



**REPÚBLICA DEMOCRÁTICA DE TIMOR-LESTE
MINISTÉRIO DO COMÉRCIO, INDÚSTRIA E AMBIENTE**

ADDRESS BY HIS EXCELLENCY

**THE MINISTER OF COMMERCE, INDUSTRY AND
ENVIRONMENT**

MR. ANTÓNIO DA CONCEIÇÃO

**ON THE OCCASION OF THE LAUNCH OF UNESCAP
REPORT TITLED: *“THE ECONOMIC AND SOCIAL
SURVEY OF ASIA AND THE PACIFIC 2013”***

Dili, 18 April 2013

Excellencies.

Ladies and Gentlemen.

Colleagues,

I have been asked to speak on the theme: *The Macroeconomic Policy Paradigm to Achieve More Inclusive and Sustainable Development in Timor-Leste*.

I accepted this challenge made by UN-ESCAP through UNDP, and I would like to take this opportunity to present what I believe could be done in Timor-Leste over the coming years so that our independence could bring meaningful benefits. I believe that the best way to honor those who gave their lives to achieve our independence is through development in a manner that engages actively all citizens and ensure that the benefits of their engagement are shared by all.

The UN-ESCAP Survey titled: *“The Economic and Social Survey of Asia and the Pacific 2013”*, which will be launched simultaneously today in more than 30 countries around the world, including capitals in the ESCAP region, New York, Geneva and hubs in Latin American and Africa, challenges us to think beyond our usual way of thinking. Today, Dr. Noeleen Heyzer, the Under-Secretary-General of the United Nations and Executive Secretary of ESCAP, will launch the *Survey 2013* in Beijing, China. The presentation of the findings of the *Survey* by Dr. Clovis Freire has pointed to some key messages that are important for all of us to reflect on. Let me reiterate some of the key messages of this report: First, the *Survey* shows that it remains unclear as to the extent to which the Asia-Pacific region’s economic growth is contributing to the achievement of key developmental goals. Second, despite a significant reduction in poverty, the Asia-Pacific region is still home to almost 800 million poor struggling to survive on an income of less than \$1.25-a-day. This figure represents nearly two-thirds of the world’s poor. Third, rapid growth in income since the 1990s has been accompanied by increases in income inequality. Fourth, the high resource intensity of economic growth has spurred a rapid rise in emissions of greenhouse gases and made countries increasingly vulnerable to commodity price shocks, while key natural resources, such as forest cover, fisheries and fresh water, have been overexploited. Fifth, economic insecurity has also risen amid rapid growth. More than 1 billion workers in the Asia-Pacific region are in vulnerable employment—characterized by low wages, no benefits, no job security and difficult conditions of work that undermine workers’ fundamental rights. Sixth, food security is also a major problem in Asia and the Pacific, with an estimated 563 million people undernourished. The *Survey* reminds us of the fact that despite the Asia-Pacific region’s rapid economic growth, hundreds of millions of people continue to be highly vulnerable and insecure. The *Survey* argues for more inclusive growth by stimulating domestic sources of aggregate demand, which can have beneficial spillover effects across the Asia-Pacific region.

Development practitioners elsewhere have tried to define what inclusive growth is all about. Inclusive growth refers to the broader idea of a growth process that includes all segments of the society. It is about the extent to which economic growth creates

opportunities for poor women and men through their active participation in markets, communities and states. Hence, part of the on-going debate on inclusive growth is about the issue of the actual contribution of economic growth to poverty reduction.

The literature¹ we know of tries to analyse the relationship between economic growth and poverty incidence across countries and time periods. These experts have shown how faster economic growth is generally associated with faster poverty reduction; the conclusion that we get from their studies show that on average, a 1 percentage point increase in the rate of per capita income growth can produce up to a 2 percentage point decrease in the proportion of people living below the poverty line. But the studies also show that this kind of relationship is not always linear and does not apply equally to all countries. Whilst some countries experienced only modest reduction in poverty incidence despite significant levels of economic growth, others experienced significant falls in the incidence of poverty even where growth had been very modest. Part of the explanation to this can be found in Ravallion's work in 2004 where he showed that the contribution of economic growth to poverty reduction depends on initial levels of inequality; his study shows that a one percent increase in income level could result in a poverty reduction of as much as 4.3% for countries with very low inequality, and as little as 0.6% for countries with very high inequality.

Despite differences in experiences across countries, evidence suggests some common features, that is, growth is inclusive when it takes place in the sectors where poor work (for example, agriculture), occurs in places where poor live (for example, relatively backward and isolated areas), uses the factors of production that poor possess (for example, unskilled labour), and reduces prices of consumption items that poor consume (for example, food, fuel and clothing). I hope that this should be the foundation of our understanding.

Part 1: An Overview of Timor-Leste's Economy

Following the political crisis of 2006 and a subsequent contraction of the economy by 3%, Timor-Leste has indeed seen strong economic recovery, growing at an annual average of 11.7% between 2007 and 2010, with an estimated 10.6% growth for 2011 and 2012. In 2013, output growth is expected to remain high at around 10%. Two factors may have contributed to this double-digit growth, namely high world fuel prices and public expenditure. The world fuel prices have allowed financial resources to be accumulated in our Petroleum Fund, which have reached US\$12 billion in March 2013, from a total of US\$2.08 billion in 2007. This is an average increase of more than 30% per annum between 2007 and 2012. The total accumulated savings in the Petroleum Fund is fifteen times the non-oil GDP. Furthermore, GDP growth of the domestic economy has been mainly driven by the large-size budgets. The national electrification project² has accounted for much of the increase in the size of the 2011 and 2012 budgets. However, the rate of execution of Capital

¹ For example, Ravallion and Chen (1997), Bruno, Ravallion and Squire (1999), Adams (2004), Pasha and Palanivel (2003) and Chhibber and Nayyar (2007).

² It is estimated that close to US\$1 billion was spent in 2011 to finance the two new power stations in Hera and Betano, a new transmission line covering all the country, and distribution network.

Development in 2012 was around 50%. If the electricity component is taken aside, the execution rate was far lower, at 29% of the total allocated for 2012.

For 2013, the fiscal envelope is US\$1.647 billion. As the country continues to be one of the most-petroleum-reliant countries in the world, more than 90% of the 2013 budget will be funded by the Petroleum Fund while the remaining is expected to come from domestic revenues, which is expected to reach US\$146 million towards the end of 2013. The ratio of this level of expenditure represents approximately 200% of the non-oil GDP. Unfortunately, domestic taxes contribute only 4.8% of total revenue, and represent only 3.4% of the non-oil GDP in 2013. Timor-Leste will have to make major efforts in order to increase the domestic revenues up to the level of international ratio of 20-25% of GDP. This is particularly necessary as Timor-Leste will want to join the Association of Southeast Asian Nations (ASEAN), planned for 2013 or later, whose experience in the area could be tapped.

Part 2: The Challenges Ahead

Like many countries in the Asia-Pacific region, Timor-Leste has a rough road ahead, full with challenges but also opportunities. The biggest challenge in my view is to be able to translate high economic growth rate into more inclusive and sustainable manner, in order for us to reduce significantly poverty, which is still the most pressing issue in the country. Let me turn into some of the challenges below that require our attention.

Timor-Leste remains a net importer of goods and services. One of the main sources of GDP growth in Timor-Leste has been imports of goods and services. As the country lacks a productive structure that can supply enough basic inputs, the need for imports of goods and services have also grown significantly over the last three years. These include intermediate inputs such as cement, fuel, steel, and other building materials, as well as capital goods and consumer goods that go directly to the public domain. Timor-Leste's dependency on imported goods has drained approximately US\$680 million of imports, notwithstanding the push for the intermediate goods to promote economic growth in the country, raising the coefficient to 0.49 per dollar of rise of the GDP. This value is significantly high, and it has to be taken into consideration when public investment is to be made although there is no foreign exchange gap in the economy.³

Inflation continues to haunt Timor-Leste. As a net importer country and as the fiscal envelope continues to expand, Timor-Leste cannot but face the inflationary pressures. Over the last two years the annual average fell from 13.5% in 2011 to 11.8% in 2012, with an expected decline of 8% in 2013. This inflation rate is higher in Timor-Leste than in countries in the Asia-Pacific region. As public expenditure remains the main driver of economic development, combined with Timor-Leste's full dependence on imports in the face of steady depreciation of the US Dollar, inflation could remain high and this could serve as a destabilizing factor. The approval of the General State Budget for 2013 with a fiscal

³ Using the traditional methodology of logarithm in order to calculate the import to growth elasticity, the value is 0.551. The coefficient can be interpreted straight forward as the percentage of change.

envelope of US\$1.647 billion will continue to place the country under inflationary pressures. The double-digit inflation, particularly in food prices over the last two years, is a serious concern that needs to be watched closely. Inflation is a crucial element to be taken into consideration when preparing budgets, not only because it has a direct impact on the goods and services that the Government purchases, but it also affects the well-being of those that have fixed incomes, putting pressure on the provision of public goods and State assistance. I believe that one of the ways to control inflation is by containing imports, particularly of food stuff that the country can produce. I will come to this issue later on.

Timor-Leste is now classified as the medium income category. Timor-Leste's Human Development Index value for 2012 was 0.576—in the medium human development category—positioning the country at 134 out of 187 countries and territories. Between 2000 and 2012, Timor-Leste's HDI value increased from 0.418 to 0.576, an increase of 38% or average annual increase of about 2.7%.⁴ Between 1980 and 2012, Timor-Leste's life expectancy at birth increased by 28.3 years, mean years of schooling increased by 1.6 years and expected years of schooling increased by 1.7 years. Timor-Leste's Gross National Income per capita increased by about 356% between 2000 and 2012. Timor-Leste's 2012 HDI of 0.576 is below the average of 0.64 for countries in the medium human development group and below the average of 0.683 for countries in East Asia and the Pacific. From East Asia and the Pacific, countries which are close to Timor-Leste in 2012 HDI rank and population size are Fiji and Solomon Islands, which have HDIs ranked 96 and 143 respectively.

However, almost half of the Timorese population continues to experience poverty, deprivation and insecure employment. In Timor-Leste 68.1% of the population lived in multidimensional poverty (the Multidimensional Poverty Index “headcount”). The multidimensional poverty figure uses 10 indicators to measure poverty in three dimensions other than just income. The three dimensions are education, health and living standards. So, if we compare income poverty, measured by the percentage of the population living with US\$1.25 a day would be 37.4% in 2007, and 72.8% (at US\$2 a day). Yet, this income poverty only tells part of the story if we look into deprivations in other dimensions to provide us with a more comprehensive picture. By including the three dimensions, the multidimensional poverty headcount is 30.7 percentage points higher than income poverty of US\$1.25 a day. This implies that the proportions of the population that are poor may still suffer deprivations in education, health and living conditions.

The contributions of deprivations in each dimension to overall poverty complete a comprehensive picture of people living in poverty in Timor-Leste. For example, nutrition contributes 20% (which is the largest slice of the pie) to multidimensional poverty. As a matter of fact, food insecurity affects up to 70% of households during the lean season from

⁴ United Nations Development Programme 2013, *Human Development Report 2013. The Rise of the South: Human Progress in a Diverse World*.

December to March,⁵ thus further exacerbating the poor nutritional status of women and children, in particular. This explains why 58% of the children suffer from chronic undernourishment.⁶ Official reports also indicate significant gaps in terms of access to adequate water and sanitation facilities, particularly in rural areas, where approximately 43% of households do not have access to clean water and 74% of households do not have access to improved sanitation.⁷ In early 2012, the Special Rapporteur on Extreme Poverty and Human Rights noted: “...poor water quality implies that only a very small percentage of Timorese have access to safe drinkable water, and many must walk considerable distances to obtain it. The lack of access to clean water and sanitation facilities contributes to illnesses among children, including diarrhoea, one of the leading causes of death of children under 5 years old.”⁸

Furthermore, income inequality has risen significantly between 2007 and 2010. The Timor-Leste *Demographic and Health Survey 2009-10* data reveals that the 75% of Timorese people who live in rural areas suffer disproportionately from poverty and disadvantage. The disparities between those who live in Dili, 71% of whom fall within the highest wealth quintile in Timor-Leste, and those who live in rural areas, are stark: rural populations experience far higher rates of chronic income poverty and food insecurity, and far lower health and education outcomes.⁹

Timor-Leste has one of the Asia-Pacific region’s youngest populations with approximately 70% of its population being below the age of 30. Youth unemployment is particularly high in urban areas with estimated youth unemployment rates ranging between 20 and 30% in the capital Dili (the definition of youth in Timor-Leste is 16 to 30 years old).¹⁰ And youth unemployment is on the rise. Given the age cohort and the relatively high population growth rate of 2.4% per annum, the new entrants into the labor market are estimated to be as many as 16,000 per year, and they will soon reach 20,000 per year in the coming years. High unemployment rates generally indicate that an economy is underperforming or its potential output (or potential GDP) has not been fully achieved. This large number of young job seekers simply cannot be absorbed unless effective policies for job creation are in place, aside from improving employment quality in the small and medium enterprise sector and cooperatives, which currently employs the majority of the youth. What is also troublesome is the fact that over 70% of total employment is vulnerable. “Vulnerable employment” is defined as those whose status in employment is own-account worker or contributing family member. By definition, the vulnerable employment rate of 70% is vulnerable employment

⁵ United Nations Development Programme 2011, *Timor-Leste Human Development Report 2011*, p. 52; *Timor-Leste Strategic Development Plan 2011-2030*, p. 109; World Food Programme, *Timor-Leste: coping with seasonal food shortages*, 1 April 2010.

⁶ Democratic Republic of Timor-Leste 2011, *Strategic Development Plan 2011-2030*, p. 40; National Statistics Directorate, *Timor-Leste Demographic and Health Survey 2009-10* (Dili, 2010), p. 150.

⁷ Democratic Republic of Timor-Leste, *Millennium Development Goals 2010 booklet* (Dili, 2010), p. 34.

⁸ United Nations General Assembly, No. A/HRC/20/25/Add. 1, *Report of the Special Rapporteur on Extreme Poverty and Human Rights, Magdalena Sepúlveda Carmona*, 24 May 2012, p. 5.

⁹ National Statistics Directorate, *Timor-Leste Demographic and Health Survey 2009-10* (Dili, 2010).

¹⁰ National Statistics Directorate, *Timor-Leste Population and Housing Census 2010*.

as a proportion of total employment. This particular segment of the working population is less likely to have formal work arrangements, and is therefore more likely to lack decent working conditions, adequate social security and “voice” through effective representation by trade unions and similar organizations. Most of the rural poor rely upon low productivity subsistence agriculture for livelihoods, and experience periods of food insecurity during the lean months.

The sectoral pattern of economic growth has been less inclusive. According to the National Accounts, the growth performances of the three major sectors of the economy, namely, agriculture, industry and services, have been diverse. The growth in the agriculture sector has been the most volatile and also the lowest among the three sectors. Growth in the industry and services sectors has been more or less constant in Timor-Leste. The agricultural sector, which is typically home to some 80% of the poor, has grown by less than 2% in Timor-Leste over the last five years, while non-agricultural sectors (industry and services) have grown by about 10% in the same period. Since a large section of the population continues to be dependent on the agriculture sector, directly or indirectly, this has serious implications for “inclusiveness”. If what matters is the pattern of growth for poverty reduction, then the sectoral growth rate in which most of the poor are employed becomes more important than the overall growth rate. This suggests that a dynamic rural sector based on the improved agricultural productivity could promote faster rural poverty reduction and thereby inclusive growth.

Increasing social spending would automatically increase living standards of a very large number of poor. However, we have noticed over the years the allocation for education and health, for example, has not been satisfactory. For example, public spending on education and health (as percentage of the non-oil GDP) has declined over the last five years. Only 4% of the non-oil GDP is spent annually on health and 6-7% on education in Timor-Leste. Although the allocation to education is 2 percentage points higher than in some of the countries in the Asia-Pacific region (for example, Malaysia, Mongolia, Thailand, and PNG), the allocation is insufficient to respond to all requirements for good quality. Healthy populations are essential not only for the sake of productive labour force for economic growth but also to achieve a healthy society is a goal in itself. As public spending on health has remained low, on average 4% as percentage of the non-oil GDP, Timor-Leste registered the highest maternal mortality rate with 557 deaths per 100,000 live births.

The emerging picture of existing educational and health related dimensions of human capital suggest an urgency to increase social spending in Timor-Leste, not only to make economic growth more inclusive, but also sustainable.

Part 3: How can we turn our economic growth into a more inclusive and sustainable manner?

The above analysis indicates several points. First, the data suggests that the economic growth impact on poverty is actually low indicating a weak relationship between growth and

poverty over the period 2007-2012. Since faster economic growth during the period did not translate into faster reduction of poverty, the natural inference would be that the distribution must have worsened. Second, economic growth has not been inclusive. This is due to uneven growth across sectors and locations in the country: growth has been uneven between agricultural (rural) and non-agricultural (urban) sectors, and the type of growth we are promoting has also been uneven across districts and sub-districts. Third, employment growth relative to gross domestic product (GDP) growth has been low and perhaps declining; employment is the primary channel through which the majority of the population can benefit from economic growth. This calls for a different direction of growth that is the one that ensures inclusiveness, which requires high employment-intensity of growth and a significant rise in productivity. Third, and related to the previous point, women's increased participation in the labor markets have may have been detrimental women because they are more likely to work in low productivity jobs, earn less, be informal workers and experience higher unemployment rates when compared to men. As a result, women may end up having lower bargaining power, hence resulting in increased inequalities overall. Fourth, there has been a relative neglect of the agriculture sector and rural development by national and international policymakers. The deterioration of rural public sector social services, lack of effective social protection, lack of access to formal credit for agricultural and micro, small and medium enterprises (MSMEs) sectors (as a result of lack of financial inclusion) have probably contributed to the exclusion of disadvantaged groups during high economic growth.

From this brief analysis, what firstly emerges is the need to have a growth pattern that generates full employment. Full employment has to be at the centre of macroeconomics, and that has to become a nationwide guaranteed wage employment. Growth in agriculture sector as the main employer in Timor-Leste is an important element of inclusiveness. By utilizing poor people's key assets of land but mostly unskilled labour, rapid agricultural growth creates a vibrant economy in rural areas where the majority of poor people live. In addition to agricultural growth, using more labour-intensive technologies and creating non-farm jobs in rural areas would also benefit the poor, particularly when land distribution is skewed in rural areas.

Let me expand a little bit on what I believe should be at the center of macroeconomics. The rationale for having a nationwide guaranteed wage employment program rests on the following four premises. First, the program will create a clear channel for income transfers to poor households to enable them to face external shocks, due to weather-related impact on food production, or inflation of imported food stuff that I have highlighted earlier. Second, income transfers to poor households will enable consumption smoothing, especially during slack agricultural seasons or years. Third, in a country like Timor-Leste with high unemployment rates, transfer benefits from such a workfare program can prevent poverty from worsening, particularly during lean periods between December and March each year. Fourth, durable assets that this program may create will have the potential to generate second-round employment benefits as needed infrastructure is developed and maintained.

In a context of high poverty incidence and persistent unemployment, such a workfare program will have important impacts for many years. The wage employment program can typically provide unskilled manual workers with short-term (three to six months) employment on public works such as, irrigation infrastructure, reforestation, soil conservation and road connectivity, such as in the case of the cash-for-work program done by our colleagues at SEPFOP. Hence, the main objective of the program, which will have to be defined and regulated by law, is to create durable assets and strengthen the livelihood resource base of the rural poor. The choice of works to be suggested in the law will address causes of poverty including drought, deforestation, soil erosion, so that the process of employment generation is likely to be sustainable. Soil erosion and deforestation are particularly high in Timor-Leste and therefore will require maintenance on a continuous base. Initially, the law should cover all the thirteen districts for a period of five years, and extension will be sought pending evaluation and impact assessments of such a program. It is the responsibility of the Government to make such a program happen, providing not less than one hundred days of guaranteed employment in a financial year to every household in the rural areas covered under the program, and whose adult members volunteer to do unskilled manual work under the uniform basic wage defined by the law.

The second point I would like to make, and it is connected to the previous one is, given that the centre of economic gravity is moving towards non-farm sectors and urban areas, particularly that of Dili, a growth pattern which addresses the issue of segmented labour markets is necessary. A major challenge for growth to be inclusive through the channel of employment is the segmented labour markets. Segmented markets offer limited mobility from low productive economic activities to high productive ones. Additionally segmented markets offer lower wages for women. Poor people rarely get jobs in high productive sectors as I have pointed out, and hardly move to higher productivity economic activities. One of the biggest challenges of inclusive growth in the Timorese context is how to increase the availability of decent, high productivity work opportunities for the poor, particularly for poor women, through employment-intensive economic growth. Providing decent employment opportunities to all, and enhancing women's equality and empowerment would also enhance progress to achieve all the off-track Millennium Development Goals since large numbers of poor and unemployed people are also an increasing threat to socio-economic and political stability.

My third point is that if we want to translate high economic growth rates into more inclusive and sustainable manner, we will have to ensure that the benefits of growth are shared widely to help build better lives by improving physical and social infrastructure. Therefore, for sustainable economic growth to happen, improvements in social and physical infrastructure will require immediate attention from policy makers in this country to not only leap-frog modern economic development for better lives, but also to keep up with modern economic growth.

Furthermore, and this is my fourth point, given the high prevalence of existing vulnerabilities in Timor-Leste, combined with frequent natural disasters due to unpredictable changes in weather, social protection policies to protect the poor from economic and environmental vulnerabilities will have to be an absolute necessity for stability and sustainable economic growth. Social protection measures such as cash transfers and employment schemes that we have been doing over the past four years will help diminish exposure to risks, and enhance capacity for self-help and resilience in the face of various shocks.

My last point is to stress the importance of inclusive finance. During my mandate, I would like to encourage our financial institutions to diversify their products beyond micro-credit, such as remittances, micro-insurance, savings accounts and other financial instruments are needed to expand financial access to all *Sucos*. I am glad to see a number of initiatives, including on-going projects that are working in Timor-Leste that facilitate financial inclusiveness such as credit bureaus and credit guarantee funds. The Fifth Government will undertake large-scale financial literacy campaigns to equip the poor to benefit from financial inclusiveness. I hope to be able to engage banks to set up more branches along transportation routes and provide mobile banking services, to extend their reach to the poor and in remote areas.

I believe that if we join our efforts together, Timor-Leste will be able to make a dent on poverty in the coming five years. Our Strategic Development Plan (SDP) 2011-2030 does offer a clear direction as to where Timor-Leste would like to be by 2030—to achieve an upper-medium income country. The SDP identifies four pillars: (i) Social Capital, which is comprised of health, education and social protection, and aims to improve human development outcomes, create a labour force with marketable skills, and protect the vulnerable; (ii) Infrastructure, including transport, telecommunication, power, and water supply and sanitation, to increase connectivity, reduce transaction costs and attract private investment, and facilitate access to services; (iii) Economic foundations, which targets three sectors for development of the non-oil sectors such as agriculture and tourism, as well as petrochemicals with the aim of creating ample job opportunities and new sources of public revenues; and (iv) Good Governance, including institutions for sound macroeconomic management, aiming at improving the capacity and effectiveness of state institutions through civil service reform and sound public financial management, and to strengthen mechanisms of oversight.

Thank you.

Minister of Commerce, Industry and Environment
António da Conceição