

Timor-Leste Must Win Independence from Petroleum

Remarks at launch of the UNDP 2011 Timor-Leste Human Development Report

By Charles Scheiner, La'o Hamutuk

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The Timor-Leste Human Development Report is a major contribution to the challenge of moving Timor-Leste away from dependency on non-renewable resource wealth.

It provides a welcome alternative to the divisive partisanship, self-censorship, and wishful thinking which often prevails here, where enticing visions are pursued regardless of whether they can be achieved. In contrast with papers based on short-term institutional or political agendas, the NHDR seriously discusses the actual situation in Timor-Leste and suggests concrete, practical ways to develop our economy to improve living standards and sustainability over the long term.

The report contains valuable ideas to improve thinking about how Timor-Leste can attain and surpass the Millennium Development Goals. It is a much-needed complement to other reports which trust in macroeconomic statistics, models or theories that don't consider the realities of each country, especially one as exceptional as Timor-Leste.

Specific recommendations to develop the non-oil economy, especially in areas of agriculture and added-value processing, will help Timor-Leste move away from its unfortunate distinction of depending more on exports of nonrenewable resource wealth than any other country in the world. The report also emphasizes the quality of public investment, and recommends that more money should be invested in health and education.

Nevertheless, it has been toned down by the inevitable cautious editing of publications by multilateral institutions which depend on government permission to remain here, and by institutional sensitivities raised by unplanned pre-release publicity.

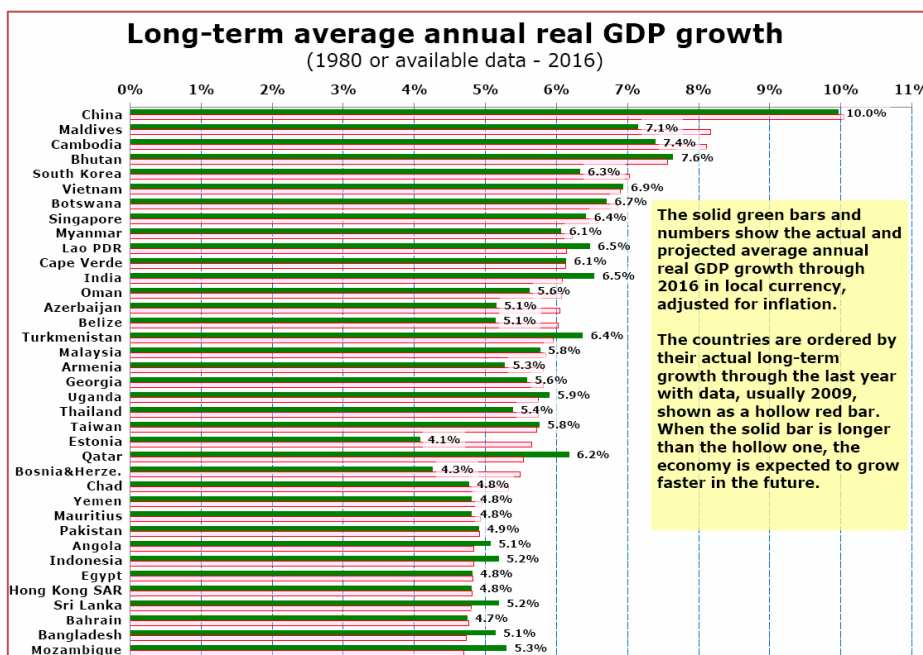
La'o Hamutuk is known for frankly sharing facts and analysis, and I won't disappoint you today. I will underline a few of the report's main points, more forthrightly than UNDP can, in an effort to help improve the lives of current and future generations of Timorese.

Gross Domestic Product – GDP – is often used to indicate the size of a country's economy.

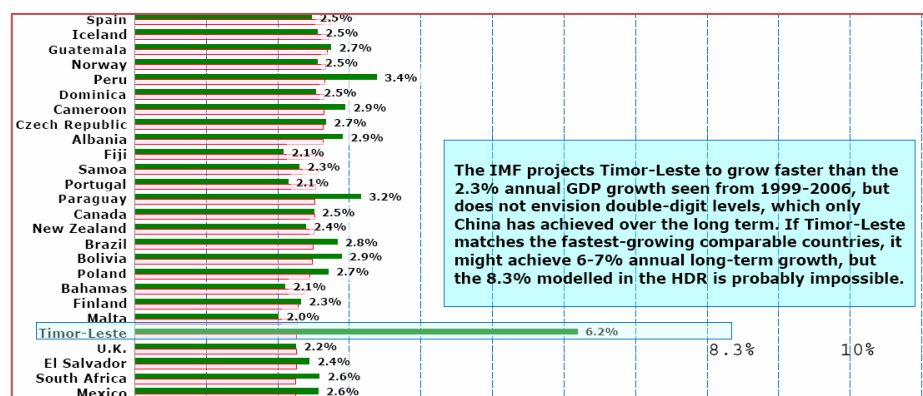
Although many experiences – most recently obvious in Egypt – show that GDP growth often doesn't benefit less affluent families, that's a discussion for another time. The HDR presents a "moderate-to-high growth scenario" to achieve annual growth in real non-oil GDP averaging 8.3% over the next 15 years. Although this is less fanciful than the double-digit dreams behind some macroeconomic models, it is still unrealistic.

China is the only nation which has achieved such growth rates over a long period, and Timor-Leste is totally different from China in size, education, population control, industrialization, government management of the economy, export markets, working conditions, wages and human rights.

Timor-Leste cannot increase its non-oil GDP over the long term more than any other country. This graph shows average real GDP growth since 1980 (or when data is



available) in every country, as well as projections through 2016. China has achieved 10%; the Maldives, Cambodia and Bhutan are between 7 and 8%; with a few others between 6 and 7%. Optimism often can be useful, but impossible dreams are impossible to achieve.

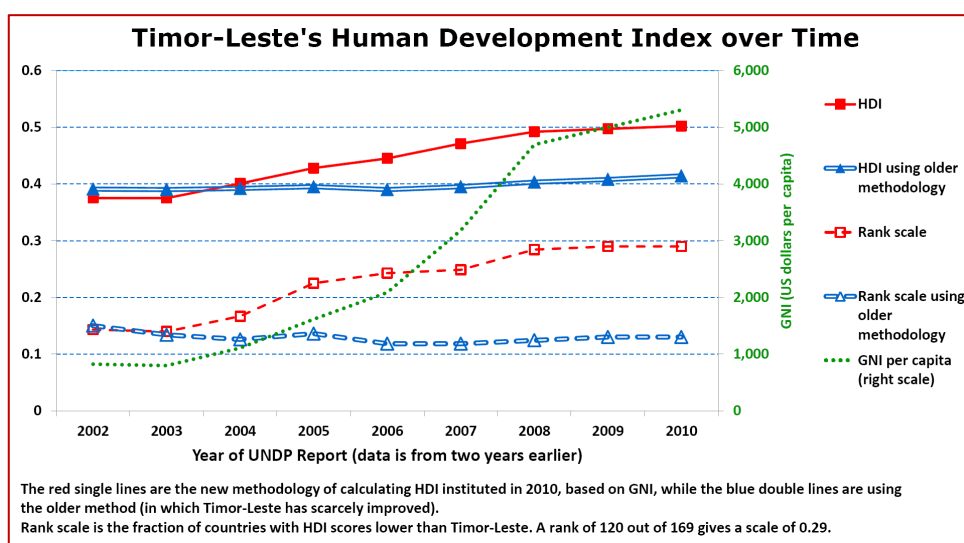


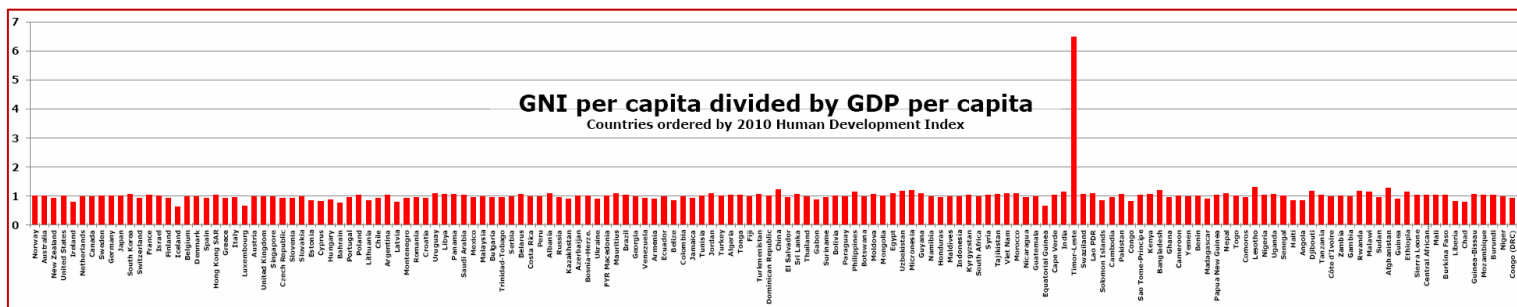
Every year, UNDP calculates a Human Development Index - HDI - for every country, combining indicators of health, education and income. As the graph and table show, Timor-Leste has improved slightly and now ranks 120th of 169 countries, based on data from 2008.

Timor-Leste: Human Development Index Trends, 2005-10

Year	Life expectancy at birth	Expected Years of Schooling	Mean years of schooling	GNI per capita (PPP US\$)	HDI value
2005	59.7	11.2	2.8	1,167	0.428
2010	62.1	11.2	2.8	5,303	0.502

In 2010, UNDP changed how they calculate the HDI, making it a less accurate indication of human development for Timor-Leste. In 2009, our HDI ranked Timor-Leste 162nd of 182 countries, but applying the new methodology to past data, as shown by the red lines in the graph, our rankings for 2009 and 2010 are identical. Applying the older methodology, blue lines, shows negligible progress in Timor-Leste since the restoration of independence.





One change was to substitute Gross National Income (GNI) – which includes offshore oil revenues – for GDP to indicate a country’s economic development. For most countries this did not change much; only six of 169 countries have a GNI more than 20% above their GDP. Kiribati has the second largest difference in the world, with a GNI 79% more than its GDP. But Timor-Leste is unique – our GNI is more than six times larger – 548% higher – than our GDP. This is a consequence of our extreme dependence on exporting nonrenewable resources. Since Timor-Leste has wisely created a Petroleum Fund to extend people’s benefit from these resources, the GNI is not reflected in the lives of individual citizens today.

UNDP also changed the education indicator in the HDI, from literacy to years of schooling, to distinguish small differences among highly-educated countries. In places like Timor-Leste, with inferior quality and resources for education, this does not measure education. A malnourished child who sits for a year at a shared desk (or on the floor), without books, listening to an underqualified teacher in an unfamiliar language, will not learn as much as a student in a more affluent country with well-equipped facilities and experienced teachers.

The background papers for this Human Development Report were written in 2008. Two and a half years later, some information is out of date.

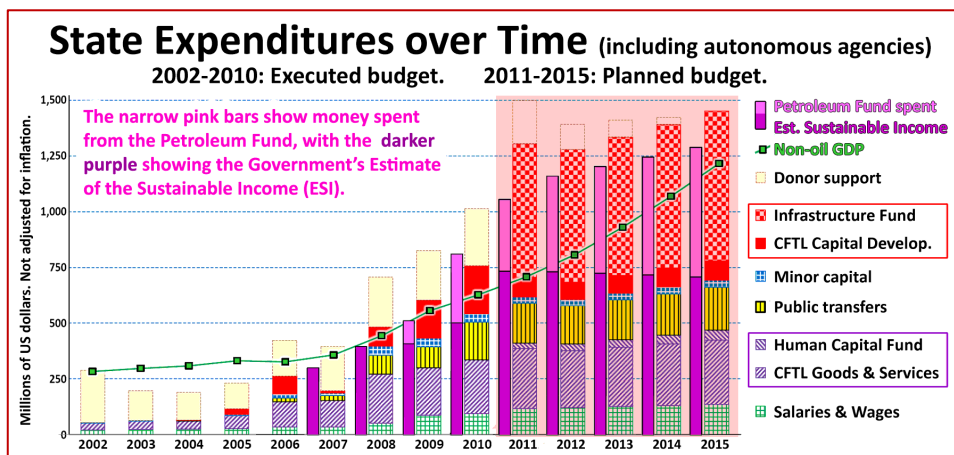
Most of the HDR was written more than a year ago and uses data from 2009 or early 2010. Since then, events have moved Timor-Leste further from the report’s recommendations. Recent policies, particularly unsustainable state spending levels and prioritizing capital mega-projects over human resources, have pushed this country deeper into the “resource curse,” while doing little to develop the non-oil economy.

For example, the report says that Timor-Leste allocated 15.6% of state expenditures to the social services sector – health and education – in the 2010 budget. The report explains that countries making progress toward the MDGs spend about 28% of their budgets on this sector, concluding “that not enough priority is being accorded to education and health. If Timor-Leste is to move faster in achieving the MDGs in these areas, then the share of social services in the budget will have to be virtually doubled.”

Share (%)	State Budget ^a		Including Donors 2010 Budget
	2009 Budget	2010 Budget	
Executive	21.5	21.9	20.3
Legislative	2.0	2.5	2.2
Judiciary	3.0	2.8	3.6
Social Protection ^b	12.4	9.7	8.6
Directly Productive Activities	14.5	9.3	9.2
Social Services	14.0	15.6	18.3
Physical Infrastructure	19.5	26.1	24.7
Defence and Security	9.6	7.1	8.9
Autonomous Agencies	2.9	4.6	3.5
Others	0.6	0.4	0.5
Total	100.0	100.0	100.0

After that part of the report was written, Timor-Leste enacted two more State Budgets, doubling overall expenditures. The percentage allocated to social services in the 2011 State Budget is 9.6%, less than two-thirds the previous year.

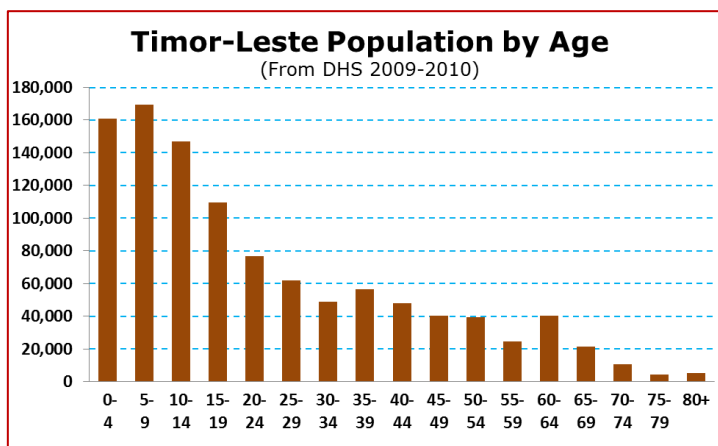
More generally, recent rapid growth in public spending is likely to accelerate when the Strategic Development Plan is implemented and the State takes out loans. The HDR discusses the “resource curse” at length, diplomatically declining to state that Timor-Leste is already suffering from it, and suggesting improvements in institutional capacity to prevent it.



La'o Hamutuk believes that the resource curse is already here, manifesting itself in a range of symptoms including inflation (“Dutch disease”), extreme import dependency, neglect of non-oil sectors and revenue sources, ineffective public expenditures, credible rumors of corruption, and failure to plan for the long term. This curse is not inflicted by a malevolent supernatural force, but by the economic and political situation of a new country with a tiny non-oil economy and a large number of impoverished people. It afflicts almost every petroleum-dependent country, although it may be possible to overcome with long-term planning and implementable policies based on facts, as the HDR recommends.

One cause of the resource curse, which is exacerbated by democracy, is the failure to implement policies with goals beyond the term of the next project, election or MDG deadline. One example is the issue of jobs, often highlighted as a “youth unemployment” problem. The HDR reports that 15,000 young Timorese enter the labor market each year, and there only a few hundred new jobs to keep them occupied. Although this is true, it ignores the more fundamental problem: Timor-Leste does not have enough jobs for everyone who wants or needs to work.

Many people had children after the referendum, and Timor-Leste has twice as many people between the ages of 0 and 9 as between 20 and 29. In the year 2023, 34,000 young people will enter the job market, and today’s youth will need full-time, permanent jobs to support their own children. Bayu-Undan and Kitan will be used up. Without a non-oil economy, Timor-Leste will be in serious trouble.



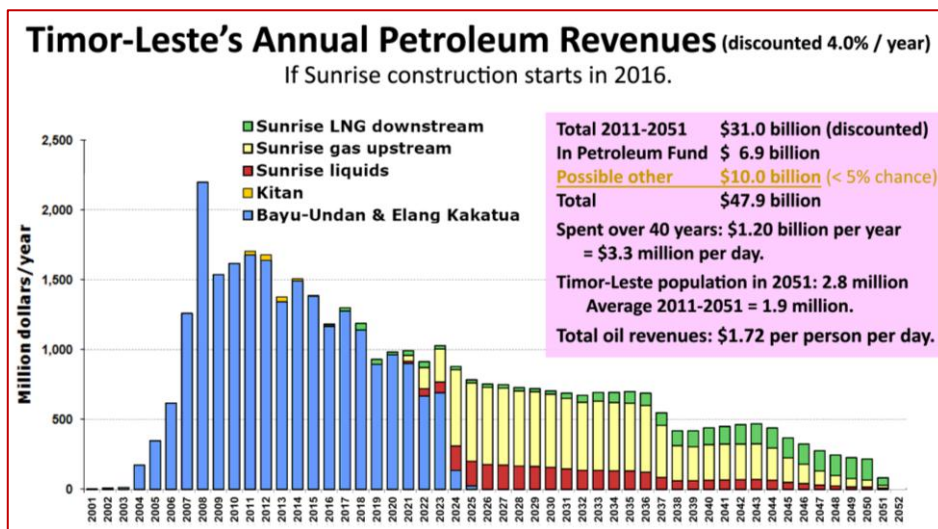
Timor-Leste’s oil and gas reserves are extremely limited, and I am more willing than UNDP to be the bearer of bad news.

Currently producing oil and gas fields will run dry in 12 years, and all known reserves in 40.

Timor-Leste is the most petroleum-dependent country in the world, with oil revenues paying for 95% of Government expenditures. The state’s oil and gas revenues are four times larger than Timor-Leste’s entire non-oil economy. Everyone wishes Timor-Leste had as much oil and gas as Norway or Brunei, to underpin our economy for the indefinite future. Unfortunately, this is not the case, and our total nonrenewable resource wealth is not enough to pay for the quality of life Timor-Leste’s people deserve.

This graph is based on optimistic assumptions, similar to the Government's:

1. Long-term global oil prices will be as high as those used to estimate the Estimated Sustainable Income (ESI) in the 2011 budget, which are 40% higher than those used in 2010.
2. Timor-Leste will build an onshore plant to process Sunrise LNG.



Although this debate may take a few years more, we believe it is better for Timor-Leste to prolong Sunrise revenues, saving the gas in the ground until it is needed to replace Bayu-Undan's declining revenues.

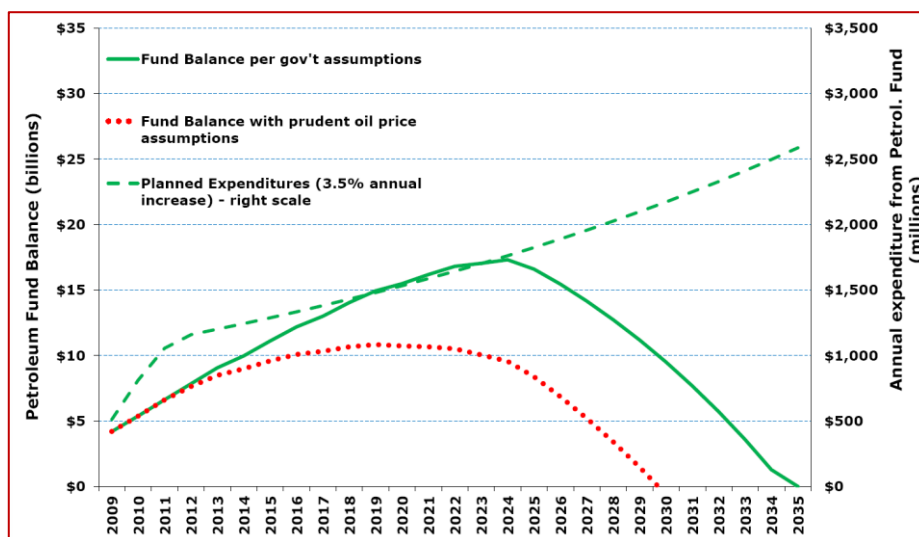
3. Oil exploration will discover additional fields in Timor-Leste, with a total value 70 times larger than the Kitan field. This is very unlikely -- Kitan is the only new discovery since the mid-1990s, although ten exploration wells have been drilled since independence.

These assumptions are less prudent than the ones La'o Hamutuk normally uses, as we prefer to err on the side of caution. But today I don't want to distract attention from my main message. (For the same reason, the HDR sometimes accepts dubious premises or omits controversial topics. Although this may be advisable in Timor-Leste's polarized climate, consideration of all relevant realities is necessary to come up with effective, achievable, practical goals and strategies for developing the nation's future.)

The Sunrise gas project, even with an LNG plant in Beaçu, will provide limited revenues and very few Timorese jobs. Using the Government's projections for oil prices and discount rate, an on-shore LNG plant will create about \$3 billion in additional state revenues, adding to \$13 billion from Sunrise gas and oil extraction and \$15 billion from Bayu-Undan and Kitan. Together with \$7 billion in the Petroleum Fund already, Timor-Leste's total petroleum wealth could be \$48 billion. If this is spent as it comes in, it will provide an average of \$1.72 for each Timorese citizen for each day of the next 40 years, and nothing after that.

Timor-Leste's Petroleum Fund saves some oil wealth for future generations, and is sustainable if investment targets are achieved and no more than 3% of the total petroleum wealth is spent each year. With the optimistic projections I mentioned above, and the invalid assumption that the ESI guideline will be followed, the ESI when the all these potential reserves run out in 2051 will be \$1.41 per person per day, about half of the \$2.65 per person per day which is being withdrawn from the Fund in 2011.

If Timor-Leste continues to spend more than ESI, as the Government has done since 2009 and plans to do for the foreseeable future, this will be much less. In the worst case – if Sunrise is



not developed and no significant new oil fields are discovered -- current spending plans will empty the Petroleum Fund entirely by 2035 under Government price assumptions, and by 2030 under more prudent ones. Today's babies will be starting to look for work.

If we have not developed other sectors of our economy – agriculture, tourism, small industry, food processing – Timor-Leste will have more poverty and poorer public services in 30 years than it does today. We will no longer be able to import food and water, or to pay for scholarships, advisors or contractors from overseas.

UNDP's Human Development Report emphasizes developing Timor-Leste's non-oil economy to avoid this disaster, and I hope everyone here today will join the rest of Timor-Leste's people in the hard thinking, difficult decisions and serious work necessary to make this happen.

Thank you.