth. It increases the frequency of booms and busts and leaves countries ultimately worse off with lower real GDP growth. Another channel is that too much finance leads to a diversion of talent and human capital away from productive sectors and toward the financial sector. A very large financial sector may be particularly susceptible to moral hazard or rent extraction from other sectors, both of which would lead to a misallocation of resources. The bell-shaped relationship between growth and the FD index pertains only to the depth components of the index, for both markets and institutions.

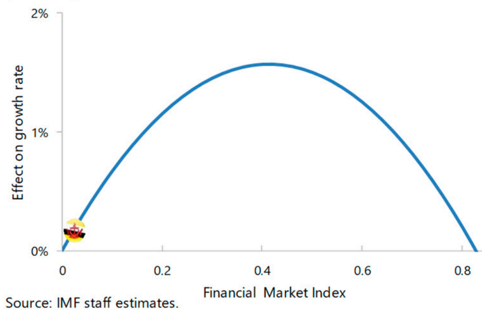
6. Brunei could benefit from further financial development, improving financial institutions depth and developing capital market and institutions. Financial development, including financial market development, increases growth up to a certain point (between 0.45 and 0.7 on the FD index and between 0.4 and 0.6 on the market index) after which, further development has a negative impact (see the charts below). Brunei is below the optimum index value for both development and market index, suggesting further development would support growth.

Financial Development Effect on Growth
(In Percent)



Source: IMF staff estimates.

Financial Market Development Effect on Growth
(In Percent)



Source: IMF staff estimates.

7. The authorities should continue to implement Financial Sector Blueprint (2016-25) along with other financial deepening measures. The financial sector is bank-centric. There is room for non-bank financial sector development. Developing the capital market could reduce the dependency on the banking system for long-term financing demand and mitigate vulnerabilities emanating from duration mismatch. The authorities should continue their efforts to develop efficient interbank money market and secondary bond market, establish a market benchmark for risk free interest rate, improve the primary market issuance framework for corporate bond, and develop derivatives market to achieve the aim of further economic development and diversification.

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INTERNATIONAL MONETARY FUND

BRUNEI DARUSSALAM

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

August 26, 2019

Prepared By	Asia and Pacific Department

CONTENTS

FUND RELATIONS

(As July 31, 2019)

Membership Status: Joined October 10, 1995; Article VIII

General Resources Account

	SDR Millions	Percent of Quota
Quota	301.30	100.00
Fund holdings of currency (exchange rate)	266.31	88.39
Reserve position in Fund	35.20	11.68

SDR Department

	SDR Millions	Percent of Allocation
Net cumulative allocation	203.50	100.00
Holdings	217.26	106.76

Outstanding Purchases and Loans: None

Latest Financial Arrangements: None

Projected Obligations to Fund: None

Implementation of HIPC Initiative: Not applicable

Safeguards Assessments: Not applicable

Exchange Arrangements

Brunei Darussalam's exchange rate regime is a currency board arrangement, with the Brunei dollar exchanged at par with the Singapore dollar. Brunei has accepted the obligations under Article VIII, Sections 2(a), 3 and 4, and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation

Brunei is on the 12-month consultation cycle. The Executive Board concluded the 2018 Article IV consultation on September 17, 2018.

FSAP Participation: Not applicable

Technical Assistance

FAD: A Medium-Term Strategy for Fiscal Sustainability (June 1998)

FAD: Public Financial Management (December 2006, June 2011, April 2014)

FAD: Fuel Subsidy Reform (April 2016)

MFD: Developing the Financial System of Brunei Darussalam (December 1997)

MCM/MFD: Establishment of Brunei Darussalam Monetary Authority (January 2006, December 2006, August 2008)

MCM: Payment and Settlement Systems/Liquid Payment and Settlement Systems (May 2012), Liquidity Monitoring (January 2015), Monetary and Financial Statistical (March 2015), Scoping mission on the systemic risk monitoring and macroprudential policy frameworks (April 2018), Framework for bank resolution and crisis management (April 2018)

STA: Monetary and Financial Statistics (October 1998, January 2006, July-August 2008, October 2009, July 2010, November 2011)

STA: Balance of Payments Statistics (May 1996, June-July 2003, June 2004)

STA: Government Finance Statistics (October 2011, May 2017)

STA: Enhanced General Data Dissemination System (June 2019)

STATISTICAL ISSUES

Assessment of Data Adequacy for Surveillance	
General: Data provision continues to improve and is broadly adequate for surveillance (Category B). Data dissemination delays after the reference period (TCIRS) are being reduced for a number of indicators thanks to the introduction in 2015 by the Department of Statistics (DOS) of an Advance Release Calendar (ARC) in line with international standards for national statistic releases. The DOS also started submitting data through the IMF Integrated Correspondence System to the IMF Statistics Department (STA). In 2015, the Department of Economic Planning and Development (DEPD) launched its new website (http://www.depd.gov.bn/) with the latest national statistics. The DOS is also working on providing data to all users through several links such as www.data.gov.bn/ and social media like www.instagram.com/statistics.jpke/. The National Statistics Committee is working to strengthen data collection and compilation processes across relevant agencies. The authorities remain committed to continue improving statistical capacity to enhance data quality and progressing toward international standards and best practices. The use of the IMF's Data Quality Assessment Framework for all national statistics is recommended.	
National accounts: Quarterly GDP is available with a one-period lag. New GDP estimates rebased to 2010 were released in 2015. The new series incorporate data from the most recent benchmark censuses and surveys, such as the 2010/11 Household Expenditure Survey, the 2011 Population and Housing Census, and the 2011 Economic Census. The coverage of the government sector was extended to include statutory bodies. GDP by Income Approach as well as Gross National Income and Savings are also released. Work has started for the compilation of the Supply and Use Table, which will incorporate data from the 2015/16 Household Expenditure Survey, the 2016 Population and Housing Census Update, and the 2016 Economic Census. **Price statistics**: Monthly CPI is available with a one-period lag. The CPI weights were derived from the results of the 2015/16 Household Expenditure Survey.. The compilation of producer and construction material price indices remains in the plans. The feasibility of compiling import and export price indices is being assessed. **Labor statistics**: The DEPD has improved employment statistics and now provides some data on a monthly basis. The 2014 Labor Force Survey was designed and implemented with technical assistance from the International Labor Organization using the latest international standards. For the first time, an inter-censal update was conducted in 2016 to update the housing and household frame to be used for the Labor Force Survey, which is now conducted annually. Data on wages are limited. There is still scope to enhance data quality.	
Government finance statistics: Shortcomings exist mainly in classification of some flows and in consolidation of major government institutional units. Deficiencies in budgetary central government data include: recording taxes net of subsidies and omission of key fiscal flows e.g., property income on assets, unrecorded subsidy schemes, and some capital transfers to extra-budgetary institutions. Currently, the Treasury's priority is to ensure that the GFS cash flow statement for the budgetary central government is updated quarterly. Data sources generated from Treasury Accounting Financial Information System are continuously monitored and enhanced. The coverage could be expanded to general government by consolidating the financial accounts for the budgetary central government, the extra-budgetary units, and the social security funds. Government finance statistics are not reported for publication in either the *Government Finance Statistics Yearbook* or the *International Financial Statistics*. The authorities are committed to improving their capacity to compile GFS, including through participating in IMF training courses on GFS.	
Monetary statistics: The Autoriti Monetari Brunei Darussalam (AMBD) compiles and reports to STA monthly monetary data for the central bank, other depository corporations (ODCs), and other financial corporations (OFCs) using the standardized report forms (SRFs). The data are comprehensive and reported on a regular and timely basis. The AMBD is working to further improve data compilation and reduce dissemination lags.	
Financial sector surveillance: The AMBD reports quarterly the financial soundness indicators (FSIs) to the Fund, which are published on the IMF's FSI website. The reported FSIs comprise all the core (12) and 10 encouraged FSIs for deposit takers.	
Balance of payments: Quarterly balance of payments statistics have been reported to STA in BPM6 format since the end of 2015, with both quarterly and annual data available from 2008. There is a break in the data series due to changes in compilation techniques and methodology. Notwithstanding that the coverage of other investment has been significantly improved by making use of data from monetary statistics. However, net errors and omissions remain large. Imports of goods coverage have shortcomings. Counterpart data on imports of goods showed large discrepancy. Work is underway to improve services data. The direct investment (DI) survey assisted in better capturing the liabilities of direct investment enterprises. However, data on DI assets remain not captured. Compilation of international investment position in BPM6 basis has finished but not released.	
Data Standards and Quality	
Participant in the e-GDDS.	An e-GDDS mission took place in June 2019.

Brunei Darussalam: Table of Common Indicators Required for Surveillance

(As of July 2019)

	Date of Latest Observation	Date Received	Frequency of Data[8]	Frequency of Reporting[8]	Frequency of Publication[8]
Exchange rates	6/19	6/19	D	M	D
International reserve assets and reserve liabilities of the Monetary Authorities[1]	06/19	06/19	M	M	Q
Reserve/base money	3/19	4/19	M	M	Q
Broad money	3/19	4/19	M	M	Q
Central bank balance sheet	3/19	4/19	M	M	Q
Consolidated balance sheet of the banking system	03/19	05/19	M	M	Q
Interest rates[2]	3/19	4/19	D	M	D
Consumer price index	6/19	8/19	M	M	M
Revenue, expenditure, balance and composition of financing[3] – general government[4]	Q4/FY2018/19	6/19	Q	I	A
Revenue, expenditure, balance and composition of financing[3] – budgetary central government	Q4/FY2018/19	6/19	Q	I	A
Stocks of central government and central government-guaranteed debt[5]	Q4/FY2018/19	6/19	M	M	M
External current account balance	Q1/2019	6/19	Q	A	A
Exports and imports of goods	4/19	7/19	M	M	M
GDP/GNP	Q1/2019	7/19	Q	Q	Q
Gross external debt[6]	NA	NA	NA	NA	NA
International investment position[7]	2018	6/19	A	I	NA

[1] Any reserve assets that are pledged of otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing. Central government data are on FY basis.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] No reported external debt.
[7] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[8] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Semi-annually (S), Annually (A), Irregular (I); Not Available (NA).