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## East Timor's Economic Engine May Be Low on Gas

By David Winning , The Wall Street Journal

SYDNEY—For nearly a decade, East Timor has relied on revenue from a huge natural-gas field to rebuild after its bloody war of independence with Indonesia. Now, the tiny nation's outlook is becoming less certain as that gas field runs low on reserves.

Australian energy company Santos Ltd. said Friday that a new assessment of the Bayu-Undan field, in waters shared by East Timor and Australia, shows its share of remaining gas reserves to be around a fifth smaller than earlier estimates.

For Santos and partners such as Houston-based ConocoPhillips (NYSE:COP) , lower reserves may mean a small dent in future cash flow. But for East Timorese officials, it's a major problem. The country's petroleum revenue topped \$3.5 billion in 2012, dwarfing the amount the government raised locally from other sources, including taxes.

**Emilia Pires** , East Timor's finance minister, has previously said that revenue from oil and gas supports 90% of the country's budget.

That ranks East Timor alongside South Sudan and Equatorial Guinea as the most oil-and-gas-dependent countries in the world, said **Charles Scheiner** , a researcher for the nongovernment organization La'o Hamutuk in East Timor's capital, Dili.

Once a Portuguese colony, East Timor declared independence in the mid-1970s, only to be invaded by Indonesia nine days later. It lost almost a quarter of its population died during 24 years of civil war, while Indonesian forces burned about 80% of its government buildings and infrastructure, leaving East Timor the poorest nation in Asia.

East Timorese voted overwhelmingly for freedom in a 1999 referendum supervised by the U.N., but the vote set off a further wave of violence by the Indonesian military and its supporters. East Timor achieved full independence in 2002, and relations with Indonesia are now much improved.

Unlike many resource-rich developing countries, East Timor didn't squander the cash on vanity projects, instead setting up a sovereign-wealth fund to store money from Bayu-Undan for future generations. Known as the Petroleum Fund, it was initially run by the central bank, but since mid-2009 responsibility has widened to include foreign managers such as Schroder Investment Management Ltd., with investments in U.S. Treasuries and global equities.

Officials hoped that returns from the fund would help offset shrinking revenues from the Bayu-Undan field, which began piping gas to a processing plant in Darwin, Australia, in 2004—just as oil prices began a sharp rise that would take them to a peak above \$147 a barrel in 2008. From an initial balance of \$370 million in 2005, the fund increased to \$11.78 billion at the end of 2012, according to the most recent annual report on the finance ministry's website.

On Friday, Santos said it had reduced its estimated share of the remaining reserves at Bayu-Undan by eight million barrels of oil equivalent. Santos, which has an 11.5% stake in the field, said the revision reflects "reservoir performance and updated modeling."

Bayu-Undan isn't the only active oil and gas field generating revenue for East Timor. The smaller Kitan oil field, operated by Italy's Eni, started production in 2011. But East Timorese officials say output at both fields has already peaked.

"The government will have to take a close look at what these revised reserves mean for the petroleum fund and what the impact is on what it has available," said **Shane Rosenthal** , the Asian Development Bank's representative in East Timor.

East Timor's finance ministry wasn't available to comment.

Another big offshore gas project in waters shared by Australia and East Timor, Greater Sunrise, is stalled by a disagreement between the government in Dili and investors led by Woodside Petroleum Ltd. East Timor wants a gas-export plant for the project built on its coast, to guarantee local jobs and form the centerpiece of a petrochemical hub. Woodside and partners, including Conoco and Royal Dutch Shell PLC, argue that a facility that can process the gas at sea would be more profitable.

A lower estimate of reserves at Bayu-Undan—and the possibility that it could run out of gas completely within a few years—is troubling observers like Mr. Scheiner, because East Timor has begun raiding the sovereign-wealth fund to pay for infrastructure projects like roads. Withdrawals in 2012 came to \$1.5 billion, about \$830 million more than the fund's managers estimate is sustainable.

Mr. Scheiner said La'o Hamutuk's modeling suggests the petroleum fund will be able to finance state spending for only about five years after production ceased at the Bayu-Undan field. Other industries, such as coffee exports, are too small to take up the slack.

"The problem for East Timor is that it's poor in everything other than oil" and gas, Mr. Scheiner said.

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