The Resource Curse in Timor-Leste

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Topics to discuss

2002: Newly independent - starting in a good place

2004-7: Established model petroleum regime and Petroleum Fund. Oil and gas revenues begin to come in.

2008-14: Revenues and state spending grow rapidly. Regulatory regime gets weaker.

2015-22: Oil revenues fall as fields are depleted. The “non-oil” economy is shrinking; poverty persists.

Future: Dreams of more oil rents could be illusory. Petroleum Fund has $18 billion, which might last 10 years

Observations and conclusions
After 400+ years of Portuguese colonial rule and 24 years of Indonesian occupation and war, Timor-Leste’s people wanted peace and prosperity for their new state.

Indonesia had destroyed their economy and infrastructure, and they had no foreign debt, and no experience with self-government or democracy.

Timor-Leste and its international advisors hoped that undeveloped offshore oil and gas fields would jump-start their state and economy.

They were determined to avoid the “paradox of plenty”, where people in extractive-dependent nations live with poverty, conflict, corruption, inequality and autocracy.

Production-Sharing Contracts with oil and gas companies are standard, published, with no bonuses.

All oil and gas revenues go into the Petroleum Fund, which is in tradable overseas investments, transparent, and independently managed. Investment returns are deposited into the PF.

Money can be withdrawn only to finance the state budget, with Parliamentary approval and sustainable rules.
It worked well for a while.

- Oil production began in 2004 and gas in 2006, while global oil prices surged, and revenues were higher than expected – reaching $2 billion/year in 2008 and peaking at $3.3 billion in 2012 (three times non-oil GDP).
- Bidding rounds for new offshore areas in 2005-6 were open and transparent, and several companies conducted seismic exploration and drilled test wells.
- The balance in the Petroleum Fund rose to $12 billion by 2012.
- After civil unrest in 2006 and elections in 2007, the new government rapidly increased spending and adopted an ambitious, oil-fueled, development plan.
Petroleum dependency dominates.

- PF withdrawals always exceeded sustainable levels. In 2010-2015, they were 154% of ESI, paying for 89% of state spending.

- High investment returns grew the PF, but more slowly. It reached $17 billion in 2015, where it stayed for four years.

- The PF law was amended in 2011 to enable higher withdrawals and riskier investments. By 2014, 40% was in the stock market.

- Economic disparity increased, with a growing middle class in Dili but unchanging widespread poverty among the rural majority.

- Nevertheless, peace and democracy prevails, corruption is relatively small, and people enjoy their human rights.

Past and present oil and gas exploration contracts

[Diagram of oil and gas exploration contracts]
The petroleum regime decays.

- After 2012, oil and gas production fell; revenues dropped rapidly. No commercially viable fields have been discovered since 2011.
- Petroleum laws were amended again in 2018-19 to undercut sustainability, reduce oversight and weaken protections.
- ConocoPhillips, the oil company with the biggest stake in Timor-Leste, sold all their interests, as did Shell.
- Greater Sunrise, which many hoped would be developed after the 2019 Boundary Treaty with Australia, remains stuck.
- The PF loaned $650 million to TimorGAP to buy 57% of Sunrise. A year later, Sunrise was revalued to zero.

Income to the state (including the Petroleum Fund)
• Withdrawals from the PF are twice the sustainable level and finance more than 80% of state spending, which is going up since 2019.

• Although the Petroleum Fund balance rose to $19 billion in 2021, it is falling rapidly as stock prices drop and withdrawals increase.

The petroleum era is ending.

• Timor-Leste has received 99% of the money it will get from existing fields. Increased oil prices do not help because production is low.

• Sunrise may never be developed because no investors have come forward. Climate change concerns have curtailed new fossil fuel projects.

• Test wells at potential new fields have not found viable reserves, although exploration continues.

• If every new field meets its proponents’ optimistic projections, they might bring in up to $1 billion in total. This could finance the state budget for six months.
TL’s trade deficit is around $1 billion every year, including many imports which could have been produced locally.

Private sector employment has been dropping since 2014. The productive economy is smaller than at independence.

Spending on education and health is below international norms. Child malnutrition is among the worst in the world.

Timor-Leste’s Human Development Index dropped from 128th in the world in 2010 to 141st in 2020.

The Petroleum Fund pays for more than 80% of the budget. It could be used up within a decade.

The non-oil productive economy is smaller than it was at independence.
What’s happening?

• It’s easier to pay for something – an overseas scholarship or a foreign investment contractor – than it is to build a university or local business.

• Most local companies and workers seek petroleum rents (through public contracting), rather than developing the productive economy. It’s more certain and more lucrative … for now.

• Prices on the petroleum and stock markets are volatile and uncontrollable.

Retrospective observations

• In a democracy with five-year terms of office, politicians have a short planning horizon.

• They prioritize visible benefits (physical infrastructure) over long-term investments (human resources).

• Legislated protections can easily be repealed.

• The petroleum industry is capital-intensive, employing hardly any Timorese workers or subcontractors.

• Non-renewable resources inevitably run out.
The independence struggle left scars.

- TL proved the ‘experts’ wrong by winning independence and by forcing Australia to accept a maritime boundary.
- Many international agencies sent incompetent ‘experts’, further devaluing the concept of expertise.
- Therefore, some Timorese believe they can accomplish anything, regardless of physical or commercial realities.
- National leaders excelled at clandestine resistance, a different skill set than is needed to govern in a peacetime democracy.
- Endemic PTSD and trauma undercut long-term planning.
- Nationalism often outweighs economic and technical concerns, leading to sub-optimal decisions.

Another world is possible.

- Although 2/3 of Timor-Leste’s petroleum-funded period has passed, there is still time and money.
- If democracy and peace continue, the PF could support transformation to a more permanent, equitable economy.
- More than half of the population was born after the Indonesian occupation. They have had more educational opportunities and exposure to the world than their elders did.
- Sustainable, equitable development will require major changes in thinking and direction.

The Petroleum Fund from 2005 thru February 2022:

$24.3 bn oil & gas revenues
+$ 8.0 bn investment returns
- $13.6 bn withdrawn
$18.7 bn remaining
Thank you.

You can find more and updated information at

- La’o Hamutuk’s website
  http://www.laohamutuk.org
- La’o Hamutuk’s blog
  http://laohamutuk.blogspot.com/

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