Democratic Republic of Timor-Leste
Ministry of Finance

Pre-Budget Statement

2022

Including the 2021 Mid-Year Report

Preface

Timor-Leste is aspired to the best international practice of Public Financial Management and the country is working its way to achieve a sustainable budgeting through several reforms. The continued publication of the Pre-Budget Statement, including the Mid-Year Report, represents a continuous step forward by the Ministry of Finance in the area of public financial management reform.

This document sets out the government priorities for the next fiscal year and for the medium term, describing their alignment to the proposed General State Budget. It details the proposed budget strategy for 2022, highlighting allocations to the various institutions, new measures and the fiscal sustainability implications. It also outlines the macroeconomic, fiscal and social context, their key developments, risks and forecasts over the medium term. The Pre-Budget Statement also covers trends and projections for other sources of financing i.e. Petroleum Fund's revenues and returns, domestic revenues, loans and grants.

The Pre-Budget Statement aims, above all, to enhance transparency and disclosure in Timor-Leste's budget process. As such, this report hopes to stimulate positive and constructive discussions across and within Government, Private Sector, Civil Society Organizations, International Partners, the People of Timor-Leste and other interested parties, expanding participation to the budget journey to all its stakeholders.

I am convinced that the 2022 Pre-Budget Statement will increase awareness and understanding of the Government's financial management and help the People become good and informed citizens by providing them with relevant information on the 2022 Pre-Budget. The inclusion of the Mid- Year Report highlights the commitment Ministry of Finance has to openness, by providing information on government expenditure and execution, as well as domestic revenue collections, for the first half of the fiscal year.

I wish to express my appreciation to the Directorates and Units of the Ministry of Finance that have contributed to the drafting and compilation of this report, whose work has been essential to its publication.

This documentation is available for consultation on the website of the Ministry of Finance, www.mof.gov.tl. Inquiries relating to this publication should be directed to the General Directorate of Planning and Budgeting on e-mail jcarvalho@mof.gov.tl – tel. +670 77304362, syaquim@mof.gov.tl – tel. +670 77305809, epmartins@mof.gov.tl – tel. +670 77879183 and lfraga@mof.gov.tl – tel. +670 77261102.

GABINETE DO MINISTRO
MINISTÉRIO DAS FINANÇAS
MINISTRO

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Abbreviations

Appropriation Category	AppCat
Asian Development Bank	ADB
Autonomous Agencies	AA
Autonomous Service Of Medicines And Health Equipment	SAMES
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Classification of the Functions of Government	COFOG
Council of Administration for the Infrastructure Fund	CAFI
Consolidated Fund of Timor-Leste	CFTL
Consumer Price Index	CPI
Dalan Ba Futuru (Timor- Leste)	DBF(TL)
Democractic Republic of Timor-Leste	RDTL
Development Partner	DP
Direct Budget Support	DBS
Timor-Leste National Police	ETNP
Economic Recovery Plan	ERP
European Union	EU
Falintil - Defense Force of East Timor	F-DFTL
Financial Management Information System	FMIS
General State Budget/ Orsamentu Jerál Estadu	GSB/ OJE
Goods and Services	GS
Government of Timor-Leste	GoTL / GovTL
Government Resource Planning	GRP
Gross Domestic Product	GDP
Gross National Income	GNI
Human Capital Development Fund	FDCH
Human Capital Index	HCI
Human Development Index	HDI
Infrastructure Fund	IF / FI
Integrated Financial Management Information System Unit	IFMISU
Integrated Municipal Development Program	IMDP (PDIM)
National Institute for Health	INS
International Development Agency	IDA
Laboratory National	LABNAS
Line Ministries	LM
Ministry of Agriculture and Fisheries	MAP
Ministry of Defence	MD
Minor Capital	MC
Ministry of Education including SEJD	MEJD
Ministry of Finance	MoF
Ministry of Health	MoH
Ministry of Interior	MI
Ministry of National Liberation Combatant Affairs	MACLAN

Ministry of Planning and Strategic Investment	MPIE
Ministry of Public Works	MoP
Ministry of Social Solidarity and Inclusion	MSSI
Ministry of Tourism, Commerce and Industry	MTCI
Ministry of Transport and Communications	MTC
National Communication Agency	ANC
National Development Agency	ADN
National Directorate of Budget	DNO
National Intelligence Agency	SNI
National Police of Timor-Leste	PNTL
Nominal Effective Exchange Rate	NEER
Organization of the Petroleum Exporting Countries	OPEC
Petroleum Fund	PF
Planning, Monitoring and Evaluation Unit	UPMA
Programme Budgeting	PB
Public Financial Management	PFM
Public Service Commission	PSC/CFP
Public Private Partnerships Unit	PPPU
Public Transfers	TP
Quarter 1	Q1
Quarter 2	Q2
Real Effective Exchange Rate	REER
Self-Funded Agency	SFA
Salaries and Wages	SW
Secretariat of State for Art and Culture	SEAC
Secretariat of State for Environment	SSE/SEA
Secretariat of State for Youth and Sport	SEJD
Special Administrative Region of Oé-Cusse Ambeno - Special Zones of Social Market Economy	RAEOA-ZEESM
Strategic Development Plan	SDP/PDE
United Nations Development Program	UNDP
World Bank	WB

1 Technical Disclaimer

Timor-Leste’s 2022 Pre-Budget Statement, including the Mid-Year Report, is published prior to the 2022 General State Budget Book. For this reason, all economic projections contained in this statement are preliminary in nature and may be amended in the 2022 General State Budget Book publication.

Both the aggregate budget ceiling and the proposed allocations to Line Ministries, Self-Funded Agencies (SFAs), Municipal Authorities and other relevant entities, as approved by the Council of Ministers, may be subject to change, following the Budget Review Committee revision, the Parliamentary discussions and Presidential assessment. Finally all 2021 actual figures for revenue and expenditure are preliminary, and might be amended at the closure of the 2021 financial year, once reconciliation of accounts by the Directorate-General of Treasury in the Ministry of Finance has occurred.

2 Executive Summary

Government Policy

Timor-Leste's Strategic Development Plan 2011 - 2030 is organized around four pillars: Institutional Framework, Social Capital, Economic Development and Infrastructure Development, all of which are priorities in the VIII Constitutional Government's mandate.

Based on these pillars, the VIII Government has set out 6 key areas for 2022. These are:

- Development of Human Capital (Education, Training and Health)
- Housing and Social Inclusion
- Productive Sectors (Agriculture, Tourism), Environment and Connectivity
- Private Sector Development
- Rural Development
- Good Governance

The proposed 2022 budget ceiling is set at $1.7bn (including development partner commitments) and its split across the funding sources as in the table below. The proposed 2022 Budget allocates the largest share to the Institutional Framework pillar, followed by Infrastructure Development, Social Capital and Economic Development.

Table 1: Combined Sources Budget 2019-2022, $ Millions

	2019 Actual	2020 Budget	2021 Original Budget	2021 Supplementary Budget	2022 Budget Proposal
Combined Sources Budget	**1,405.60**	**1,681.00**	**2,050.10**	**2,185.40**	**1,729.80**
Government Expenditures by Fund	**1,243.80**	**1,497.00**	**1,895.00**	**2,030.30**	**1,571.60**
CFTL (excl. loans, inc. social security, inc. DBS)	1,169.60	1,426.30	1,811.30	1,946.60	**1,492.60**
European Union - Direct Budget Support *	6.7	10.6	9.1	9.1	**15.6**
Australia - Direct Budget Support					**6.6**
HCDF	17.8	10.7	13	13	**10**
Borrowing/Loans (disbursements)	49.8	60	70.7	70.7	**69**
Development Partner Commitments	**161.8**	**184**	**155.1**	**155.1**	**158.2**

*Source: National Directorate of Budget and Development Partnership Management Unit, Ministry of Finance, 2021. * International Labour Organization also provided $0.7 million in one-off support in 2020*

Impact of COVID-19

Timor-Leste recorded its first COVID-19 case on 21st March 2020. As of 9th September, there have been a total of 18,211 cases of COVID-19 detected in the country and 88 deaths.

Following the first confirmed case in the country, President Lu-Olo declared a State of Emergency to run from 28th March which has subsequently been extended numerous times and is still in place currently. In March 2020, the Government asked National Parliament to approve a $250 million extraordinary transfer to reinforce the Treasury account during the duo-decimal regime and establish the COVID-19 Fund. This new law was promulgated by President Lu-Olo on April 6th. The first $150 million transfer was made in April with the second $100 million transfer made in May. Of the $250 million transfer, $150 million was assigned to the COVID-19 Fund, with broad spending on programs, and sub-programs, related to the COVID-19 response. This included funding for prevention and combating COVID-19 which focused on the acquisition of essential medical equipment and goods, the creation and maintenance of isolation centres and training for key staff. The remainder of the extraordinary withdrawal, totalling $100 million, was used to finance the Treasury account. In June 2020, through enactment of Law No 5/2020, the Parliament approved a second round of the extraordinary withdrawal from the Petroleum Fund totalling $286.3 million. This amount was to be split between the COVID-19 Fund ($69.5 million) and supporting the Treasury account ($216.8 million). It was withdrawn in two parts, one in August ($169.5 million) and the other in October ($116.8 million). Following the approval of Budget 2020 in October, another withdrawal was done in December ($350 million). Hence, the total withdrawal from the Petroleum Fund in 2020 was $886.3 million out of the $963.9 million approved by the Parliament.

In the final 2020 budget (approved in October 2020), the COVID-19 Fund received a total allocation of $333.2 million. This was divided with $151.1 million to Goods and Services, $165.9 million to Public Transfers, $4.1 million to Minor Capital and the final $10.2 million to Capital and Development. By the end of Q4, 2020, it had executed $194.7 million, giving an execution of 58.4%. In the original 2021 Budget, the COVID-19 Fund was due to receive $31.0 million to focus on risk mitigation and recovery measures. $23.9 million was allocated to Goods and Services, $3.5 million to Public Transfers and $3.6 million to Capital Development.

The first cases of community transmission were declared on 26th February as an outcome of the mass testing. On 7th March 2021, the first cases of community transmission in Dili were announced. On the 24th March the Council of Ministers approved the Law Proposal draft for the first amendment to Law No. 14/2020 of December 29th, which approved the 2021 General State Budget. The amendment increased the budget by a further $198.4 million (excluding donor funded spending). However due to internal budget reallocations, additional spending to cover these new activities will total $135.3 million.

The amendment focused on 6 key areas:

1. Employment support
2. Moratorium on credit
3. Exemption from tuition fees
4. Food acquisition
5. Support to frontline professionals
6. COVID-19 prevention and mitigation measures

The final rectified budget was approved by Parliament on the 27th April 2021. There was no changes to the total government expenditure but some additional adjustments to the appropriation category allocations. The approved budget had additional spending of $317.1 million, with $182.4 million in budget reallocations, meaning the overall increase remained $135.3 million. This did not include the additional $39.1 million rebalancing from line ministry's virements towards Cesta Basica between January to March 2021. The law was passed unanimously (with 20 abstentions). The largest economic recovery measure, $45.3 million, was assigned to National Institute of Social Security to implement employment support initiatives.

$34.5 million was allocated to Ministry of Health to implement the COVID-19 vaccination program, increasing quarantine facilities, purchasing PPE equipment and extending contact tracing initiatives. Funds were also given to the National Centre of Logistics and the Integrated Center for Crisis Management, as well as to provide subsidies for frontline workers and support the conclusion of the Cesta Basica Programme.

Impact of Cyclone Seroja

On Easter Sunday 4th April, Timor-Leste was impacted by a severe natural disaster known as cyclone Seroja which caused the largest amount of rainfall in 30 years and devastating flooding and landslides. The disaster caused great devastation including material loss and deaths. In total, 48 people lost their life and 30,350 people were dislocated across 6 different shelters across Dili (São Tiago Church Hera, Canossiana Convent Hera, Dom Bosco Comoro Dili, Ex Metiaut Restaurant, Rate-Ain near Canossa Comoro, and Manleuana Suco Centre). The most severely impacted areas were Dili, RAEOA (Oé-Cusse), Manatuto, Ainaro, and Viqueque. Dili, Ainaro and Manatuto experienced most of the fatalities.

In response, on April 9th 2021 the state declared the situation a national calamity as per Government Resolution No. 32/2021. The government originally allocated $2,247,064 in response. The fund was for clean water and food, construction materials, temporary wall protection for water and rivers. A total number of 3,710 people benefitted with 3,138 people receiving non-food support and 2,093 people receiving construction materials. Apart from the government aid, victims also received support from local support groups and the international community.

To ensure that the state is well prepared for responding similar event in the future, the Ministry of State Administration through Unit for Civil Protection Mission and Management of Natural Disaster has established a number of policies and initiatives including: identifying risk areas and banning communities to construct houses in risk areas, improving knowledge and infrastructure to mitigate risk from natural disaster, preparing and informing to the community to have culture of risk prevention and developing an efficient alert system. Moreover, a working group looking at implementation, measurement and prioritisation of natural disaster risk mitigation has been developed. A pilot multi-functional accommodation centre will be established with the objective to respond to natural disasters across the territory and contribute to urban reorganization, decentralization policy and local power. $57.3 million from the 2021 Rectified Budget was to be used to fund infrastructure maintenance and rehabilitation following the impacts of cyclone Seroja (including an extra $54 million in reallocations within the Infrastructure Fund).

Petroleum Fund Revenue

The Petroleum Fund revenues remain the main source of funding for the state budget. They consist of petroleum revenue and investment income. The Petroleum Fund projections are updated once a year as part of the Budget process. The projections used in this Pre-Budget Statement are the same as the 2021 Budget Book and will be revised in the final 2022 Budget.

For 2021, Petroleum Revenue was estimated at $68.1 million. As of May 2021, receipts from the sale of oil and gas amounted to $104.7 million. Actual receipts are 54% higher than the projection used in the Budget 2021 and have been pushed higher by oil prices. As of May 2021, the Fund's investment return is 3.47%, which translates to $633.8 million. The 2021 ESI remains at $547.9 million as in the 2021 Budget and the proposed total withdrawal for 2021 remains at

$1,377.6 million ($1.4 billion). Up until May 2021, transfers to the State Budget amounted to $350 million and the balance of the Petroleum Fund is $19.4 billion.

Macro-Fiscal Overview

Economic growth is forecast to contract by -8.1% in 2020 due the combined effect of the delayed budget, COVID-19 and the State of Emergency (at the time of writing we currently do not have the final National Accounts figures for 2020). However it is expected to return to positive growth of 1.9% in 2021.This return to growth is driven by an end to political uncertainty and return to strong government expenditure. Although this has been revised down due to COVID–19 confinement, the recent floods and poor execution of the large state budget by Q2 2021. Meanwhile, inflation is expected to rise in 2021 to 2.3%, remaining steady in 2022 at 2.0%. This is due to increasing food prices, domestically and globally.

Domestic revenues reached $66.4 million by the end of June 2020, a decline of $20.4 million on collections at the same time the year before. This is a fall of 23.5%. The main factor for this is that from the start of 2021, Electricidade de Timor-Leste E.P. (EDTL) and BEE Timor-Leste E.P. became Public Enterprises. This means that while they remain in the public sector, their revenues are no longer counted in in the Treasury account as they are not included as part of the General Government. Public Enterprises are the most autonomous of all public entities. However even when including these new public enterprises back into the total, to allow a like-for-like comparison, revenues are still only 86% of those at the same point last year. This is largely due to a rapid decline in tax revenues in Q1 due to the impact of the global COVID-19 pandemic and the associated state of emergency enacted in Timor-Leste, as well as the knock-on effects of cyclone Seroja to business activity.

Preliminary forecasts see domestic revenue set to equal $131.9 million by the end of 2021 and $148.0 million by the end of 2022. Following a fall in 2021, non-oil receipts are set to be on a consistent growth trend for the next 5 years; nearing $217.4 million by 2026 provided that positive macro-economic conditions hold, plus the approval of the VAT Law in the coming years. Enacting further key fiscal policy reforms would help to increase this growth even further.

Fiscal Sustainability Analysis

Timor-Leste is highly dependent on the Petroleum Fund to finance the fiscal deficit, therefore this is the main focus of any fiscal sustainability analysis. The long term sustainability of the Petroleum Fund is dependent only on this year’s choice of budget, but also the choices made for the subsequent years.

The analysis shows that if expenditure grows at the same rate as it has historically, the Petroleum Fund will run out in just 13 years. If the growth in expenditure is capped to keep real per capita spending the same (i.e. equal to the growth in the population and inflation), the Fund will be fully utilised within 20 years. Finally if the growth in expenditure only grows in line with the growth in domestic revenues (assuming total Petroleum Fund withdrawals are capped at $1 billion a year), the fund will still be expected to contain $4.5 billion by 2052.

Historical Expenditure Analysis

Timor-Leste was under duo-decimal DOT regime for the majority of 2020 (January – September) as the budget was not passed on a regular schedule. During the duo-decimal DOT regime, only up to 1/12 of the previous year’s original budget could be distributed per month. This meant that while the core functions of government could continue, some policies outside of normal annual activity were not be able to take place (for example the Census) and significant infrastructure projects are restricted. 2020 was also impacted by global COVID-19 outbreak and the related lockdowns both in Timor-Leste and around the world. Final execution based on the approved budget for 2020 was 76.4%. This is lower than previous 5 years where the average rate was 85.6%.

Loans and Public Private Partnerships (PPPs)

Loans – At present, external loans are provided by international multilateral banks such as the Asian Development Bank and the World Bank, and one bilateral loan from JICA. These have a considerable degree of concessionality and compare favourably to the opportunity cost of withdrawing funds from the petroleum fund.

At the end of 2020, debt stock increased to $218.37m. Considering the Covid-19 outbreak, fall in disbursement is expected in 2021 as construction projects may suffer delays.

There are currently 18 ongoing road projects funded by concessional loans of which 9 projects had already been completed. Other projects that most likely to be concluded by 2021/2022 bringing the total numbers of projects completed to 80% by end the year.

Infrastructure development is expected to continue playing a key role in the country's economic development in the medium term. Strategic sectors such as water, education, telecommunication, and air transports should receive concessional financing. This would help unleash the growth potential of other key economic activities, leading to inclusive economic growth and poverty reduction. The Government is therefore proposing an estimated ceiling of $395m for new concessional foreign loans to be negotiated in 2022.

PPPs – The PPPs projects are currently ongoing: the Tiber Bay Port PPP which is in the Implementation and Operation Stage, the Medical Diagnostic PPP, in the procurement and negotiation stage, the Affordable Housing PPP, Cristo Rei PPP and President Nicolau Lobato International Airport, in Feasibility Stage.

Development Partners

Development Partners' support reached $162.1 million in 2020. It is forecast to fall to $155.1m in 2021, a decline of 4.3%. 2022 is scheduled to experience a slight 1.9% increase compared to 2021 planned disbursements, with a forecast total of $158.1 million. Amounts for 2023 and 2024 show a dramatic decline, at $110.0 million and $82.6 million respectively. However it is important to note that historically development partner multi-year indicative future spending tends to be underreported.

3 Macro-Fiscal Overview

3.1 Summary

Table 2: Economic Indicators, 2020-2023, %

Summary		Forecast		
	2020	**2021**	**2022**	**2023**
Real GDP (non-oil)	-8.1%	1.9%	-0.1%	2.7%
Inflation CPI	0.5%	2.3%	2.0%	1.8%

Source: National Directorate of Economic Policy, Ministry of Finance, 2021.

- Real non-oil GDP growth is negative by 8.1% in 2020 due the combined effect of the Budget being delayed, political uncertainty, COVID-19 and the State of Emergency. 2021 is due to see GDP return to positive growth of 1.9% although this has been revised down due to Covid-19 confinement, the recent floods and poor execution of the large state budget by Q2 2021. The very low state budget execution for 2021 indicates that Timor-Leste does not have the absorptive capacity to spend such a large budget.
- 2022 is due to see a slight decline in GDP as budget allocation is reduced compared to OJE 2021 in order to put public finances on a sustainable footing in order to preserve the country's Petroleum Fun, but is due to return to positive growth in the in 2023.
- Inflation is expected to remain increase and stable at 2.0% and 1.8% in 2022 and 2023 respectively. This will positively contribute to increasing Timor-Leste's competeveness, with inflation expected to be lower than the regional average of around 2.7%.
- Between June 2020 and June 2021 the US dollar depreciated by -3.8% against a weighted basket of currencies of Timor-Leste's trading partners (the nominal effective exchange rate, NEER). There has been a small overall appreciation in the last few years which has reduced the price of imports, placing downward pressure on domestic inflation, benefiting Timorese consumers. However, this appreciation also made Timorese non-oil exports more expensive in international markets constraining the development of the country's exports. Therefore the recent depreciation in the nominal effective exchange rate could benefit exports.
- The exchange rate forecast suggests a small depreciation with Timor-Leste's trading partners in the medium term, 2021 to 2024, which should provide a boost to competitiveness.

3.1.1 Growth

Timor-Leste

Given the relatively low level of employment in the oil sector, total GDP is not the best measure of economic performance for Timor-Leste. Instead, it is more useful to monitor economic performance using non-oil GDP together with a wide variety of other indicators relating to the non-oil economy. This approach provides a more accurate indication of the real impact of changes in the economy on the people of Timor-Leste.

In 2019, non-oil real GDP in Timor-Leste grew 1.8% to $1,592m. National Accounts data exist up to 2019, which is the latest year of GDP data available without forecasting.

Timor-Leste experienced GDP growth, averaged 3.1% per year over 2010-2019. These growth rates have been driven by increases in government expenditure associated with the government's economic strategy to ensure that Timor-Leste has the necessary infrastructure to allow the private sector to flourish in the long-run. The Government's economic strategy uses loan financing and excess withdrawals[1] from the Petroleum Fund to finance high quality investment in infrastructure and human capital development. As outlined in Timor-Leste's Strategic Development Plan, the Government's high return investments will provide the necessary foundations for long-term sustainable private sector led development. Government investment has enabled a significant upgrade to road and electricity coverage throughout Timor-Leste, which has helped to improve both living standards and the business environment.

Non-oil GDP growth in 2019 showed signs of recovery from the recent episodes of negative growth (-4.1% in 2017 and -1.1% in 2018). The contraction was a consequence of declines in government expenditure, private sector investment and lower exports. Political uncertainty also led to lower development partner spending and reduced business activity. The coffee harvest, the main source of exports, was affected by a poor season. The preliminary non-oil GDP growth forecast for 2020 is -8.1% due to a duodecimal system, political uncertainty and impact of Covid-19. Forecasts for 2021 indicate a return to positive growth of 1.9%.

International

Table 3: Growth Indicators, 2019-2022, %

Country	Actual		Forecast	
	2019	2020	2021	2022
World	2.8%	-3.3%	6.0%	4.4%
Advanced Economies	1.6%	-4.7 %	5.1%	3.6%
Emerging and Developing Economies	3.6%	-2.2%	6.7%	5.0%
Emerging and Developing Asia	5.3%	-1.0%	8.6%	6.0%
China	5.8%	2.3%	8.4%	5.6%

Source: IMF World Economic Outlook, April 2021.

Global growth outlook is projected to recover to 6.0% in 2021. Advanced economies growth is projected at 5.1%, while growth for emerging markets and developing economies is forecast to experience a stronger rebound than advanced economies growing at 6.7% in 2021. The strong forecast growth is mainly due to additional fiscal support by large economies and rapid vaccine rollout across country was driven mostly by additional fiscal support by large economies and rapid vaccine rollout.

Global growth is expected to slow to 4.4% in 2022, the advanced economy group is forecast to decline at 3.6%, while growth for the emerging market and developing economy group is forecast at 5.0%. However, the slowdown in 2022 is uncertain and depends on how fast the pandemic will fade. A lot of effort have been done in accommodating the public health requirements around the world to prevent the spread of the virus, nonetheless this policy limited the economic activity and the financial system which contributed to the negative growth in 2020. Nevertheless high levels of growth, especially in Asia, still provides a solid foundation

[1]Withdrawals from the Petroleum Fund in excess of the ESI.

for Timorese exporters and economic development. The international environment provides favourable conditions for Timor-Leste to take advantage of in 2020 and beyond.

3.1.2 Prices and Inflation

Table 4: Global and Regional Inflation Rates (%)

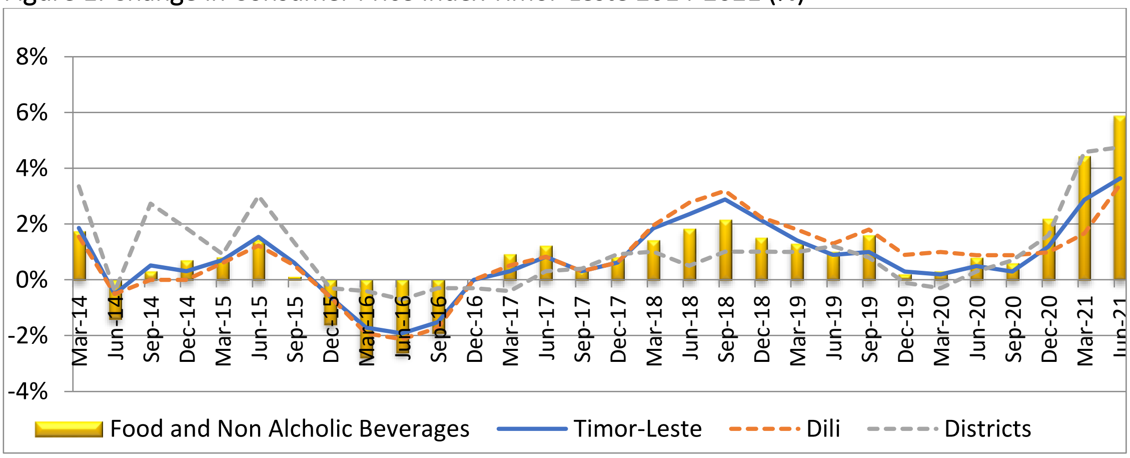
Country	Actual		Forecast	
	2019	2020	2021	2022
World	3.5%	3.2%	3.5%	3.2%
Advanced Economies	1.4%	0.7%	1.6%	1.7%
Emerging and Developing Economies	5.1%	5.1%	4.9%	4.4%
Emerging and Developing Asia	3.3%	3.1%	2.3%	2.7%
Timor-Leste*	0.9%	0.5%	2.3%	2.0%

*Source: IMF World Economic Outlook April 2021. *Ministry of Finance forecast.*

Timor-Leste

With year-on-year inflation in June 2021 of 3.6%, there has been an uptick in the momentum of inflation in Timor-Leste. Due to the significant weight of food and non-alcoholic beverages in the CPI basket and the high proportion of food imported into Timor-Leste every year, international food prices remain one of the key drivers of the overall CPI rate, and the MoF continues to monitor price levels. The World Bank (WB) food price index has increased a massive 39% between June 2020 and June 2021 whereas domestic food prices has seen a more modest increase of just 5.9% in the same time frame. This will have a negative effect on poorer households where basic foods make up the majority of their spending and this will leave them with less disposable income. However, it is expected that the current world food prices will start stabilizing in 2022 and remain flat until 2026. Rice specifically is a staple part of the Timorese diet. The benchmark (Thai 5%) decreased -10% in between June 2020 and June 2021, the price of rice is also expected to flatten in the short term- this is good news for families where rice is a large part of their diet. World coffee prices (both Arabica and Robusta) increased 36% between June 2020 and June 2021. This will positively affect those families who rely on coffee production in Timor-Leste.

Figure 1: Change in Consumer Price Index Timor-Leste 2014-2021 (%)



Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2021.

International

Global inflation forecast at 3.5% by the IMF in 2021. The rebound in the commodity prices especially increase in oil prices have contributed to the increase in consumer price inflation in 2021. In advanced economies, inflation is projected to soften in the coming years. For the emerging market economies, inflation has fallen reflecting the impact of currency appreciation making imports cheaper. Lower inflation in Timor-Leste than in the rest of Emerging and Developing Asia will help to improve competitiveness as Timor-Leste's exports are relatively cheaper.

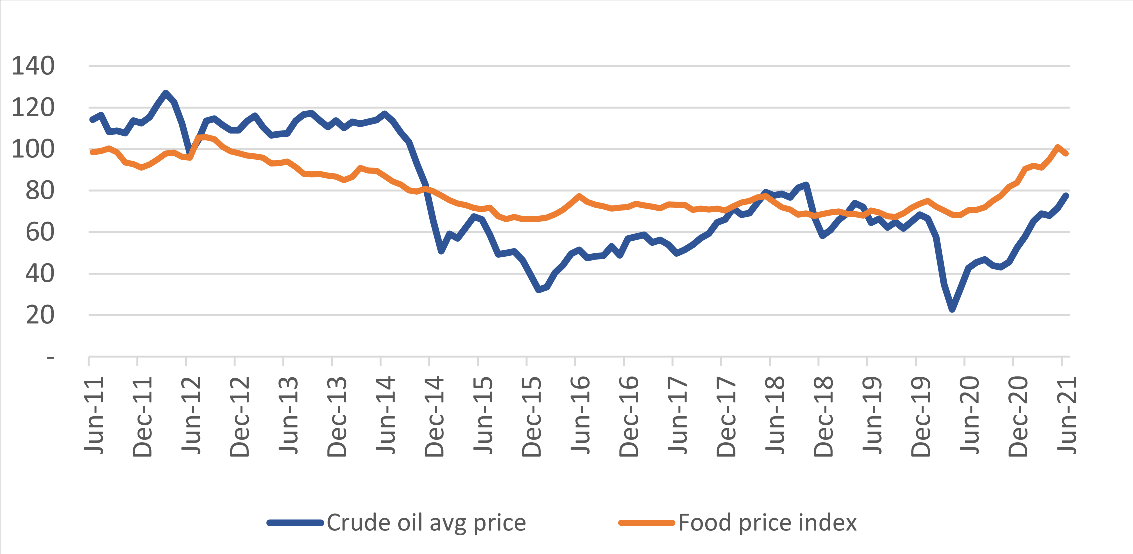
Oil prices

Oil prices are important to Timor-Leste both for consumers, through consumer prices, and as an oil exporting country. The average international price of crude oil has witnessed dramatic declines since June 2014 from highs of $112 per barrel to lows of $32.3 per barrel in January 2016. The decline in oil prices was driven by the increased global supply during a period of low global demand. The price of oil halved in the 1st quarter of 2020 year due to the fall in global demand during the height of the COVID-19 crisis, bottoming out at $21.04 per barrel in April 2020, but prices have recovered since, increasing to $71.80 per barrel in June 2021. The price of oil is now higher than it was before the start of the COVID-19 crisis in Dec 2019. This strengthening recovery has been driving by the tight demand-supply balanced this year and the production cut by OPEC+, including Russia and other non-OPEC oil exporters. The oil prices is projected to increase only moderately in the near future.

Agricultural Commodity Prices

A significant portion of the food consumed in Timor-Leste is imported and thus changes in international food prices can have a significant impact on both the rate of inflation and standard of living. According to the World Bank Commodities Price Index (2011=100), international food prices have continued to decline from a high of 105.8 in August 2012, though prices had been stable averaging at 73 and 70 in 2018 and 2019 respectively. However, international food prices have increased a huge amount recently with the World Bank (WB) food price index increasing 39% between June 2020 and June 2021. World rice price (Thai 5% benchmark) decreased 10% (YoY). Coffee Arabica Prices increased 36% (YoY). In Q2 2021, crude oil (Brent) rise dramatically 82% in June 2021 compared to the year before. Oil prices have now fully recovered and surpassed the prices prior to the COVID-19 crisis where the price of oil halved due to supressed global demand.

Figure 2: Commodity Price Indices 2011-2021



Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2021.

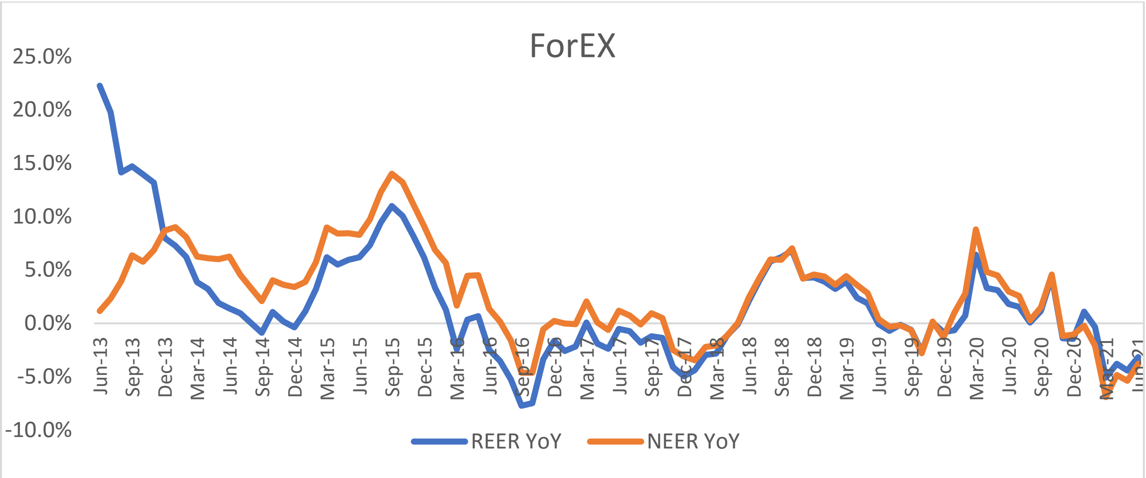
3.1.3 Exchange Rates and Competitiveness

Between June 2020 and June 2021 Timor-Leste's NEER depreciated by -3.8% while the REER depreciated -3.2%. Over this period the NEER also experience -11.1% decrease against a weighted Thai Baht and Vietnamese Dong Hong-Kong dollar basket whereas the REER depreciated by -1.1% against the same basket. This slight real depreciation places some upwards pressure on domestic rice prices and inflation (as Thailand and Vietnam export large quantities of rice to Timor-Leste).

An inflation-adjusted measure of the exchange rate, the real effective exchange rate (REER), is a better measure of competitiveness. If inflation in Timor-Leste is lower than in other countries, this can help mitigate exchange rate depreciation. The REER has depreciation by -3.2% between June 2020 and June 2021, driven by the exchange rate changes captured in the REER and lower inflation in Timor-Leste compared to its neighbours over the last year.

The inflation rate in Timor-Leste is expected to be lower than its neighbours in the near future, and so Timor-Leste can expect an improvement in competitiveness. This will help the Timorese export market be well-placed in the international market. While this is to be welcomed, the government is not complacent about the issue of competitiveness. A key priority is improving the business environment to encourage improved competitiveness, and the inflation target policy is a part of meeting the priority.

Figure 3: Exchange Rate Indices 2013-2021 (%)



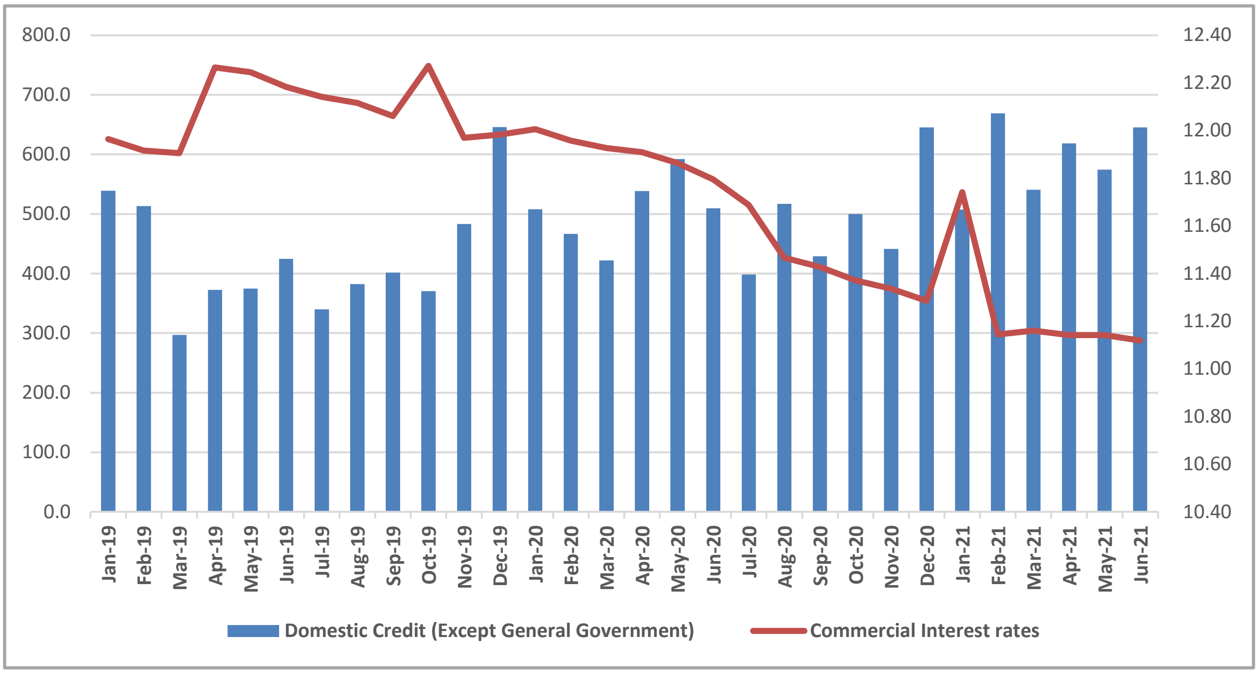
Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2021.

3.1.4 Financial Sector Trends

Commercial Interest Rates and Credit

The amount and cost of credit to the private sector is an important indicator for private sector development. Loans to the private sector were at an average interest rate of 11.12% in June 2021, these have declined over the last 18 months which is good for businesses who can borrow money to expand their business at a cheaper cost of financing. Total domestic credit, excluding general government, was $645 million in June 2021, with an average of $592, 4 million over the prior 6 months, this has also increased over the last 18 months. However, information from the Central Bank indicates that loans are increasingly being given to individuals rather than businesses.

Figure 4: Commercial Interest Rates and Credit



Source: Banco Central Timor-Leste, 2021. Interest Rate (RHS, %), Credit (LHS, $m).

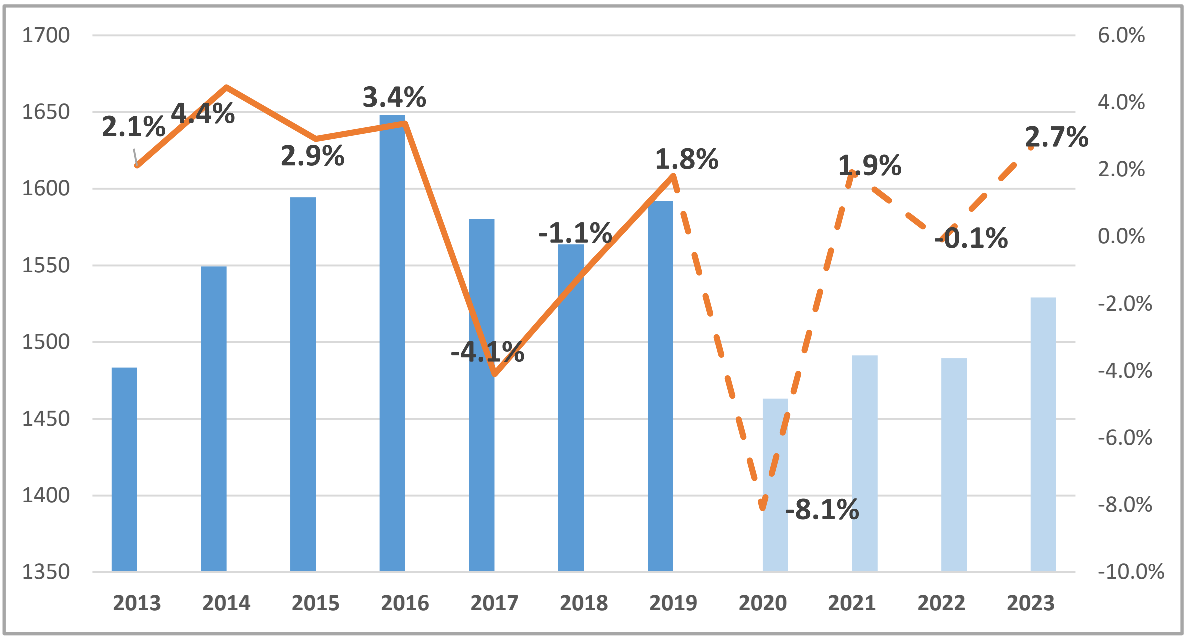
3.2 Economic Outlook

The Ministry of Finance is forecasting non-oil GDP growth to be 1.9% for 2021. Despite the large budget for 2021, this has been revised down from earlier forecasts due to the impact of discovery of Covid-19 community transmission and associated lockdown, recent floods and poor execution of government spending. An increasing inflationary environment due to the rebound in world oil prices may strain consumption to some extent, but the fall in the cost of rice and increase in the price of coffee should help poorer and rural households.

Public sector investment in 2020 was constrained by the duo-decimal system, political uncertainty and Covid-19. However, the new coalition should provide the political stability for the Budget to be approved for 2021 providing greater momentum for public infrastructure projects, especially in education, health, and water and sanitation. Despite the large budget for 2021, expected growth has been revised down to 1.9% due to Covid-19 confinement, the recent floods and poor execution of the large state budget by Q2 2021. The very low state budget execution for 2021 indicates that Timor-Leste does not have the absorptive capacity to spend such a large budget.

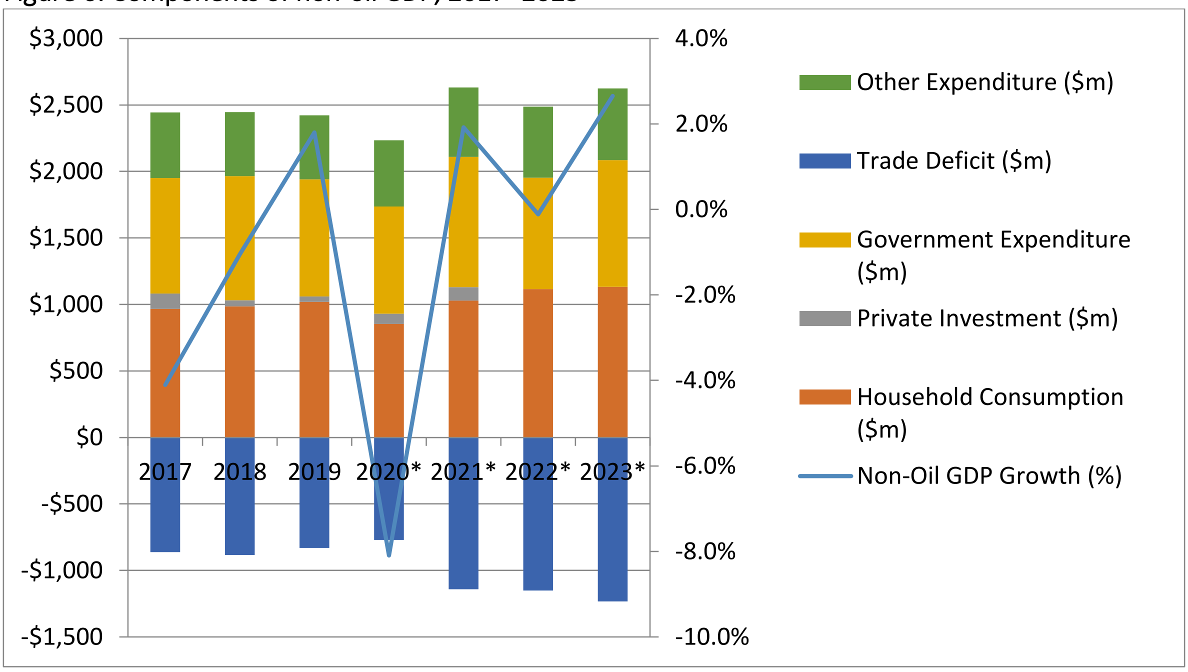
In 2022 we expect a small dip in GDP growth due to a reduction in the state budget compared to the previous year, as we move public finances onto a more sustainable footing in order to preserve the country’s Petroleum Fund which will benefit future generations and also be a positive signal to investors. Over the medium term, Ministry of Finance expects return to positive sustainable growth based on political stability and private sector investment. In the short and medium term one will see continued construction on the Tibar Bay Port, and the expansion of existing and new commercial projects throughout the country. Such investments are consistent with the Government’s economic strategy, alongside continued investments in human capital and education, to attract investors and consequently creating jobs domestically.

Figure 5: Real non-oil GDP growth rate (RHS, %) and levels (LHS, $m)



Source: Timor-Leste National Accounts 2000-2019, General Directorate of Statistics; 2020-2023 Economic Forecasts, National Directorate of Economic Policy, Ministry of Finance, August 2021.

Figure 6: Components of non-oil GDP, 2017- 2023



Source: Timor-Leste National Accounts 2000-2019, General Directorate of Statistics; 2020-2023 Economic Forecasts, National Directorate of Economic Policy, Ministry of Finance, 2021.

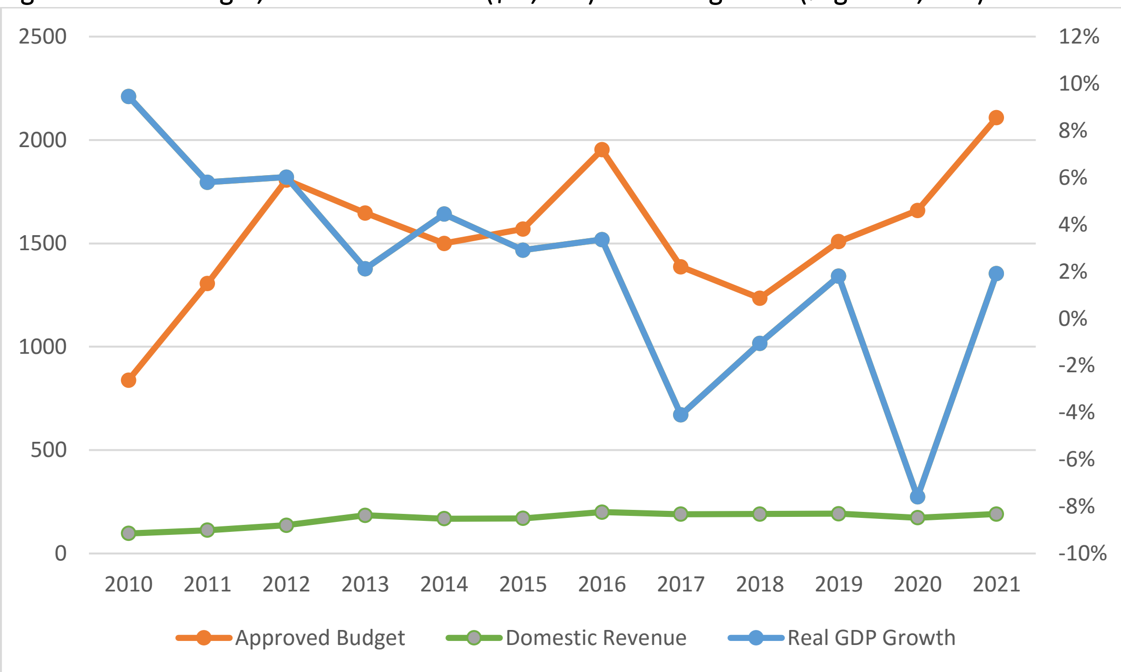
Risks and Uncertainty

Economic forecasts or projections aim to predict annual GDP growth rates and high level macroeconomic figures. Making forecasts about what macroeconomic variables may be in the future is important to help governments and businesses make decisions with regard to policies, planning and investment. However, it is important to understand that in order to make these predictions we have to make some assumptions about future conditions. Therefore all projections always include an element of uncertainty. The main uncertainties in the forecast come from imports and government budget execution. If government spending is particularly import-dependent, meaning that much of the new spending goes to goods and services from outside Timor-Leste, the GDP forecasts for future years may be reduced downwards as imports have a negative effect on final GDP.

In addition, if there is a large change in execution rates this may have a noticeable impact on the economy, especially given that the state budget makes up a large portion of Timor's GDP. Execution rates differ each year for different reasons and also depend on the absorptive capacity of the Timor-Leste economy. Absorptive capacity means how much money line ministries are actually able to spend despite how much money they have. For example even if the budget was increased a large amount, line ministries may find it impossible to spend all of that money. As with all forecasting, the more time and accurate data one has, the less assumptions we have to make and the closer we move to the true value.

3.3 Government Expenditure, Domestic Revenues and GDP Growth

Figure 7: State budget, domestic revenue ($m, LHS) and GDP growth (% growth, RHS) 2010-2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Over the last 11 years there has been no clear relationship between real GDP growth, levels of domestic revenues and the state budget. To ensure government expenditure contributes to economic growth, allocation of state budget supporting sectors that have high potential contribution to economic growth is essential.

A cut in government spending may not necessarily have a proportionally negative effect on GDP growth rate as long as government spending focuses on sector promoting private sector investment such as basic infrastructure and investment in human capital in order to create job opportunities and reduce the poverty rate.

In addition, larger budgets have not necessarily lead to higher economic growth as line ministries may not be able to spend all the money and this leads to a lower execution rate. This is known as the government's absorptive capacity i.e. how much money it is actually able to spend.
Government revenue may affect the economy through changes in tax policy to influence investment decisions, consumption, savings and employment. Like government spending priorities, in order to contribute to economic growth, government tax reform should promote private sector investment decision, job creation and help diversify the economy. In Timor-Leste, government revenue has been low; and at this stage it needs improve tax collection to sustain the state budget.

Other key factors that influence GDP growth, separate to the total government expenditure ceiling:

- **Political stability**; Political stability encourages private sector, foreign direct investment and facilitates development projects. In Timor-Leste, recent political instability, delays to the budget being approved and subsequent duo-decimal regimes in 2017, 2018 and 2020 contributed to the negative growth in those years.

- **Private sector activity**; Private sector plays an important role in poverty reduction, promoting economic development and diversifying the economy away from oil dependency. To achieve this the government will need to provide better business environment especially in productive sectors such as agriculture, tourism and other transformative industries. Improving the business environment means improving laws and regulation to reduce bureaucracy and streamline business as well as improving the workforce's overall skills and health. High private sector investment can provide jobs and reduce the poverty rate.

- **Composition and allocation of budget**; Fiscal policy is crucial to boost economic growth. The *type* of government spending influences economic growth when the share of budget allocation is higher in productive sectors. Investment in crucial infrastructure such as roads, machinery, research and development may encourage private sector to invest. Social capital investment i.e. health and education spending may not have an instant impact on GDP but are crucial for the medium and long term growth and prospects of the country.

- **Development partner spending;** Development partner spending will contribute to economic growth. To support long term growth, aid tends to be more effective in supporting institutional strengthening, health and education. Aid is also effective in short term growth in sectors like infrastructure, agriculture and industry.

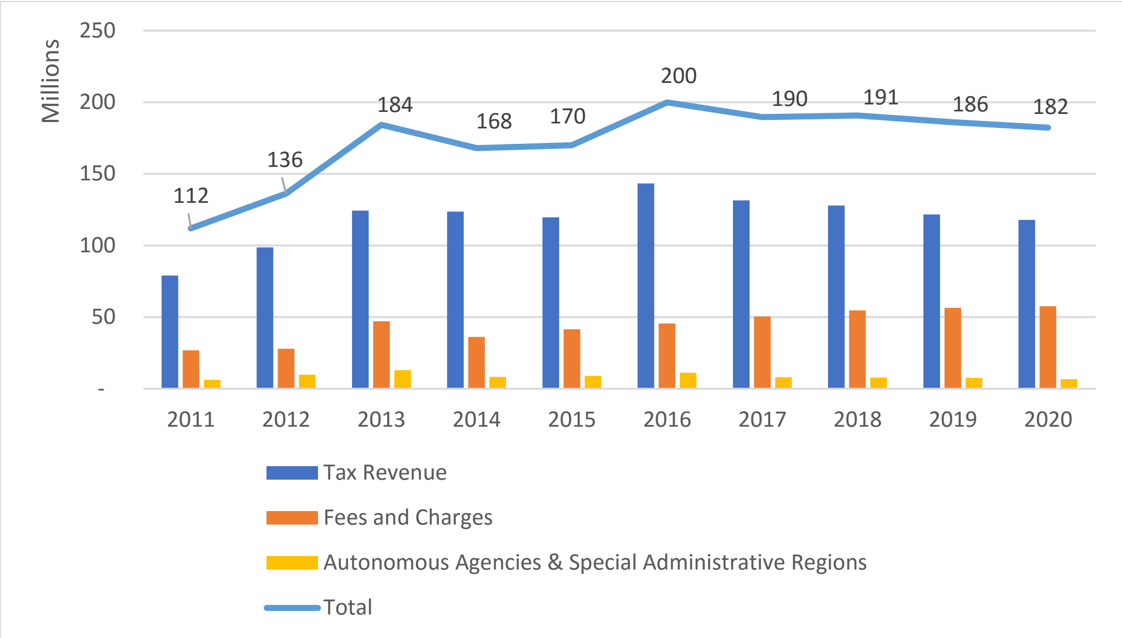
- **Household consumption**; When employment rate is higher, households tend to spend more as many people tend to have higher disposable income to spend on non-essential non-food items, this has a multiplier effect in the economy.

3.4 Domestic Revenue

3.4.1 Historical Trends

Over the past 10 years, domestic revenues have not followed a consistent growth pattern. During the period from 2010 to 2014, revenues increased at an average rate of 24% per year. They then saw a decline in 2014, followed by another rise to a peak in 2016 of $199.7 million. The political instability of 2017 caused a subsequent fall in overall revenues, largely due to a fall in tax receipts. This decline continued into 2018 and 2019 as tax receipts and total revenues continued to fall. In 2020, domestic revenues fell to their lowest total since 2015. However revenues in 2020 ended the year only 2% lower than those collected in 2019. Given the COVID-19 crisis and related global economic downturn, this decline was lower than forecast.

Figure 8: Domestic Revenues, 2010-2020

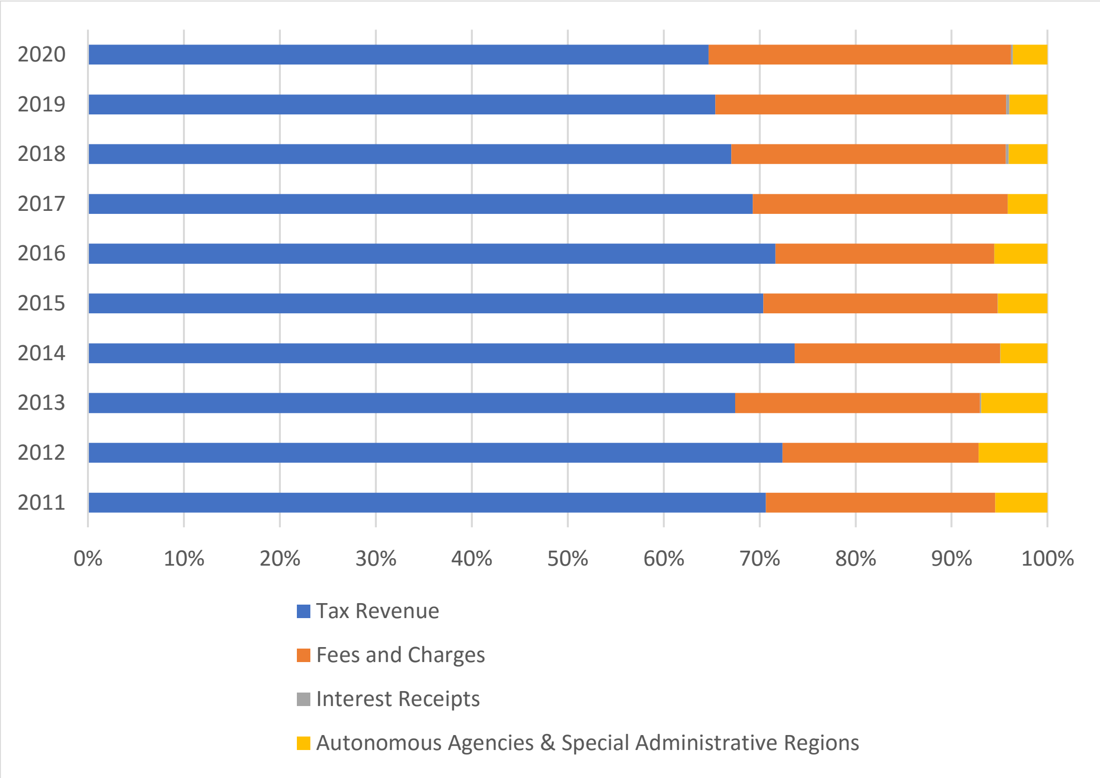


Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Comparing the composition of different year's revenues, it is clear that taxes are consistently the largest contributor, making up nearly 2/3 of the total revenue collection (an average of 69% of the total across the last 10 years). This is in comparison to 26% for Fees and Charges and 5% for Autonomous Agencies & Special Administrative Regions. The composition of revenue i.e. the proportions that come from tax, fees or AAs tend to be consistent over time even if some years overall revenue is different. However the past 4 years have seen a fall in the total percentage contributed to tax, alongside a fall in overall collections. 2020 was the lowest year in the past 10 years for tax contribution to total revenues, making up 65%. This was compensated by a rise in Fees and Charges to 32% and Autonomous Agencies making up the final 4%. While interest receipts have been increasing over recent years, they still make up less than 1% of overall collections.

It is important to note that the totals for 2019 and 2020 not include ZEESM revenue collections as those figures have not yet been made available. Therefore to allow a fair comparison, none of the sections will include either ZEEM taxes or fees and charges in their analysis.

Figure 9: Domestic Revenue Composition, 2011-2020

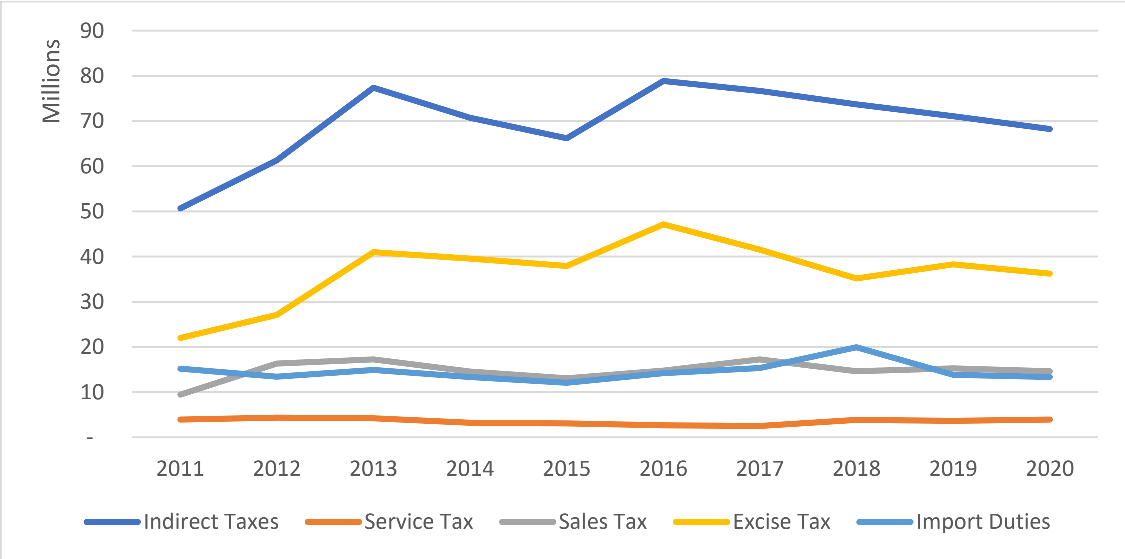


Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Focusing in on tax revenues in more detail; like total domestic revenues, after a rise at the start of the period, the past few years have seen significant fluctuations with 2020 seeing a continued fall in total tax receipts to \$117.8 million from a total on \$122.3 million the previous year, excluding ZEEMS taxes.

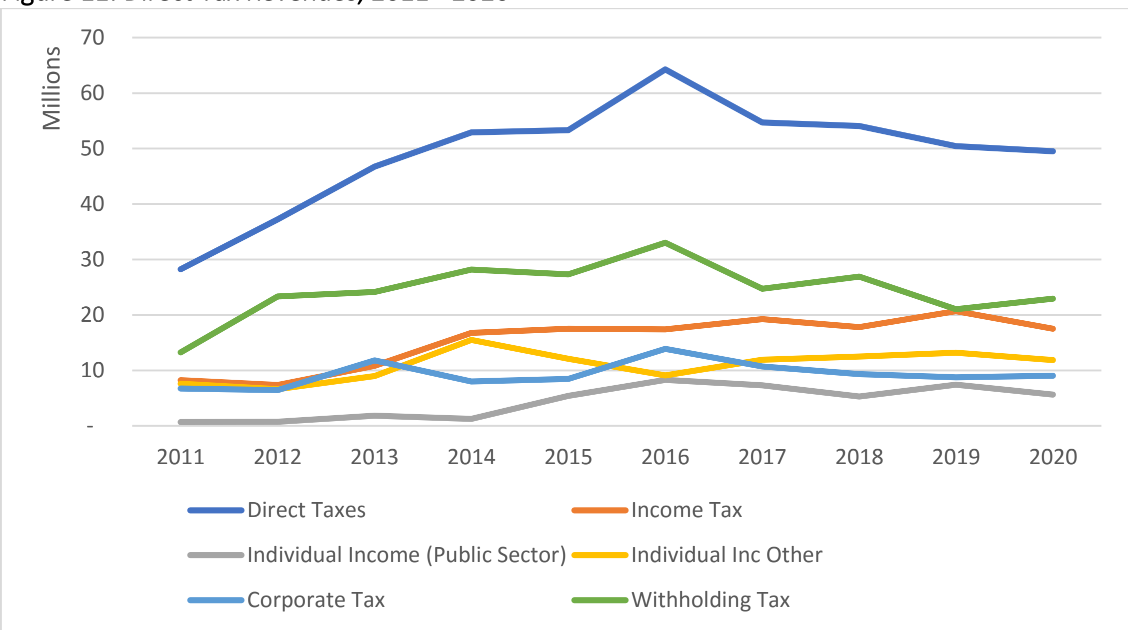
Taxes in 2020 started the year higher than those in 2019 but saw a significant flattening during Q2 and continued to remain lower. The biggest year on year fall was seen by income taxes which fell 24% for the public sector and 10% for the private. Excise and sales taxes and import duties were also all lower than the previous year. Withholding taxes in fact rose 9%, largely due to high collections during Q1 as a spill over from projects at the end of 2019. Corporate and sales taxes also saw rises. Excise taxes continued to be the largest contributor, making up 31% of total tax revenues. Withholding taxes, making up 19%, and sales tax, making up 12%, remained the second and third highest taxes. Indirect taxes continue to exceed direct taxes in 2020, as they have for the past 10 years

Figure 10: Indirect Tax Revenues, 2011 - 2020



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Figure 11: Direct Tax Revenues, 2011 - 2020

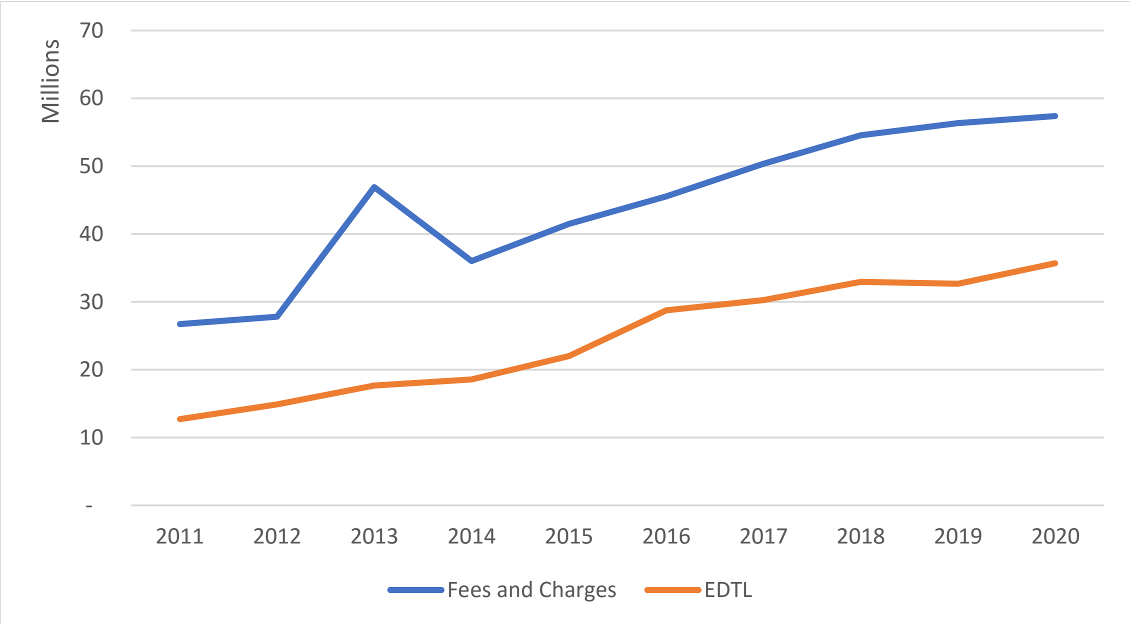


Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Looking at Fees and Charges, they have seen consistent growth over the past 6 years. 2013 was a significantly high year due to an exceptionally large contribution of other non-tax revenues which grew from just below $1 million in 2012 to over $15 million in 2013 and fell back to $4.7 million in 2014. Excluding 2013 from the trend line, due to its exceptionally high levels, revenues from Fees and Charges have grown since 2011. This continued in 2020, increasing to $57 million in 2020 compared to $56 million the previous year. However the rate of growth was slower than in previous years, as seen by the graph below.

Revenues from EDTL (electricity fees and new installation costs) still dominated the total, comprising just over 62% of the total fees and charges revenue from fees and charges. The move to make EDTL a public enterprise will allow it greater autonomy and the ability to take its own decisions regarding policy decisions including future planning. However it also mean that they get greater control of their revenues which will become independent of Central Government, kept in their own private account and no longer part of the General Government Account, causing a significant fall in domestic revenues.

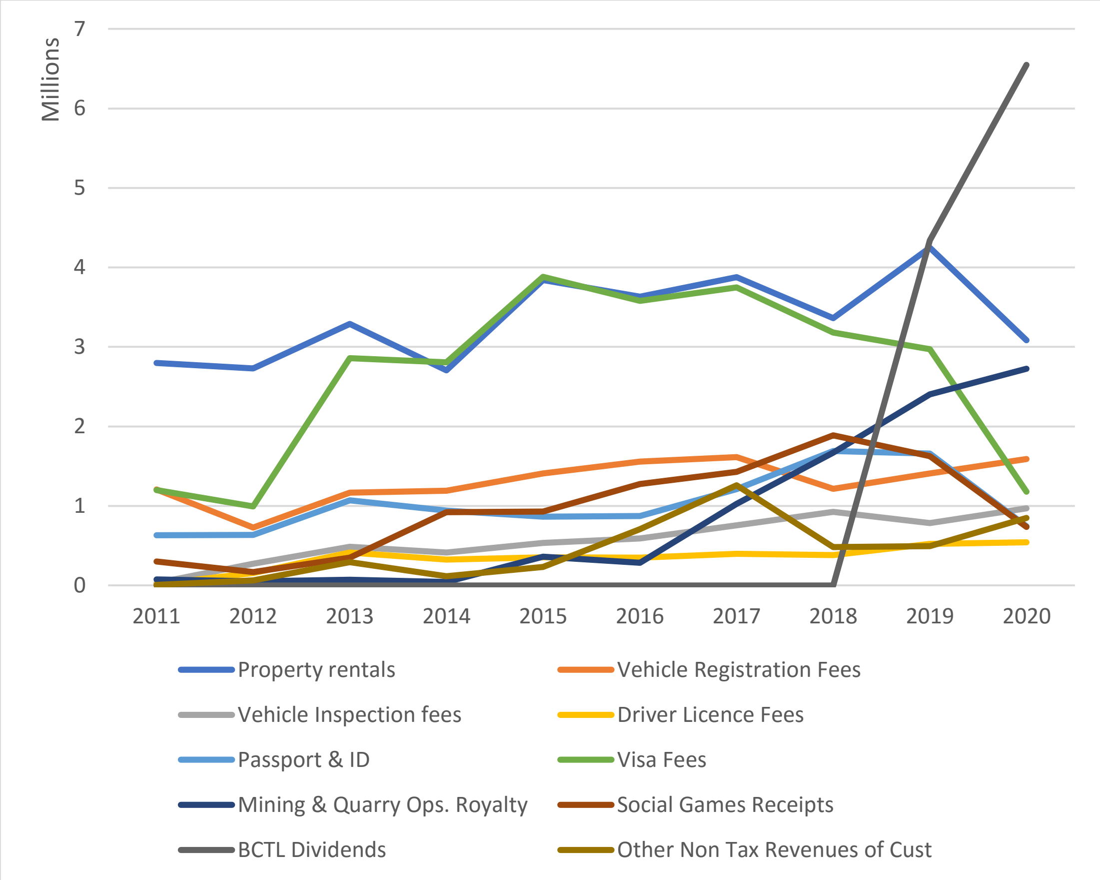
Figure 12: Electricity contributions and total Fees and Charges, 2011-2020



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Regarding the other top contributors, many of them have collected similar amounts for the past 10 years. The key exception is the addition of BCTL Dividends which only saw collections begin in 2019. Last year, it was the second highest fees and charges collection, behind EDTL fees and charges. Mining and quarry royalties have been growing year on year from 2016 while visa fees, usually one of the largest contributors fell dramatically in 2020 largely due to the rapid decline in new arrivals to the country given the COVID-19 pandemic and State of Emergency restrictions.

Figure 13: Top Contributors to Fees and Charges Revenues excluding Electricity, 2011-2020



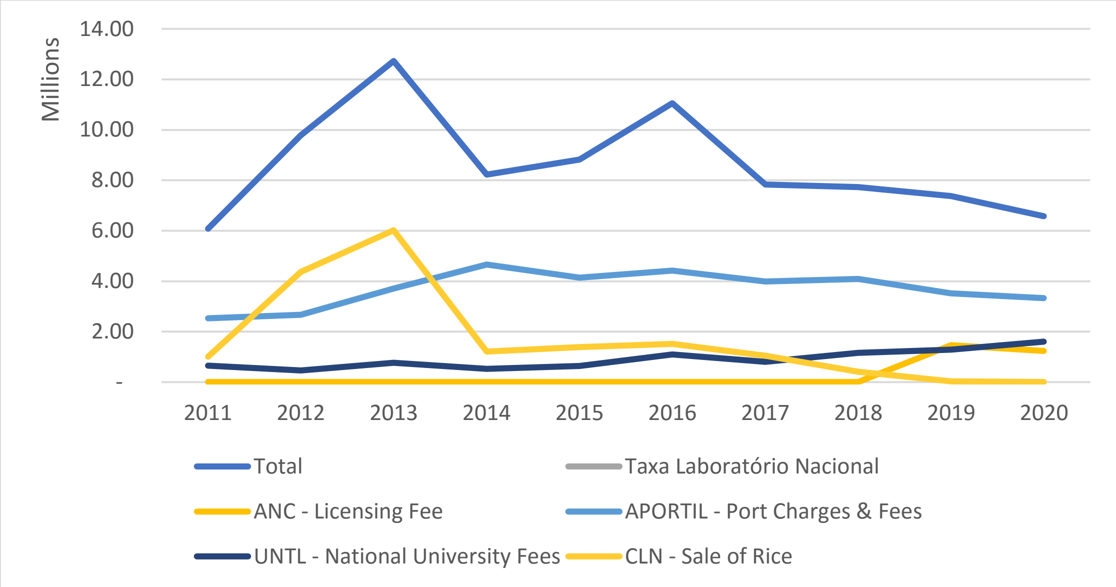
Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Autonomous Agencies do not seem to follow any historic trend. However the large spikes in 2013 and 2016 do coincide with rises in the overall revenue collection. The Autonomous Agencies total for 2019 was -11% lower than those in 2019. APORTIL has consistently been the largest contributor to the total, contributing over 50% in 2020 and averaging around 40%.

2020 saw the introduction of a new revenue stream from the National Laboratory relating to charges for COVID-19 and other testing conducted there. A number of Autonomous Agencies failed to report any collections in 2020, despite doing so in previous years. These include Hospital Nacional Guido Valadares, SERVE IP, and Centre of National Logistics (specifically from the sale of rice).

As mentioned before, Special Administrative Regions are not included in this analysis, unlike previous years, due to the delay in data collection.

Figure 14: Autonomous Agencies Revenues including top contributors, 2011-2020



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

3.4.2 Mid-Year Analysis

From the start of 2021, Electricidade de Timor-Leste E.P. (EDTL) and BEE Timor-Leste E.P. became Public Enterprises. This means that while they remain in the public sector, as they are held within the institution, their revenues are no longer counted in in the Treasury account as they are not included as part of the General Government. Public Enterprises are the most autonomous of all public entities.

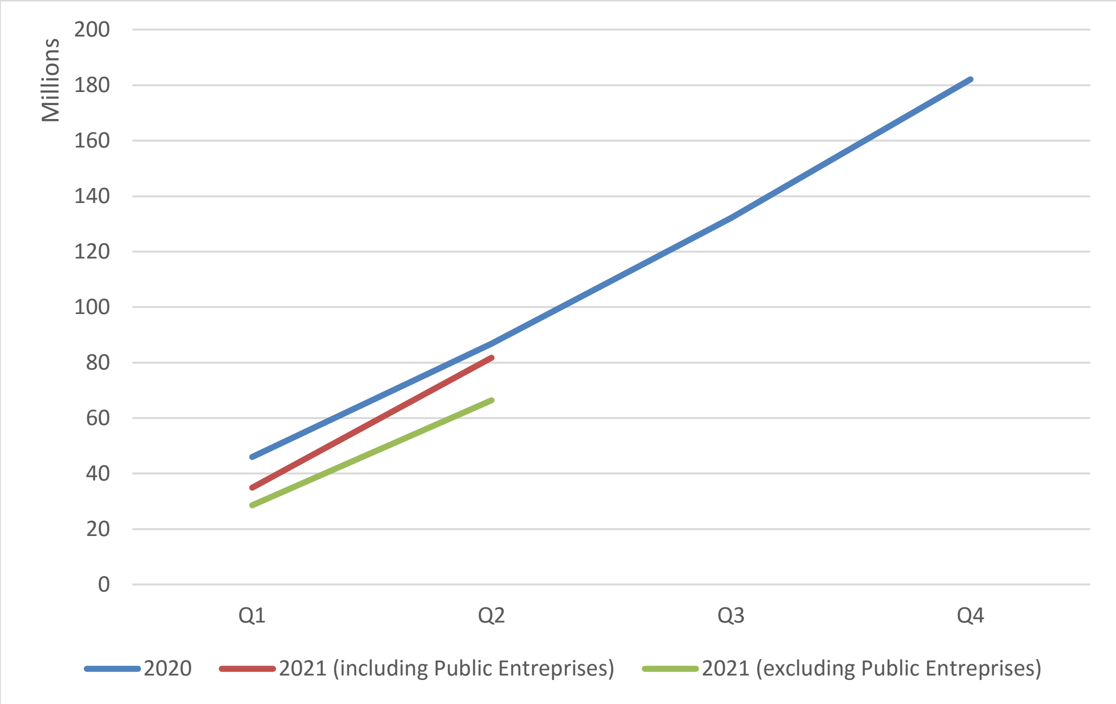
In the context of this report, Public Enterprises will refer to the line items that were part of the Treasury account in 2020 but are now included under a Public Enterprise. These are Water Fees, Electricity Fees & Charges and EDTL Receipts from New Installations.

Domestic revenues saw a slow start to collections in 2021, with collections 24% lower than those the year before. However this is excluding those entities that are now Public Enterprises. To allow a direct comparison between quarters, it is important to include them back into the total, though it is important to note that their revenues are no longer included. However even comparing like for like, domestic revenues fell 10.3% in Q1 between 2020 and 2021. It is important to note that Q1 2020 was particularly high, due to a number of delayed payments of some key taxes at the end of 2019, especially withholding taxes.

Collections saw some recovery in Q2. However they are still below the same time last year, even when factoring in the public enterprise collections. The impact of COVID-19, especially the periods of mandatory confinement and sanitary fences, are a key factor in this.

At the end of Q1, domestic revenues were $17.5 million lower than those in 2020. By the end of Q2, that had increased to $20.4 million.

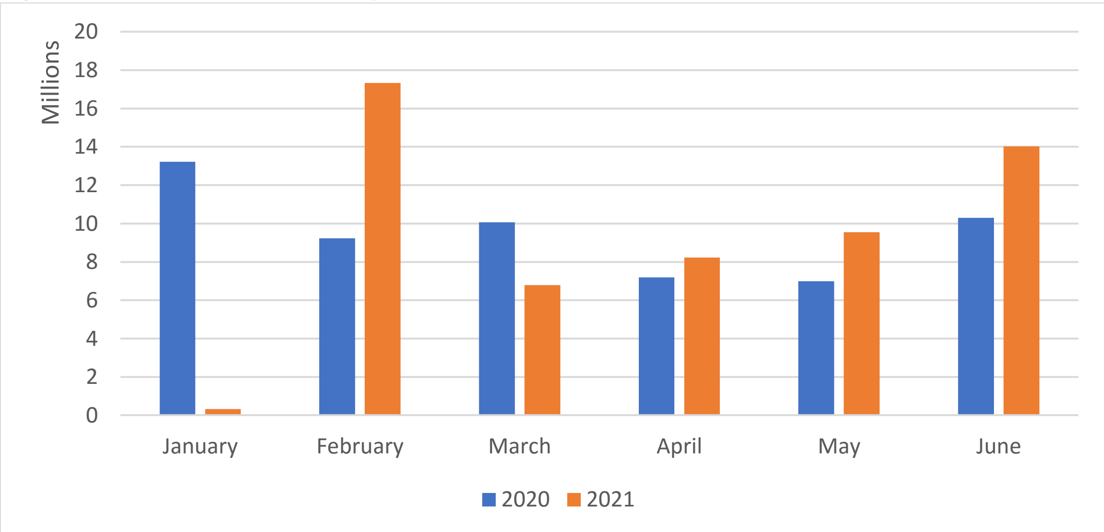
Figure 15: Cumulative Domestic Revenue Totals 2020 and 2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Due to a delay in revenue collections in January, tax revenues appeared to see a rapid increase in February. However overall tax revenues declined 24.8% between Q1 2020 and 2021 and fell 24.7% between Q1 2021 and the previous quarter (Q4 2020). However they saw a significant rise in Q2, increasing 30.1% on the previous quarter and 29.9% on the same period last year.

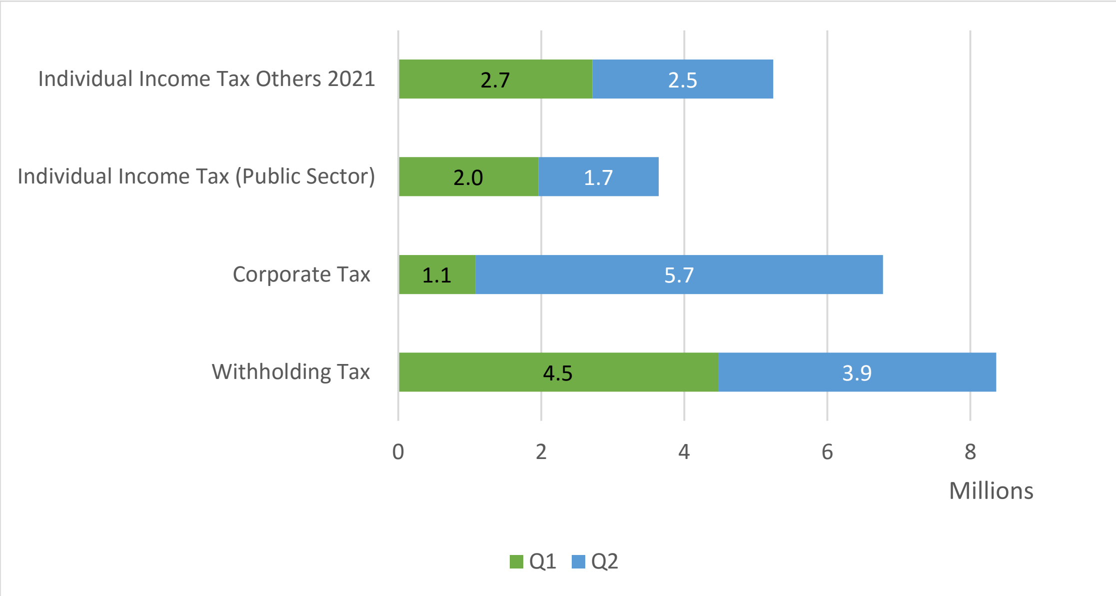
Figure 16: Tax Revenues, January - June 2020 and 2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2020.

Focusing on direct taxes only, Corporate Tax saw a fall in comparison with the same period the previous year. Despite a large rise in Q2, and increasing over 400%, it was still nearly $400 million lower than at same point last year. This is likely due to the longer period of mandatory confinement in Dili in 2021. Withholding Tax, commonly linked to the level of capital spending, is down nearly $4 million on the same time last year. This suggests a substantial reduction in the construction sector during the first half of 2021. On the other hand, Public Sector and Private Sector income taxes are slightly exceeding their aggregate spending compared to 2020.

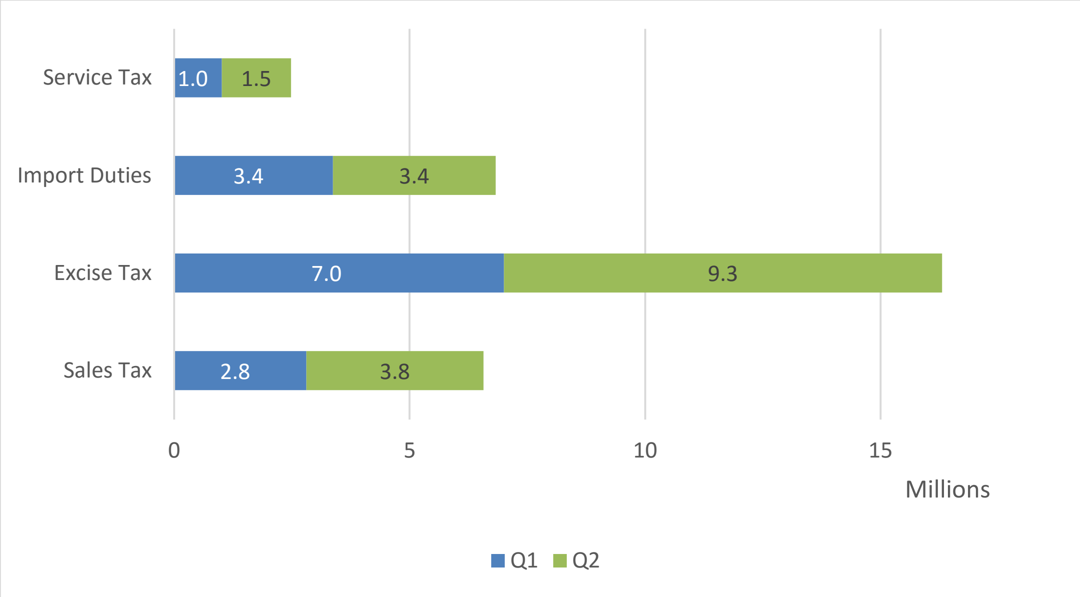
Figure 17: Direct Taxes, Q1 and Q2 2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Indirect taxes also fell in Q1, though not to the same degree as direct, with most taxes seeing a similar amount of collections by the end of the quarter. All 4 taxes saw a rise in Q2, particularly Sales and Excise taxes which had had the largest fall in the previous quarter. Indirect taxes are often used as proxy for household consumption, therefore this increase shows promising signs for the overall condition of the Timorese economy. Emphasising this, all indirect taxes are exceeding their collections at the same point last year.

Figure 18: Indirect Taxes, Q1 and Q2 2021



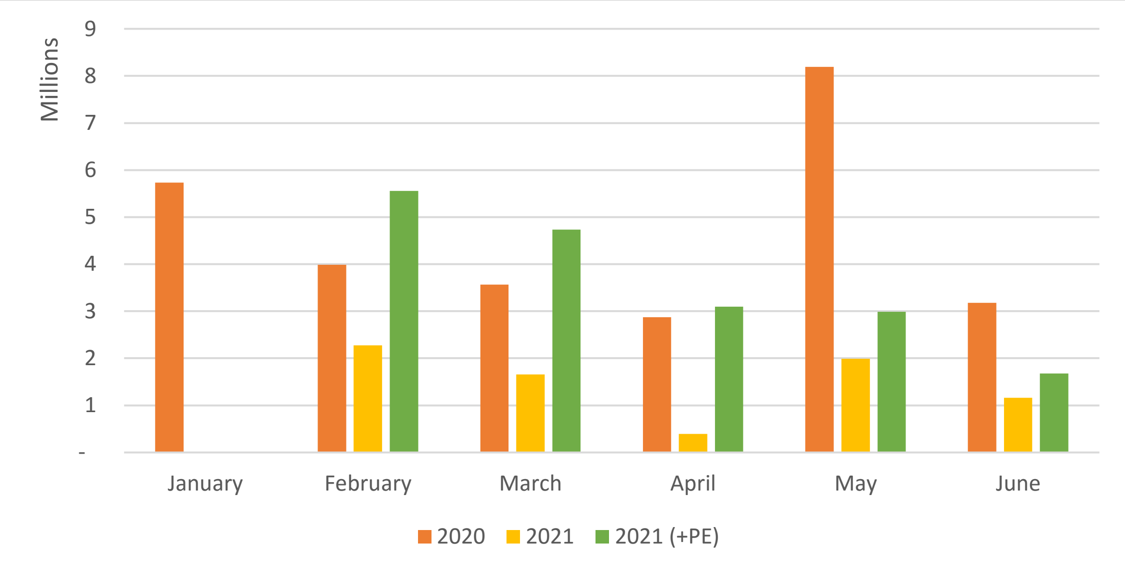
Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Revenues from fees and charges have seen a dramatic fall compared to 2020. By the end of Q2, collections were just one quarter of those in 2020 (27%). It is important to note that, as mentioned before, this does not include collections for EDLT and Bee TL in the 2021 amounts due to them becoming public enterprises at the start of 2021. However when comparing like for like, with both amounts including all line items, Fees and Charges still see a significant fall, with collections still only two-thirds of the previous year (66%).

While Mining and Quarry Operations Royalties saw a dramatic rise in Q1, nearly tripling year on year, this was not maintained to Q2 with a decline of 95% between the quarters. Passport and ID collections and visa fees saw the large falls. This is unsurprising given the continuation of the State of Emergency ensuring the validity of all visas, thus reducing the need for extensions, as well as the significant reduction of international travel given the COVID-19 pandemic and associated closure of most commercial flights. BCTL Dividends saw a significant collection of $1,541,100. However this is large decline on the same line item last year, when revenues were over $5 million higher at $6,549,832.

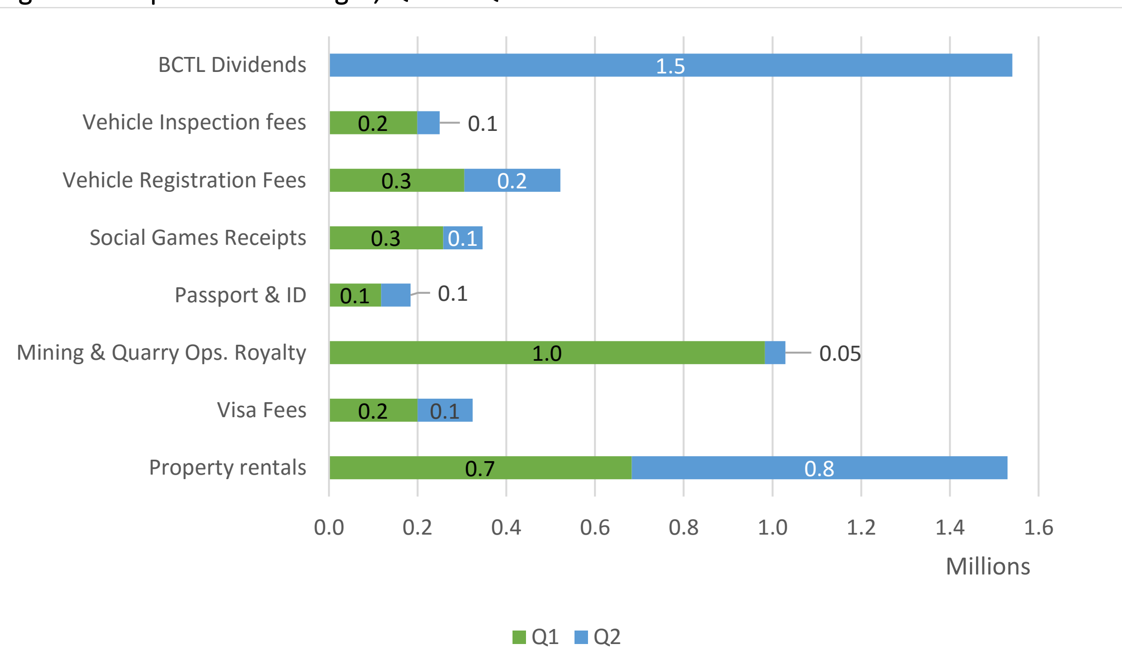
Collections from the line items that are now Public Enterprises and no longer included in the Treasury account are also down on the previous year. This suggests that the mandatory confinement in Dili may have led to the temporary closure of a number of businesses, therefore reducing their demand for electricity, as people were recommended to stay at home. Revenues from all of the Public Enterprise line items are below the amount they had collected by the end of Q2 last year.

Figure 19: Fees and Charges Revenues, January - June 2020 and 2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

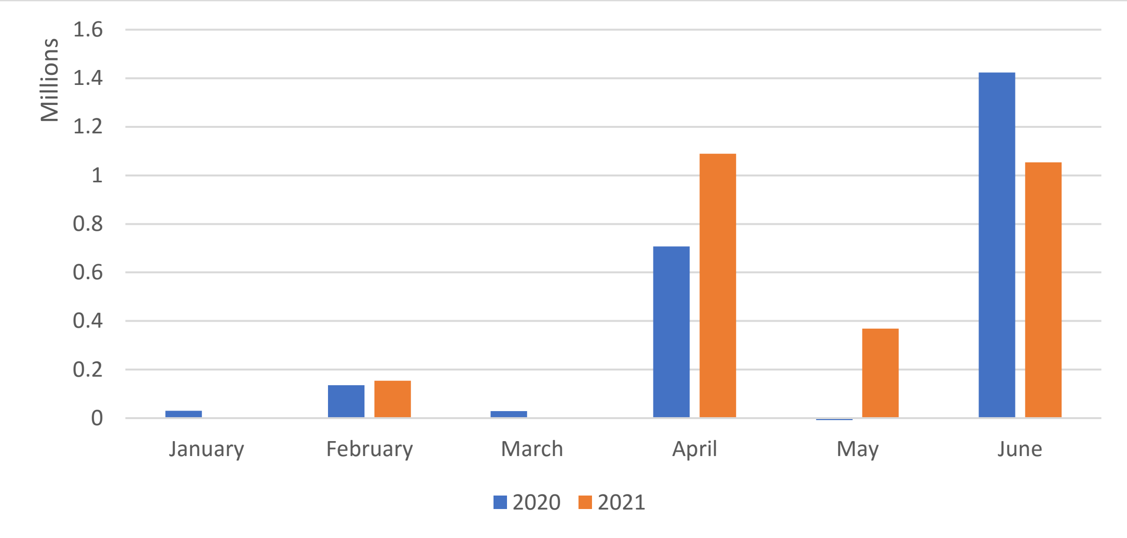
Figure 20: Top Fees and Charges, Q1 and Q2 2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

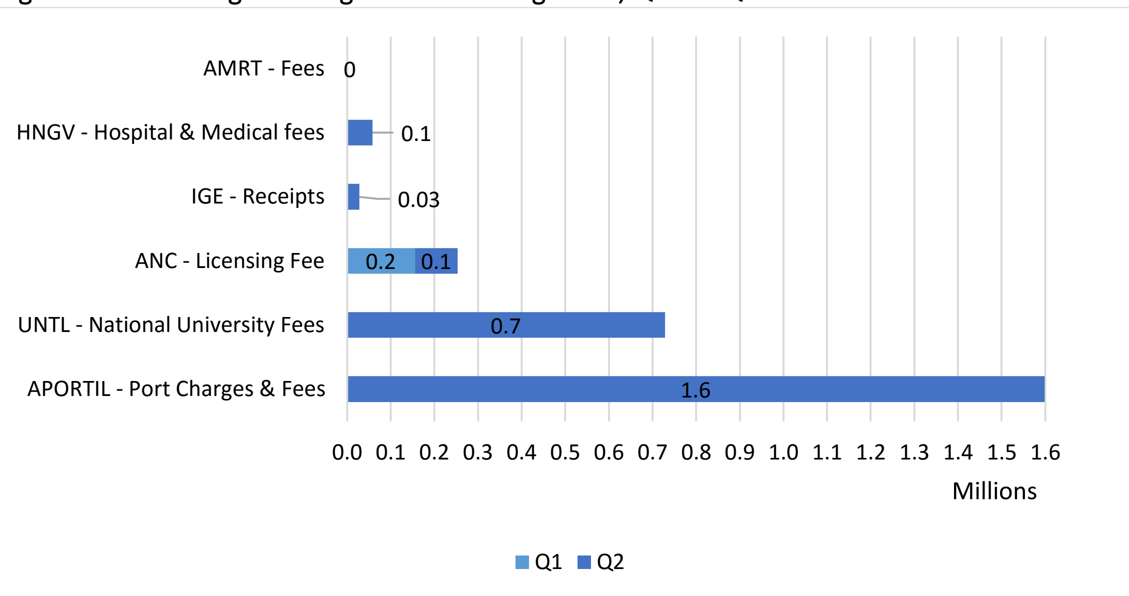
Autonomous Agencies have a cumulative collection that are 18.2% higher than the same point in 2020. This is largely due to a larger number of autonomous agencies reporting in 2021 in comparison to 2020 (6 AA instead of 4 AA). By the end of Q1, only two Autonomous Agencies (Autoridade Nacional de Comunicações (ANC) and Arquivo & Museu da Resistência Timorense (AMRT)) had reported revenues in Q1 2020 but this increased considerably in Q2. IGE (Instituto de Gestão de Equipamentos), HNGV (Hospital Nacional Guido Valadares) and AMRT (Archives & Museum of East Timorese Resistance) all reported revenues by the end of Q2 of this year, but none by the same point the year before. APORTIL is the autonomous agency with the highest collections so far in 2021, with revenues 26.0% higher than the same point in 2021. UNTL, the second highest revenue generator, had collections 11.4% lower than those at the same time last year.

Figure 21: Autonomous Agencies Revenues, January - June 2020 and 2021



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

Figure 22: Revenue generating Autonomous Agencies, Q1 and Q2 2021



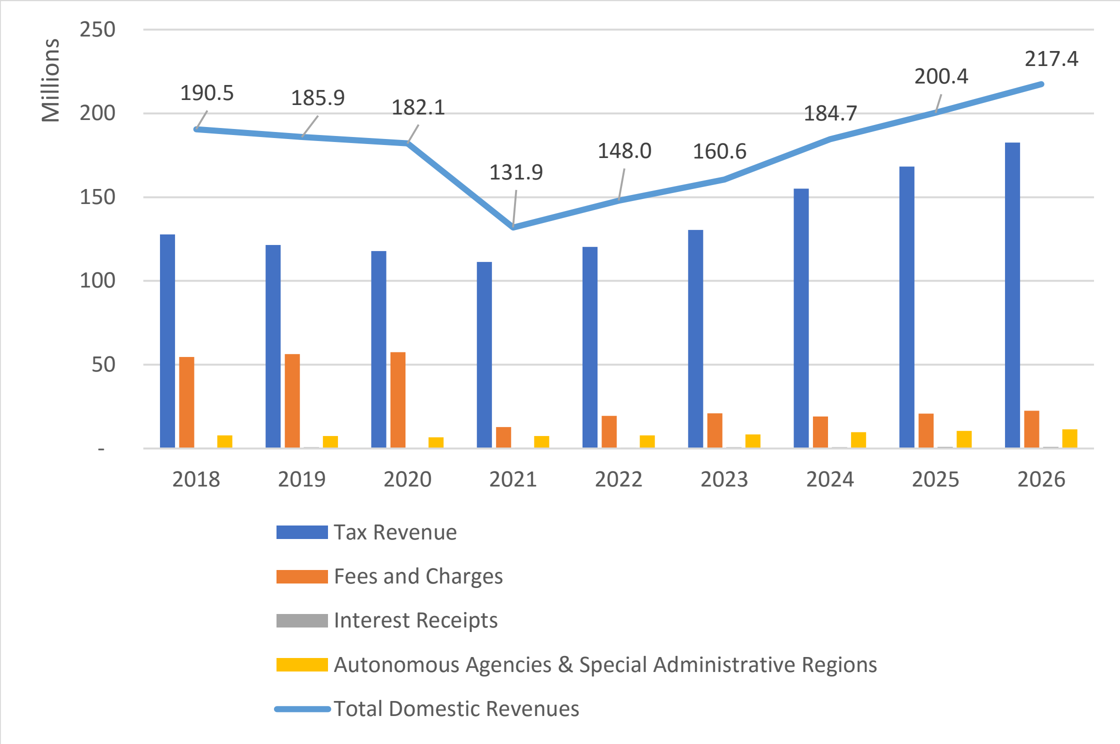
Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

3.4.3 Revenue Projections

Forecasts for 2021 see a significant fall in domestic revenue collections. This is mainly due to the exclusion of EDTL and BEE TL line items from Fees and Charges collections. However the economic downturn associated with the continuation of the COVID-19 global pandemic has also put a downward pressure on tax revenues, particularly Excise, Sales and Withholding. The decline in Infrastructure Fund spending as part of the rectified 2021 budget will also impact

Withholding tax collections due to its link to capital spending. Autonomous Agencies are expected to end the year slightly higher than 2020 due to more agencies reporting collections than the previous year. Due to this rapid decline, and due to the structural changes in revenue collections, domestic revenues are forecast to continue to remain below 'normal' levels (the amount collected in 2019) until 2025.

Figure 23: Domestic Revenue Forecasts (excluding ZEEMS), 2020-2025



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

However future years are expected to see a rise in revenues, driven by a stable macroeconomic and political environment and an expected economic bounce back from the GDP decline of 2020. Tax revenues are expected to be boosted by reforms in the tax collection systems, in particular the shift to SIGTAS (Standard Integrated Government Tax Administration System) 3.0, which aims to increase the Tax Authority's capacity to enforce greater tax compliance. The above forecasts also assumes the enactment of the new VAT law. The law was originally drafted in 2017, but it was delayed in parliament given the political uncertainty. In December 2020, the Ministry of Finance through the Tax Authority started to revisit the draft VAT law and have plans to seek the opinion, comments and feedback from a third party on the draft law prior to submission and presentation to Council of Minister and National Parliament by the end of this year. The boost to tax revenues is expected to occur in 2024 due to a delay in implementation to allow for the necessary infrastructure, training and tax payer education, to be put in place.

The move to increased decentralization of government activity has also seen the introduction of a number of new revenue streams through local advertising and parking services. Further decentralization, improvements and reinforcement of collection mechanisms in line ministries and the introduction of new non-tax instruments are expected to boost collections of Fees and Charges. Autonomous Agency collections, while they have no planned policy changes or reforms, are expected to rise with the improved economic conditions.

3.5 Petroleum Fund Revenue

Withdrawals from the Petroleum Fund remain the main source of funding for the state budget. The Fund's revenue consists of petroleum revenue and investment income. The Petroleum Fund projections are updated once a year as part of the final Budget process. The projections used in this Pre-Budget Statement are the same as the 2021 Budget Book and will be revised in the final 2022 Budget.

For 2021, Petroleum Revenue was estimated at $68.1m. As of May 2021, receipts from the sale of oil and gas amounted to $104.7m. Actual receipts are 54% higher than the projection used in the Budget 2021 and have been pushed higher by oil prices. As of May 2021, the Fund's investment return is 3.47%, which translates to $633.8m. The 2021 ESI remains at $547.9m as in the 2021 Budget and the proposed total withdrawal for 2021 remains at $1,377.6m ($1.4 bn). Up until May 2021, transfers to the State Budget amounted to $350m and the balance of the Petroleum Fund is $19.4bn.

The petroleum revenue is currently from one major project, the Bayu-Undan (BU) field, a mature field with a declining production profile. The field is expected to continue to generate revenues to Timor-Leste at least until its current PSCs expire in 2021/22.

The *Autoridade Nacional do Petróleo e Minerais* (ANPM) approved Phase 3C infill drilling program at the BU field as proposed by Santos, the Operator of the Bayu-Undan Joint Venture. The Phase 3C involves drillings of 3 production wells. The first drilling commenced in May 2021 and production is expected by Q3 2021. The drillings are expected to add over 20 million barrels of oil equivalent gross reserves and to extend the life of the Bayu-Undan.[2] However, production beyond 2022 will depend on contract negotiations and whether the remaining reserve is economically profitable. Potential revenues from other exploration licences will be included in the estimate of the present value of the petroleum revenues when they are declared proven and approved for development.

The petroleum revenue is mainly driven by three major factors: the oil price, production and costs. The projections in the State Budget 2021 were based on the EIA's projected Brent price in September 2020. The production and costs information were provided by the Operator in July 2020 for both Budget 2020 and 2021. The new information will be available in August 2021 and will be incorporated in calculating the ESI for Budget 2022 and projecting future revenues.

The Brent oil price had been averaging about $60/barrel since it declined in mid-2014. In March and April 2020, oil prices fell sharply with the onset of the Covid-19 pandemic and excess supply. Oil recovered from its lows although global demand was lower as a result of reduced economic activity. The Brent oil price averaged $42/b in 2020. The actual production in 2020 was 35.6m barrel of oil equivalent, which is 27 per cent higher than estimated in Budget 2020.

The higher than estimated production pushed the actual total petroleum revenue collected in 2020 to $326.2m, 7 per cent higher than estimated.

[2] https://www.santos.com/news/bayu-undan-infill-development-fid/

Table 5: Petroleum Fund Revenues 2020-2021 ($m)

	2020 Budget	2020 Actual	2021 Budget	YTD May-2021 Actual
Total Petroleum Fund Revenue	**1,337.7**	**2,185.1**	**729.7**	**738.5**
PF Investment return, net	1,031.6	1,858.9	661.6	633.8
Petroleum Revenue	**306.1**	**326.2**	**68.1**	**104.7**
Petroleum Taxes *	78.1	145.5	7.8	56.1
Royalties and Profit oil	169.3	164.6	32.9	47.7
Other Taxes payment **	58.7	16.1	27.4	0.9

Source: Petroleum Fund Policy and Management Office, Ministry of Finance.
** Petroleum taxes includes petroleum income taxes and additional profit tax.*
*** Other taxes payment includes Withholding Tax, BU Value Added Tax, Wages Tax, other taxes minus tax refund.*

The Budget 2021 projections for total petroleum from the sale of oil and gas are $68.1m. This has already been exceeded. As of May 2021, receipts from the sale of oil and gas amounting $104.7m has been paid into the PF account. The benchmark oil price, Brent crude oil, was higher than estimated, averaging about $63 per barrel between January and May. The oil price may increase further in the second half of 2021 as global demand increases and the global economic outlook improves. The revenues for 2021 will be higher than the estimates in the 2021 Budget Book and a new estimate will be made in August 2021. However, the future petroleum revenue will be low relative to prior years as the reserves in Bayu-Undan have declined, even if production is extended. With low petroleum revenue over the coming years, withdrawals will be financed by selling the Petroleum Fund's investments. This will continue at least until inflows are received from the Greater Sunrise or other significant prospective fields.

Investment returns in 2020 were higher than projected at $1,858.9m, which represents a total return of 10.67%. The equity allocation (35% of the Fund) returned 14.03% and Bonds (60%) posted 5.04%. The equity rally in 2020 was aided by fiscal stimulus, very accommodative monetary policy and, in quarter 4, news of an effective vaccine for containing the Covid-19 outbreak. Up to May 2021, the Fund's total return was 3.47%, which translates to $633.8m, with equity posting returns of 12.31%, fixed income delivering a negative return of 1.30% (a rise in interest rates caused capital losses), and the investment in the oil operation accrued interest of about 1.9%. The total return for 2021 will depend on market movements over the coming months; a downturn in markets will erode the return. The annual nominal investment return since inception of the Fund is 4.9%, about 2.9% in real terms after deducting US inflation. While the Fund's historical return has been near the 3% real return target, future investment returns are expected to be lower because of very low interest rates.

3.6 Petroleum Wealth and ESI calculation

According to the Petroleum Fund Law, the Estimated Sustainable Income (ESI) is the maximum amount that can be appropriated from the Petroleum Fund in a fiscal year and leave sufficient resources in the Petroleum Fund for an amount of the equal real value to be appropriated in all later years. The ESI is set to be 3 percent of the Petroleum Wealth. However, the Government can withdraw an amount from the Petroleum Fund in excess of the ESI given an explanation that it is in the long-term interest of Timor-Leste and that is approved by the National Parliament.

The ESI is only updated once a year as part of the main budget process. Therefore, the ESI of $547.9m in the 2021 Budget is adopted for the pre-budget statement. Table 2 shows the estimated Petroleum Wealth and the ESI from 2020 and 2021.

Table 6: Petroleum Wealth and the Estimated Sustainable Income (ESI)

	2020 Budget	2021 Budget
Estimated Sustainable Income (PWx3%)	**544.4**	**547.9**
Total Petroleum Wealth (PW)	18,145.1	18,262.4
Opening PF Balance	17,691.8	18,065.6
Net Present Value of Future Revenues	453.2	196.8

Source: Petroleum Fund Policy and Management Office, Ministry of Finance, 2021.

The revised Petroleum Fund balances are shown in Table 3 and take into account the actual result in 2020 and 2021 discussed above.

Table 7: Petroleum Fund Savings 2020-2021 ($m)

	2020 Budget	2020 Actual	2021 Budget Annual	YTD May-2021 Actual 5 months
Opening PF Balance	**17,691.8**	**17,691.8**	**18,065.7**	**18,990.6**
Petroleum Revenue (excluding PF Interest)	306.1	326.2	68.1	104.7
PF Interest, Net	1,031.6	1,858.9	661.6	633.8
Total Withdrawals	(963.9)	(886.3)	(1,377.6)	(350.00)
Closing PF Balance	**18,065.7**	**18,990.6**	**17,417.8**	**19,379.2**
Net change in value	373.90	1,298.8	(647.90)	388.60

Source: Petroleum Fund Policy and Management Office, Ministry of Finance, 2021.
Where: PF Interest, Net = PF Net Investment Return

The proposed withdrawal for the FY 2021 remains at $1,377.6m, as in the original Budget 2021. This is almost three times the 3 per cent ESI. Since 2009, the withdrawal is averaging at 8% of Petroleum Wealth and the cumulative withdrawals totalled $12,820.9m (approximately $13bn). From January to May 2021, $350m has been transferred to the State Budget and the Balance of the Petroleum Fund is $19.4bn.

The Petroleum Fund's balance is projected to decline as a result of the expected net cash outflows from withdrawals and lower investment returns. The 2021 Budget Book projected that the Fund will be exhausted by 2033. The Fund is expected to fall in value at least until there are inflows from Greater Sunrise. The balance was able to grow in both 2019 and 2020 mainly because equity market performance was well above current expectations.

Equities also involve exposure to the downside. To manage this risk the Ministry of Finance has adopted advice from the Investment Advisory Board to segment the Fund into 1) a liquidity portfolio of very low risk assets that will be used to finance withdrawals over the next three years; and 2) a growth portfolio that maintains the 35%/65% allocation to equities and fixed interest. The structure balances the need to reduce risk in the part of the Fund that will finance near-term withdrawals, while allowing the longer-term holdings to participate in the potential upside from investing in equities.

3.7 Fiscal Sustainability Analysis

The economy of Timor-Leste is currently highly dependent on the Petroleum Fund for financing the fiscal deficit. In recent years, government policy has been one of front-loading expenditure, running high government budgets in the short run to finance capital spending for key infrastructure, with the aim to encourage development of the private sector, increase diversification and grow the overall economy. A stronger non-government Timorese economy would require less funding from the Petroleum Fund in the future as the fiscal deficit would be smaller due to higher non-oil domestic revenues and a lower need for government spending to boost the economy in normal times.

The Ministry of Finance conducts a fiscal sustainability analysis for the budget ceiling chosen each budget cycle. Through the use of modelling, the impact of the selected budget ceiling on the long term sustainability of Timor-Leste can be estimated, specifically the overall balance of the Petroleum Fund. The model used mainly focuses on the impact of capital spending on longer-term GDP and domestic revenues and their impact on the Petroleum Fund reserves.

Due to uncertainty of future variables in the model, e.g. the budget of future years, the model uses a number of assumptions. Firstly, it makes assumptions about the growth rates of the ceilings for all appropriation categories, based on historical data, while the growth of Capital and Development is estimated to follow the requested amounts set out by the Infrastructure Fund in the years 2022-2026 and a long term growth rate based on past data after that. Short term GDP and inflation figures are based on forecasts by the National Directorate of Economic Policy in the Ministry of Finance. The long run growth rate of GDP, inflation and domestic revenue growth and the long term return on the Petroleum Fund are constructed using set base line levels. Changes to any of these assumptions would have significant changes on the forecasted end date of the Petroleum Fund. For example, if the rate of expenditure growth were to increase more than that assumed in the model, then the Petroleum Fund would finish quicker than forecasted. The ESI (Estimated Sustainable Amount) from the Petroleum Fund is set at 3% of the Petroleum Fund value and counted as part of Total Revenue. This means that as the amount of the Petroleum Fund falls, so does the amount of the ESI.

It is important to state that the model does not factor in any effect to GDP when the Petroleum Fund balance hits zero, or close to it. This seems unlikely as the associated fall in expenditure would likely cause an economic downturn, with a fall in consumer and private sector spending and a decline in GDP. This downturn would also have an effect on domestic revenues, further decreasing possible expenditure.

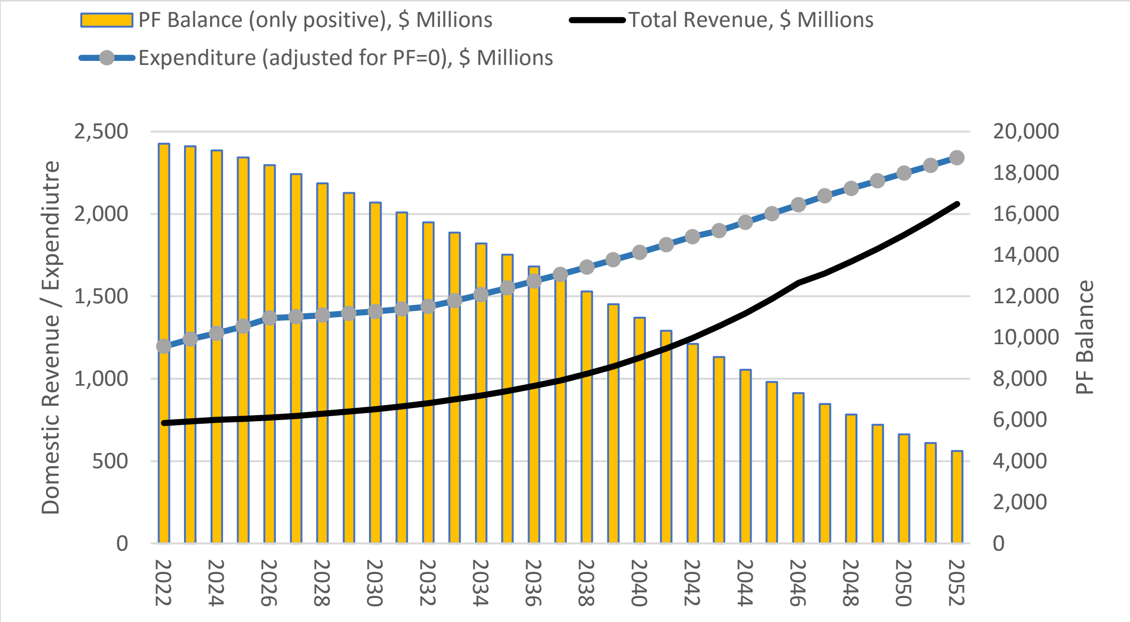
The sustainability of the petroleum fund is not only dependant on the choice of expenditure, but also all subsequent years. Here 3 different expenditure paths are presented to show the potential impact on the lifetime of the fund.

Option 1: Petroleum withdrawals capped at $1 billion a year

Under the new petroleum fund segmentation approach, it is assumed that total withdrawals (ESI plus excess withdrawals) will total $1 billion each year. This assumption is used to estimate the amount to be moved into the liquid portfolio to allow it to be accesses quickly and efficiently, leaving the rest of the fund’s resources in a growth portfolio with higher yields but lower accessibility.

Assuming that spending sticks to these guidelines, the model estimates that the Petroleum Fund would not run out over the next 30 years.

Figure 24: Fiscal sustainability analysis under Petroleum Fund segmentation, $millions



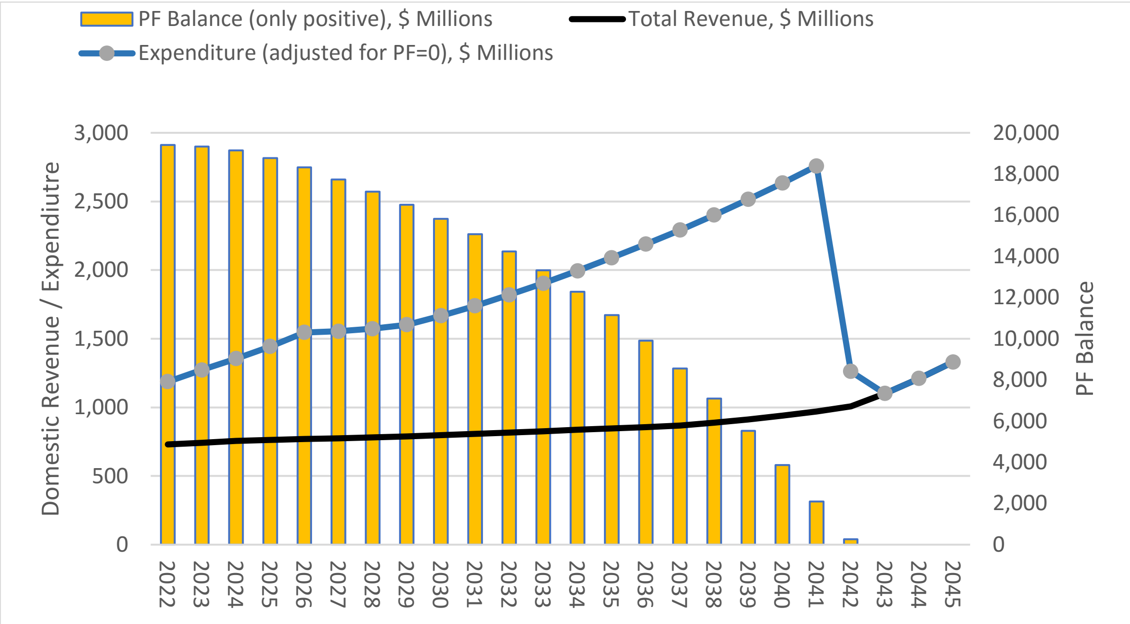
Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

The model does suggest that the Petroleum Fund would be likely to run out at some point in the future, as the fund is estimated to total $4.5 billion in 30 years' time and domestic revenues have not yet reached the level of expenditure. As the Fund begins to get close to zero, expenditure would have to fall rapidly in order to match domestic revenues as that would be the only source of income (excluding external debt). ESI would no longer exist. However the increased timeframe would give the private sector more time to grow, thus allowing domestic revenues to rise to a higher level. This means that when the Petroleum fund did run out, the required fall in expenditure would be much lower; making the process much less difficult and the adjustment time shorter.

Option 2: Population and Inflation growth rates

To ensure that the budget remains constant per capita in real terms, it would be necessary for the budget to grow at both the same rate as the population and as the expected rate of inflation. The long-run population growth rate and expected level of inflation is 3.9% per year. Using this assumption as also the long run budget growth rate, the model estimates that the Petroleum Fund would run out in 2043. This is 22 years away.

Figure 25: Fiscal sustainability analysis under population and inflation growth rates, $millions



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

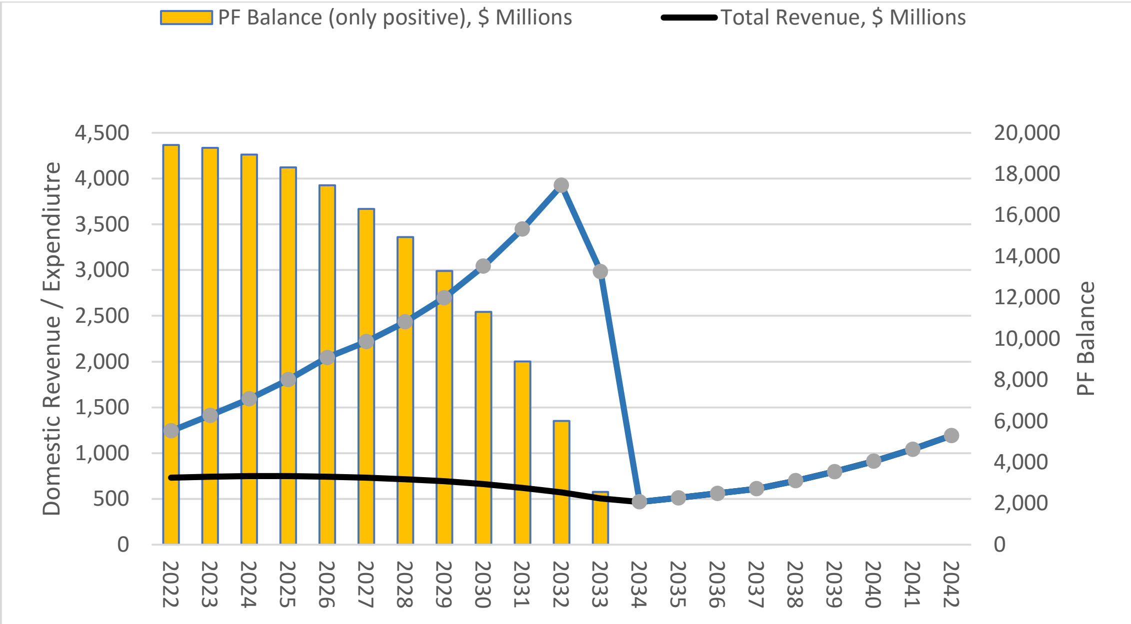
The model estimates this would be mean a 60% fall in expenditure in two years (2031-2043), the final two years that the Fund can be used to support government spending. This relates to a fall from $2.8 billion to $1.1 billion (when expenditure must equal domestic revenue). If revenues do not rise as quickly as the model forecasts, the fall in expenditure would have to be even greater. Therefore it is vital that mobilisation of domestic revenues is a key focus of the government over the coming years.

Option 3: Historic appropriation category growth rates

The average growth rate of approved budget spending (not adjusted for execution) across all appropriation categories (including loans but excluding contingency expenditure) between 2012 and 2021 was 28.1% per year. This masks significant variation between categories with Minor Capital seeing the largest annual growth (95.3%) and Capital and Development the smallest (5.0%).

Assuming spending follows these historic growth rates (with some small adjustments for categories with excessively high changes), the model estimates that the Petroleum Fund would run out in 2034, 13 years away.

Figure 26: Fiscal sustainability analysis under historic appropriation category growth rates, $millions



Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

The model estimates this would be mean an 88% fall in expenditure in two years (2032-2034), falling from $3.9 billion to $468 million (when expenditure must equal domestic revenue). This is the largest shock from all three options presented and would likely cause a rapid decrease in GDP

3.8 Contingent Liabilities

Timor-Leste, like any other nation has a number of contingent liabilities, ie potential government spending that is triggered by a specific event. It is important for governments to understand their contingent liabilities as they are a type of fiscal risk. Fiscal risks are factors that may cause fiscal outcomes to be different from expectations or forecasts. In the case of Timor-Leste this can lead to excess withdrawals, depleting the petroleum fund or last minute virements which divert resources away from planned activities.

Timor-Leste's contingent liabilities are varied: for example, natural disasters such as the recent floods can lead to government interventions to rebuild infrastructure or droughts can trigger government intervention to support farmers for example. Some are more specific and can be quantified (for example the Central Bank's SME Government Guarantee Scheme).

Some contingent liabilities are more difficult to quantify and will take some time and further consultation to better understand. Examples include, unpaid taxes, government participation in private companies and the social security fund. It is the government' responsibility to identify, manage and mitigate risks to reduce to possibility of unexpected pay outs. The government will aim to provide comprehensive disclosure in the coming years.

4 Social Economic Indicators

All data sourced from the World Bank, unless otherwise indicated.

1. Human Development Index

The Human Development Index (HDI**)** is a summary measure of average achievement in three key dimensions of human development: a long and healthy life, being knowledgeable and have a decent standard of living. The health dimension is assessed using indicators such as life expectancy at birth while the education dimension is impacted by mean of years of schooling for adults aged over 25 years and expected years of schooling for children of school entering age. The standard of living dimension is measured by gross national income (GNI) per capita. The HDI uses a logarithm of income, to reflect the diminishing importance of income with increasing GNI.

HDI is broken down into four ranges including score very high human development (0.8-1.0), high human development (0.7-0.79), medium human development (0.55-. 70), and low human development (below 0.55).

In 2019 Timor-Leste was ranked as Medium Human Development stage with score of 0.61 and ranking 141 out of 189 countries. The rank was lower than Fiji but is above Solomon Island as shown in Graph 2. Over time Timor-Leste's HDI score has improved a lot since 2010 and 2011 when it was a low human development country but the improvements have plateaued in recent years.

Timor-Leste's mean years of schooling score was lower than Fiji, Vanuatu, Solomon Island, Lao PDR and Brunei Darussalam in last five years. On the other hand, Timor-Leste has seen progress on the life expectancy score which is now above Myanmar, Lao PDR and Fiji compare to 2018.

Figure 28: Timor-Leste HDI score, 2010 - 2019

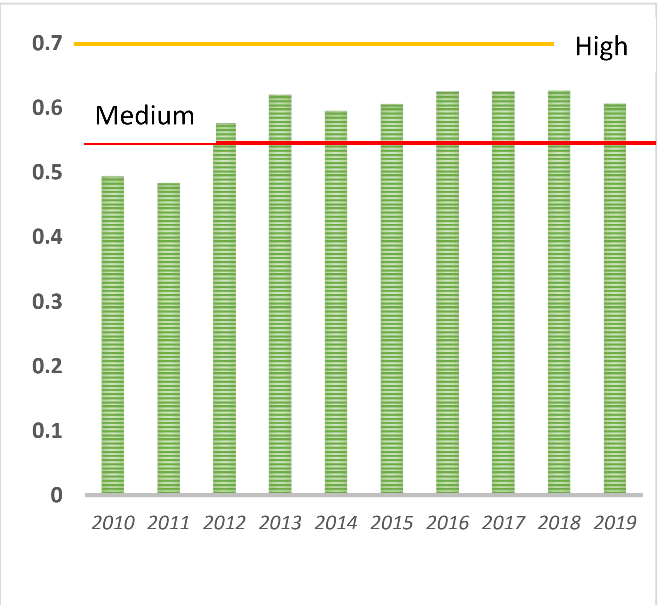
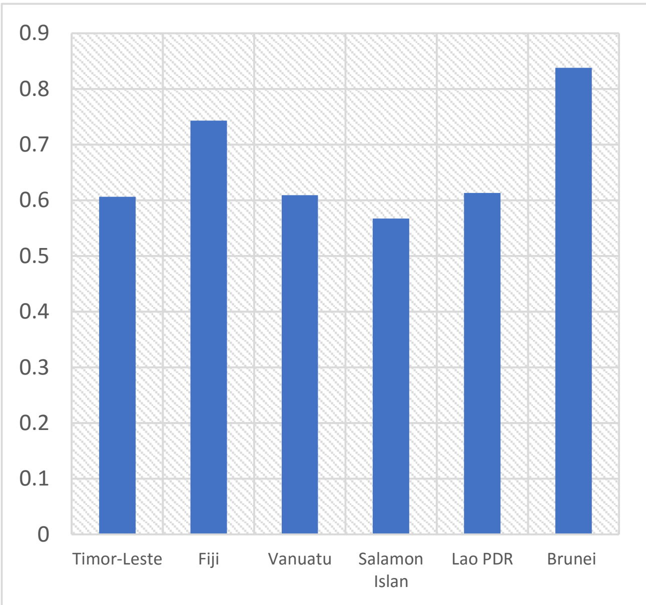


Figure 28: Comparison of Timor-Leste HDI with other countries in Asia Pacific, 2019



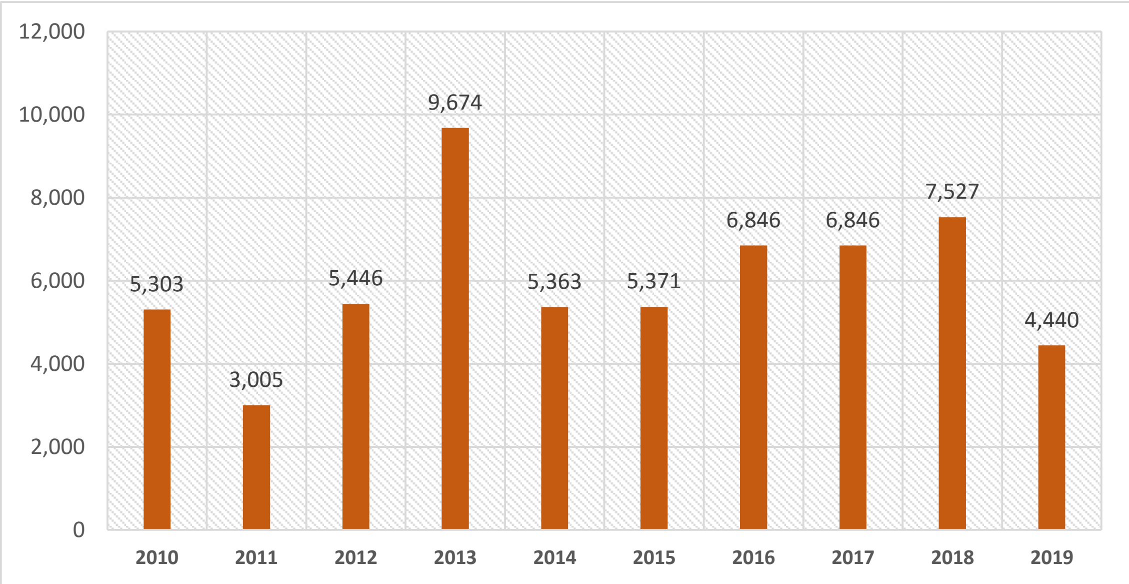
Source: UNDP, Human Development Report 2020

2. Inequality

The Gini index is used to measure how much the distribution of income within an economy deviates from a perfectly equal distribution. The Gini index is ranged from 100 to 0. A Gini Index score of 0 represents perfect equality i.e. all citizens have equal income and 100 implies perfect inequality i.e. 1 citizen has all the wealth. In 2014, the GINI index for Timor-Leste was 28.7 % (World Bank 2014). GINI index of Timor-Leste fell gradually from 35.9 % in 2001 to 28.7 % in 2014 indicating the society has become more equal.

On the other hand, the trend of GNI per capita in the last five years was volatile. In 2019 it went down to $ 4,440 per capita. The highest GNI per capita since 2010 to 2019 was in 2013 as shown in table 2.

Figure 29: Trend of Timor-Leste GNI per capita 2010 to 2019



Source: UNDP, Human Development Report 2020

3. Malnutrition

According to Timor-Leste's Demographic Health Survey 2016, 46% of children under age 5 are stunted; 23% of children under age 5 are severely stunted, 24% percent of children are wasted and about 10% of children are severely wasted. 40% of children are underweight and 6% are overweight.

The prevalence of stunting has declined from 58% to 46% since the 2009/10 DHS. The prevalence of underweight children have also declined, from 45% to 40%. However, the prevalence of wasted children has increased from 19% to 24%. Additionally, the prevalence of stunting among children under 5 years is 45.6%, with males experiencing a higher rate of stunting of 48%, compared to the rate of females of 43%.

4. Human Capital Index (HCI)

HCI, from The World Bank, measures the amount of human capital that a child born today can expect to attain by age 18. It conveys the productivity of the next generation of workers compared to a benchmark of complete education and full health. Worldwide a child born in 2020 can expect, on average, to be 56 percent as productive as she/he could be when she/he grows up. All data represent the status of countries pre-COVID-19.

For Timor-Leste, a child born today will be 45 percent as productive when she grows up as she could be if she enjoyed complete education and full health. This is lower than the average for East Asia & Pacific region (give number) and Lower middle income countries (give number). However there has been progress overtime as between 2010 and 2020, the HCI value for Timor-Leste increased from 0.41 to 0.45.

5. Drinking Water

In 2017, 78% of the population has at least access to basic source of drinking water. This is lower than both the average for the East Asia and Pacific region (92%) and the average for its (lower middle) income group (81%).

6. Labour force

In 2016, 64% of Timor-Leste's working-age population was employed. This is lower than the average for its region (65%) but higher than the average for its income group (54%). The labour force participation rate for female was 62%. This is higher than both the average for its region (57%) and the average for its income group (50%).

7. Adult Survival Rate

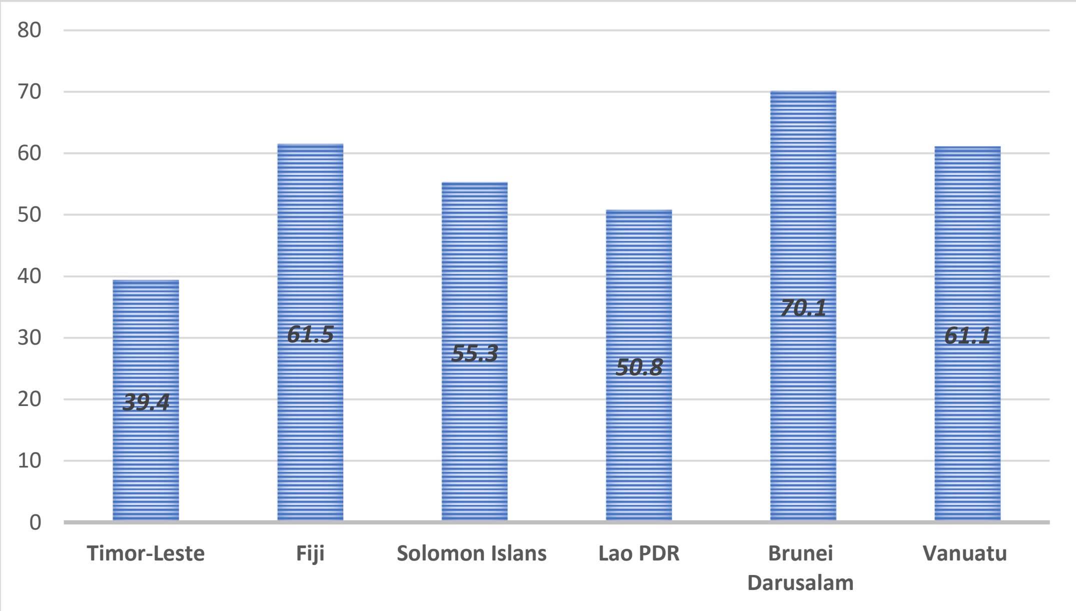
Across Timor-Leste, 86 percent of 15-years old will survive until age 60. This statistic is a proxy for the range of health risks that a child born today would experience as an adult under current conditions.

8. Ease of Doing Business

The Ease of Doing Business report is produced by The World Bank to measure the index of business regulatory performance of a country. The range of doing business scale from 1 to 100, where 0 represents the worst regulatory performance and 100 is the best regulatory performance.

For global comparison, in 2020, Timor-Leste's score was 39.4 or rank 181 out of 190 countries in the world. This score was lower compared to similar countries such as Fiji, Solomon Island, Lao PDR, Brunei Darussalam and Vanuatu.

Figure 30: Comparison in Ease of Doing Business scores of countries in Asia and Pacific



Source: World Bank, Ease Doing Business Report 2020

The calculation of ease of doing business score obtained from individual indicators for each economy including: starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts, and resolving insolvency.

Timor-Leste's best indicator was Starting a Business (68 out of 190 countries) while its worst indicator was enforcing contracts which it ranked bottom out of all 190 countries.

Table 8: Comparison of Ease of Doing Business scores between Timor-Leste and Pacific Countries

Indicator	Timor-Leste		Solomon Island		Vanuatu		Kiribati		Micronesia	
	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score
Starting a Business	68	89.4	110	85.6	137	81.5	149	78.4	174	69.6
Registering Property	187	0	155	47.4	84	65.6	150	49.1	0	187
Getting Credit	173	20	104	50	37	75	173	20	104	50
Enforcing Contracts	190	6.1	157	43.5	138	49.3	121	53.4	184	29.4

Source: The World Bank, Ease Doing Business Report 2020

5 Expenditure Analysis

5.1 Historical Trends

5.1.1 Total level of expenditure

The General State Budget (GSB) for 2020 was $1.482 billion including loans. Out of this, 85.2% of the allocation was to recurrent categories.

The materiality directive[3] of Timor-Leste states that the government must spend 100% of the budget by the fourth quarter (Q4). The total government execution by Q4, 2020 (by current budget which includes transfers, virements and contingency transfer) was 76.4%. The Infrastructure Fund including loans (IF), Human Capital Development Fund (HCDF) and COVID-19 Fund execution for Q4 2020 stood at 75.0%, 82.5% and 58.4% respectively.

The highest government expenditure in the last five year period was in 2016 at $1.64 billion a year with a rectification budget. While 2017 was a duo-decimal year, the government's execution of CFTL (85.8%) was comparable to previous years. Hence, overall execution did not decrease but the issues that line ministries/autonomous agencies (LM/AAs) faced were due to the piece-meal execution of the budget which delayed procurement, contracting etc.

2020 was both a duo-decimal year as well as a year impacted by lockdowns and the COVID-19 pandemic. Despite this, executions rates across most appropriation categories were in line with previous years. The main exceptions to this are those related to capital spending, particularly minor capital. This is not surprising given that the duo-decimal expenditure requirements limit capital spending, thus meaning that the majority of spending was focused in the final few months of the fiscal year.

Table 9: Government execution of the final budget (2016-2020)

AppCat	2016 Execution	2017 Execution	2018 Execution	2019 Execution	2020 Execution
Capital & Development	69.80%	71.20%	85.40%	71.50%	73.49%
Goods & Services	89.70%	86.00%	90.30%	82.70%	66.85%
Minor Capital	84.30%	66.30%	42.70%	74.00%	58.65%
Salary & Wages	94.50%	91.80%	96.00%	93.50%	96.85%
Transfers	98.60%	95.70%	95.60%	93.30%	78.40%

Sources: IFMISU, Ministry of Finance, August 2021

5.1.2 Expenditure by Funds

The Infrastructure Fund (IF) and the Human Capital Development Fund (HCDF) are two independent funds which deal with big infrastructure projects and skill building respectively. The IF received $409.7 million on average (original allocation) between 2016 – 2020, executing

3 Ref no: 44/DGT/III/2016 Ministerial Directive on Materiality in Budget execution analysis and conduct of financial reviews

an average of 75.3% over the same period. In 2019 and 2020, its execution was 75.3% and 75.0% respectively. Its execution is often driven down by a low execution of loan projects.

HCDF received an average budget of $21.6 million across the past 5 years (2016-2020). Its executions over that time was an average of 86.5%. In 2019 and 2020, the overall execution was 88.7% and 82.5% respectively. All of its budget is allocated to trainings, workshops and scholarships.

In 2020, Timor-Leste instituted a COVID-19 fund originally ($220 million, final allocation $333.2 million) for the health response as well as for economic recovery. The fund allocated 28.0% for goods and services, 71.1% for public transfers, 0.5% for minor capital and 0.4% for capital development. Some of the measures spent on included i) state of emergency, ii) social distancing, iii) labour productivity, iv) change in supply chains, v) market performance, and vi) social transfers (electricity subsidy, microbusiness loans, worker wage subsidy). By the end of Q4, 2020, it had spent $194.7 million, an execution of 58.4%.

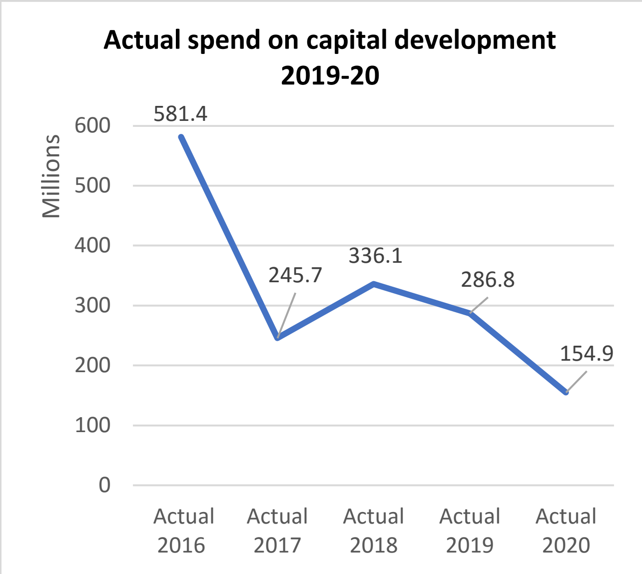
5.1.3 Expenditure by economic classification

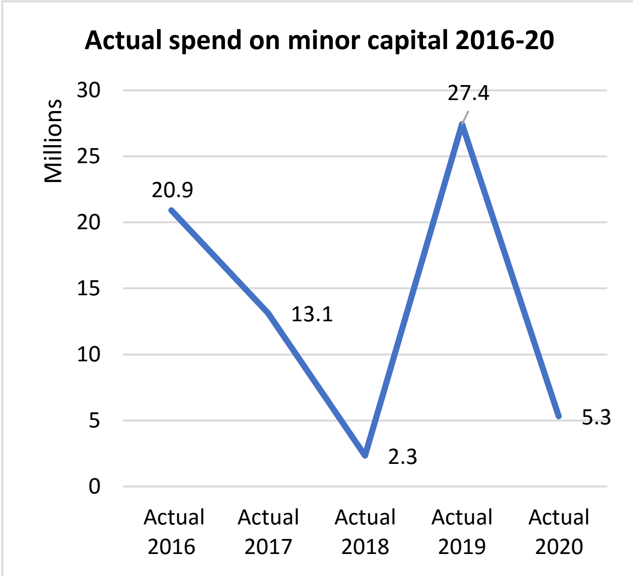
Capital

Capital development (CD) has been a stated policy objective of many consecutive governments in Timor-Leste. When looking budget allocations over the past 5 years, CD has had the highest allocation 2 out of the 5 years as well as the highest average amount with 29.1% of the total budget allocation of the government. There was a budget increase in 2016 was due to a rectification budget which allocated an additional $390k to the Infrastructure Fund for important infrastructure projects. In State Budget 2020, it received $210.8 million in the final budget, out of which $154.9 million were spent. This was a significant decrease from the previous year, largely due to the delay in the passing of the 2020 budget. The total expenditure on CD follows the trend of IF which is the main implementer of all big infrastructure projects. Therefore its execution follows the same trends, with an average execution between 2016-2019 of 74.1%, correlating with an execution of 71.5% and 73.5% in 2019 and 2020 respectively.

Minor capital includes expenditure this is used for the purchase of capital equipment such as furniture and electrical equipment, as well as machines that last for several years and do not need to be repurchased in the near future. It had has the most fluctuating budget of all the appropriation categories, largely due to the limitations on its spending during times of duo-decimal budgets. Its average execution rate for the past 5 year is 65.7%, with range from a low of 42.7% in 2018 to a high of 84.1% in 2016. Execution in 2020 was 58.7%. The spike in 2019 was spent on purchase of vehicles, including ambulances for the Municipality of Ermera, and electronic equipment for a number of Ministries.

Figure 31: Capital expenditure, 2016-2020





Sources: IFMISU, Ministry of Finance, August 2021

Recurrent

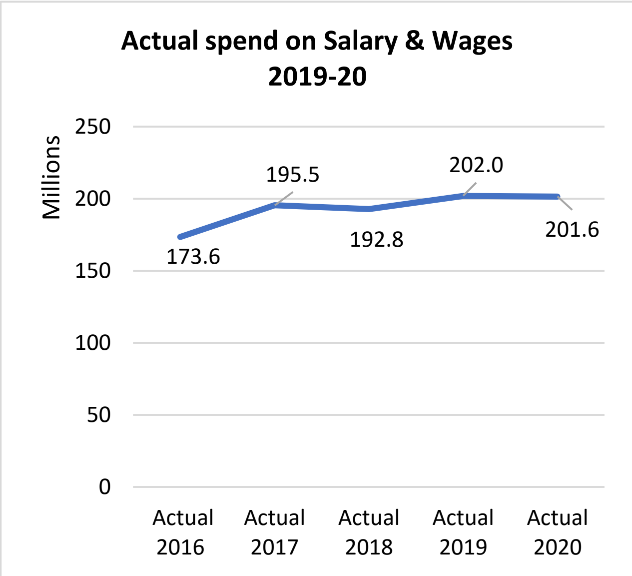
Recurrent budget (salary and wages, goods and services, and transfers) final allocation has remained between 68.7-85.3% from 2017-2020. 2016 was as an exception with an allocation of only 56.0% due to a large capital and development expenditure in that year. In 2019, recurrent budget was 85.3% of the total original allocation.

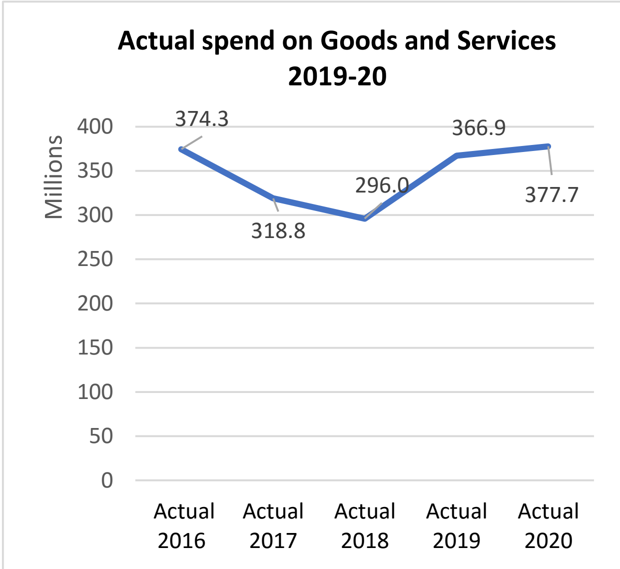
Goods and services received on average 28.5% of the total approved budget in the past 5 years, which has been growing over time. In 2020, the allocation was 37.7%. The increase in 2019/20 was due to payment of combustibles and maintenance for the Hera and Betano generators, including the master plan for water and roads. The additional rise in 2020 was due to an additional allocation to the COVID-19 Fund for health response and economic recovery projects

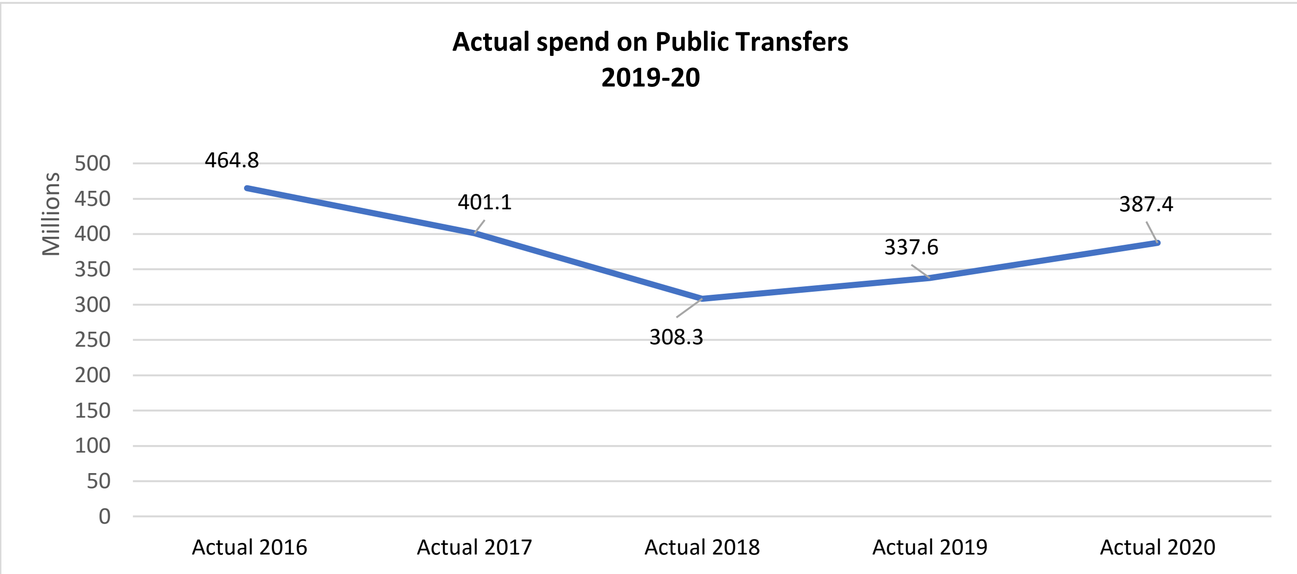
Salaries and wages have been given between 9.4 -15.7% of the approved budget allocation between 216 - 2020, averaging 13.8%. In 2020, the allocation was 13.9%. . There was an increase in the 2017 SW expenditure due to retroactive payments of teachers from 2011-2016 and recruitment of health professionals. The additional rise in 2019 was due to resulting cost increases from changes to the structure of government and pay structures.

Public Transfers comprise all of the money the Government spends on public grants and consigned payments. Transfers have composed 27.4% of the approved government budget for the past 5 years, with a high last year of 33.0% and a low of 24.4% in 2016. In general, transfers are driven by the contributory regime, veteran payments, Bolsa da Mae scheme, disaster management and social investments. Its decline in 2018 was driven by a reduced allocation for the Special Administrative Region of Oecusse Ambeno (ARAEOA) and the Oecusse Ambeno and Atauro Special Zones for Social Market Economy (ZEESM), due to their ongoing infrastructure projects using unspent funds rather than requiring additional capital financing. The rise in 2020 was due to distributions to the COVID-19 Fund to support the economic recovery package, additional investment for Timor Gap and an increased allocation to RAEOA -ZEESM.

Figure 32: Recurrent expenditure, 2016-2020



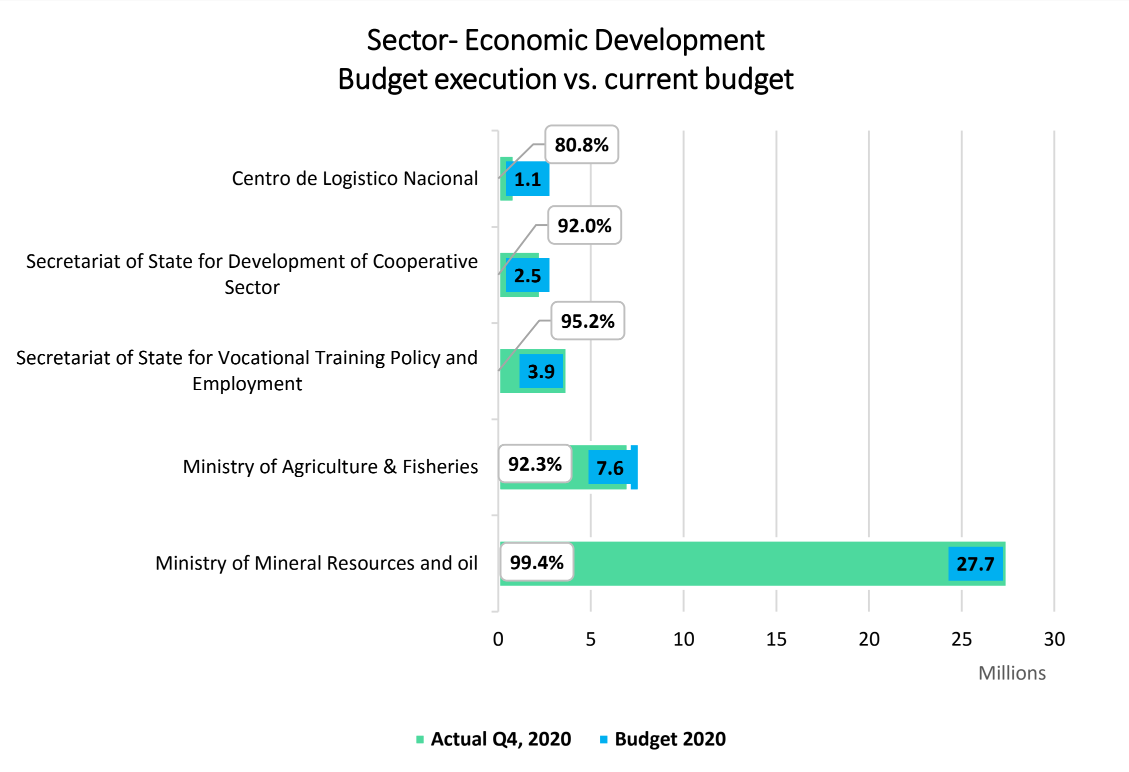




Sources: IFMISU, Ministry of Finance, August 2021

5.1.4 Expenditure by functional classification in 2020

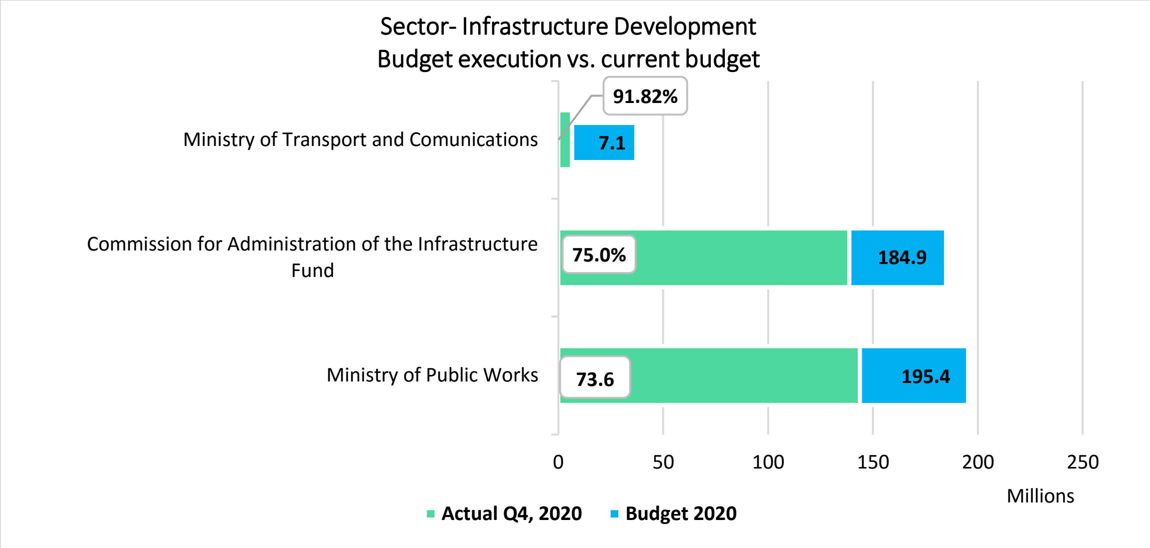
Figure 33: Q4, 2020 execution for SDP Sector-Economic Development



Sources: IFMISU, Ministry of Finance, January 2021

Ministry of Mineral Resources and Oil had the highest budget in the Economic Development SDP sector in 2020 and has also the highest execution at 99.4%. Most other Ministries and Secretariats struggled to reach 95% in their execution when the Q4 report was produced. The exception to this is the Secretary of State for Vocational Training Policy and Employment which had the third highest budget allocation and executed up to 95.2% with an execution on goods and service of just 91.8%. The Ministry of Agriculture and Fisheries (MAP) only reached an overall execution of 92.3%, due to execution on minor capital and capital development (20.2%-23.7%). The reason for low budget executing until December from those four ministries was generally related to the appropriation category in good and service (79.3% - 93.4%) and minor capital and capital development range (23.7% - 99.5%). Public transfer (98.2% - 100%) and salary and wages (80.7% - 96.8%) saw higher execution rates.

Figure 34: Q4, 2020 execution for SDP Sector-Infrastructure Development

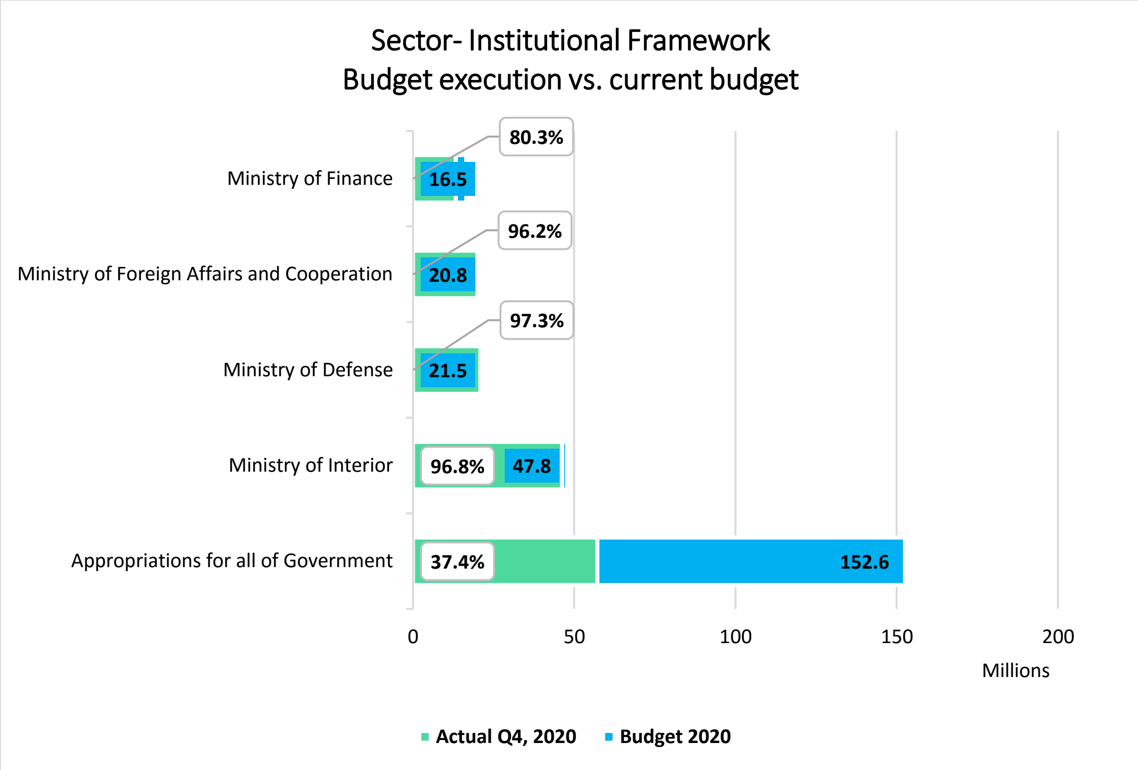


Sources: IFMISU, Ministry of Finance, January 2021

Ministry of Public Works usually has the highest budget allocated to it in the Infrastructure Development (excluding Infrastructure Fund) sector in 2020, it received a total allocation of $195.4 million even though budget execution in all appropriation category just reached 73.6%. This was due to a goods and service execution just 72.4%, the execution of capital and development was 85.4% positive execution progress of the categories on minor capital (91.1%) and salary and wages (93.4%), brought up the average execution for MOP in Q4 stand at 73.6%.

Commission of Administration of the Infrastructure Fund receive highest budget allocation in 2020. However overall execution through the end of Q4, which is execution on capital development totalling 74.9%, Salary and wages saw an execution rate of 99.2% and good and services up to 99.6%, making a total cumulative execution of 75.02%. As for Ministry of Transport and Communication, cumulative execution is 91.8%, based on executions from salary and wages of 87.3%, goods and services of 92.3% and capital development of 84.7%. Minor capital reached the target execution (100.0%).

Figure 35: Q4, 2020 execution for SDP Sector-Institutional Framework



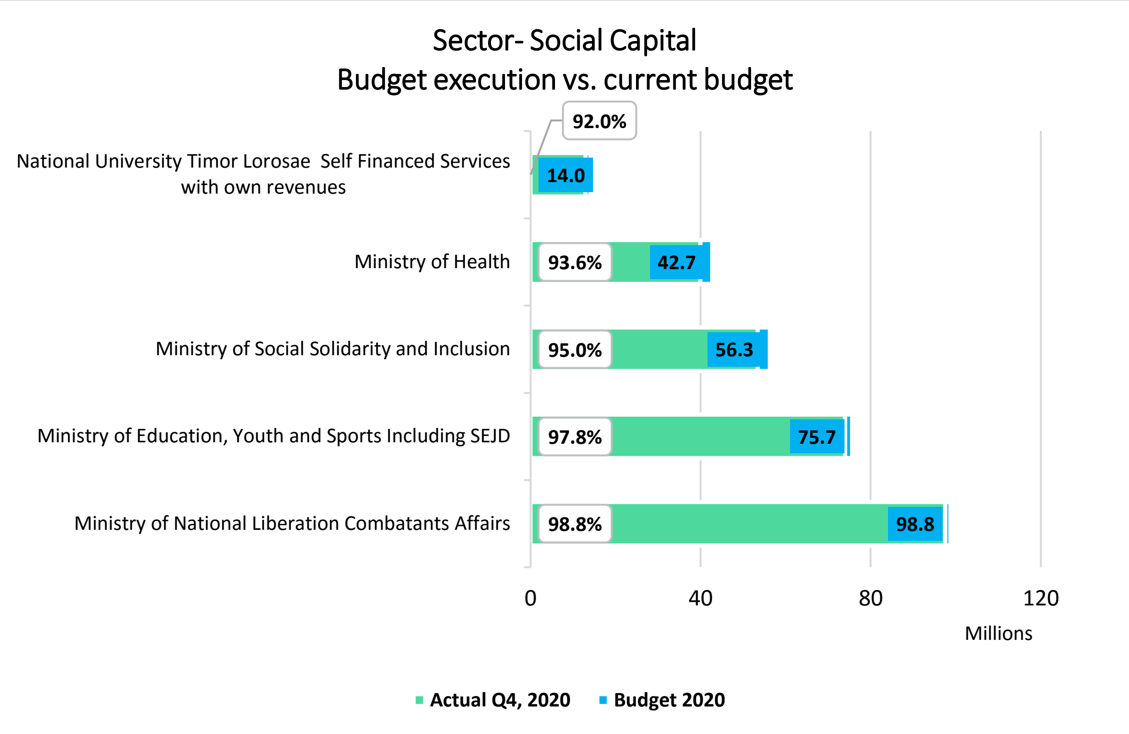
Sources: IFMISU, Ministry of Finance, January 2021

Appropriations for all of Government receive highest budget allocation in 2020 on Institutional Framework but has only executed 37.4% of its allocation due to the low execution for appropriation category on public transfer execution just 28.9%, Good and services executed 69.5%. Ministry of Interior has second highest budget allocation and managed to execute 96.8%. This is because despite an execution of just 44.1% for public transfers, execution rates in the other categories were much higher with salary and wage at 98.3%, goods and services at 96.2%, minor capital at 96.9%, and contingency budget at 116.5%.

Ministry of Finance received the lowest budget allocation in this sector and had the second lowest annual execution through Q4, 2020 due to execution on appropriation category salary and wages at only 80.32%, good and service (80.26%), minor capital (100%), cumulative execution respectively (80.30%).

Other Ministries in this sector, such as Ministry of Foreign Affairs and Cooperation and Ministry of Defence, ranged in their execution between 96.2% - 97.3%.

Figure 36: Q4, 2020 execution for SDP Sector-Social Capital



Sources: IFMISU, Ministry of Finance, January 2021

The Ministry of National Liberation Combatant Affairs (MACLAN) received the highest budget allocation in 2020, with execution until the end of Q4 of 92.6% for salary and wages, 89.5% for goods and services, 93.5% for minor capital, 11.1% for capital development, 99.8% for public transfers, giving a cumulative execution of 98.8%.

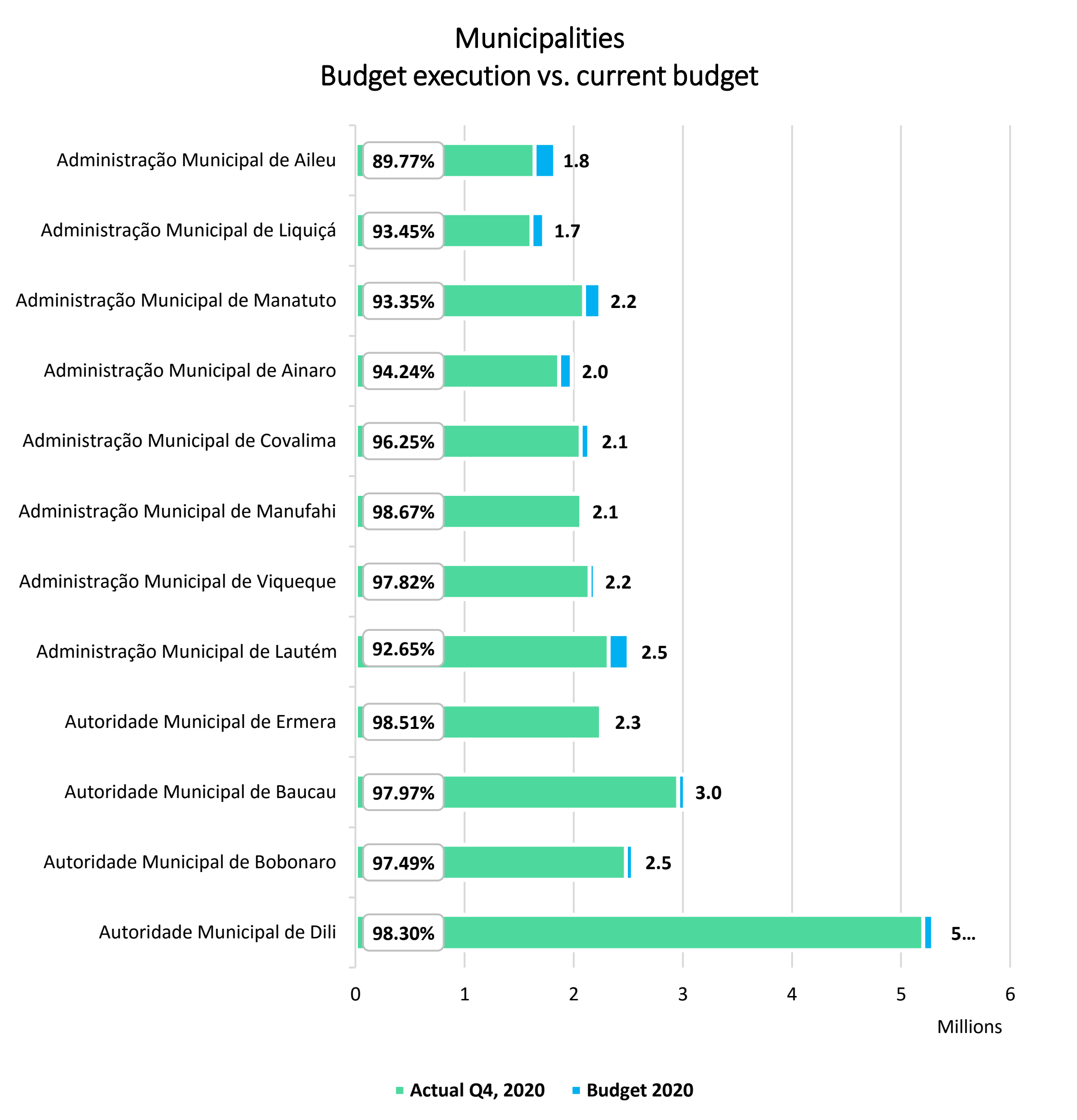
Ministry of Health had the second lowest budget allocation driven down by its category such capital development has budget allocation but not execute until the end of Q4 (0.0%), minor capital execution of 1.7% by end of Q4, 2020. However the other categories where were execution much higher, with salary and wages (95.9%), goods and services (80.5%), and public transfers (99.9%), giving a cumulative execution of 93.6%.

The National University Timor Lorosa'e self-financed services execution was 92.0% due to the execution on category capital development of just 42.8% but other categories such as minor capital, goods and services and salary and wages executed in the range 93.8% - 99.6%. Other ministries executions were relatively near target as shown in the graphs. However, some categories of the execution such like goods and services, minor capital, capital and development and contingency average between 79.8% - 100%.

5.1.5 Municipalities in 2020

Municipality budget execution stood in the 89.8% – 98.7% range. Dili having the highest budget allocation in 2020, with execution cumulative 98.3% which concern from salary and wages, good and service, and public transfer range from 97.3% - 100%. However execution for category budget contingency just stood at 93.0%, therefore Dili Municipality cumulative execution till Q4, 2020 stood at 98.3%. Municipality Aileu, which received the lowest budget allocation in 2020 and also had the lowest in the budget execution as shown in the graph below (89.8%). This is due to execution from each appropriation category such salary and wages only 86.3%, goods and services stands at 86.9%. However the appropriation category public transfers reached 99.1%. Lautem Municipality stand at top five high budget allocation had an execution of just 92.7%, due to the execution on appropriation category good and service of 86.9% only. Overall execution was affected by DOT, especially since many municipality programmes are dependent on line ministry assistance (health, education, public works) which was difficult due to consecutive state of emergency periods.

Figure 37: Q4, 2020 execution for Municipalities



Source: IFMISU, Ministry of Finance, January 2021

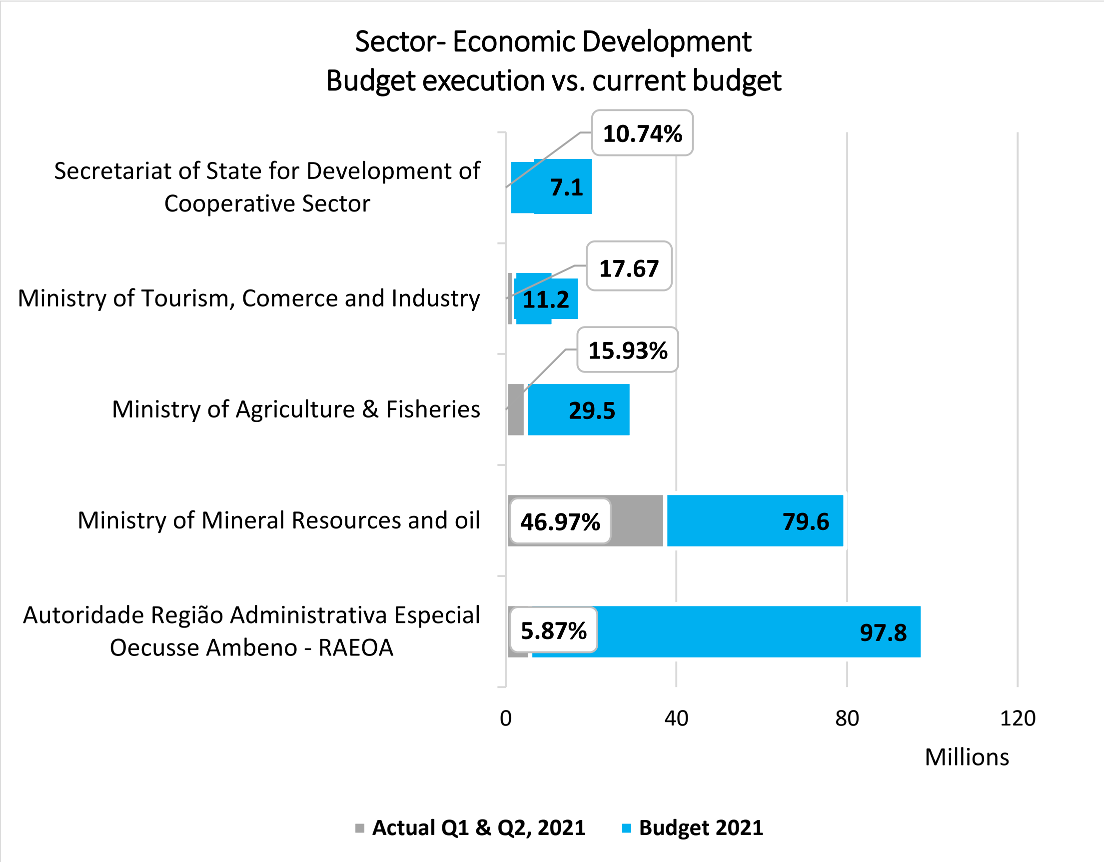
5.2 Mid-year analysis

This section describes budget execution using the Strategic Development Plan (SDP) classification of Timor-Leste. Five ministries for each sector, those with the highest budget allocation, are displayed in the following graphs.

The State Budget for 2021 also includes the COVID-19 pandemic fund. Execution is calculated on the basis of the rectified final budget that has been passed by parliament ($2.03 billion).

5.2.1 Line Ministry Execution by SDP Sector

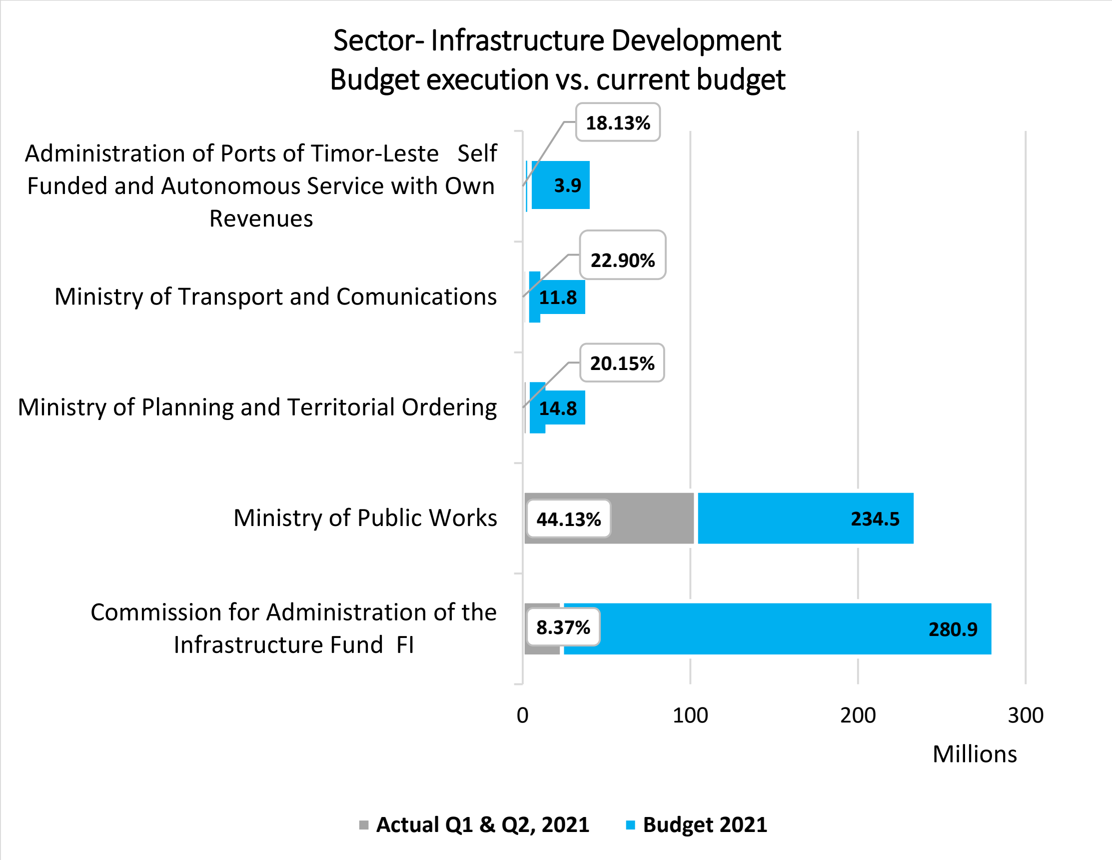
Figure 38: Q1 & Q2, 2021 execution for SDP Sector-Economic Development



Source: IFMISU, Ministry of Finance, July 2021

Autoridade Região Administrativa Especial Oecusse Ambeno - RAEOA had the highest budget in the Economic Development SDP sector in 2021. However, has the lowest execution. Ministry of Mineral and Resource is the second institution with the highest budget and has the highest execution rate of 46.97% in the first semester. Ministry of Tourism, Commerce and Industry has the second highest budget execution rate reaching nearly 18% though its budget allocation is at 4th place.

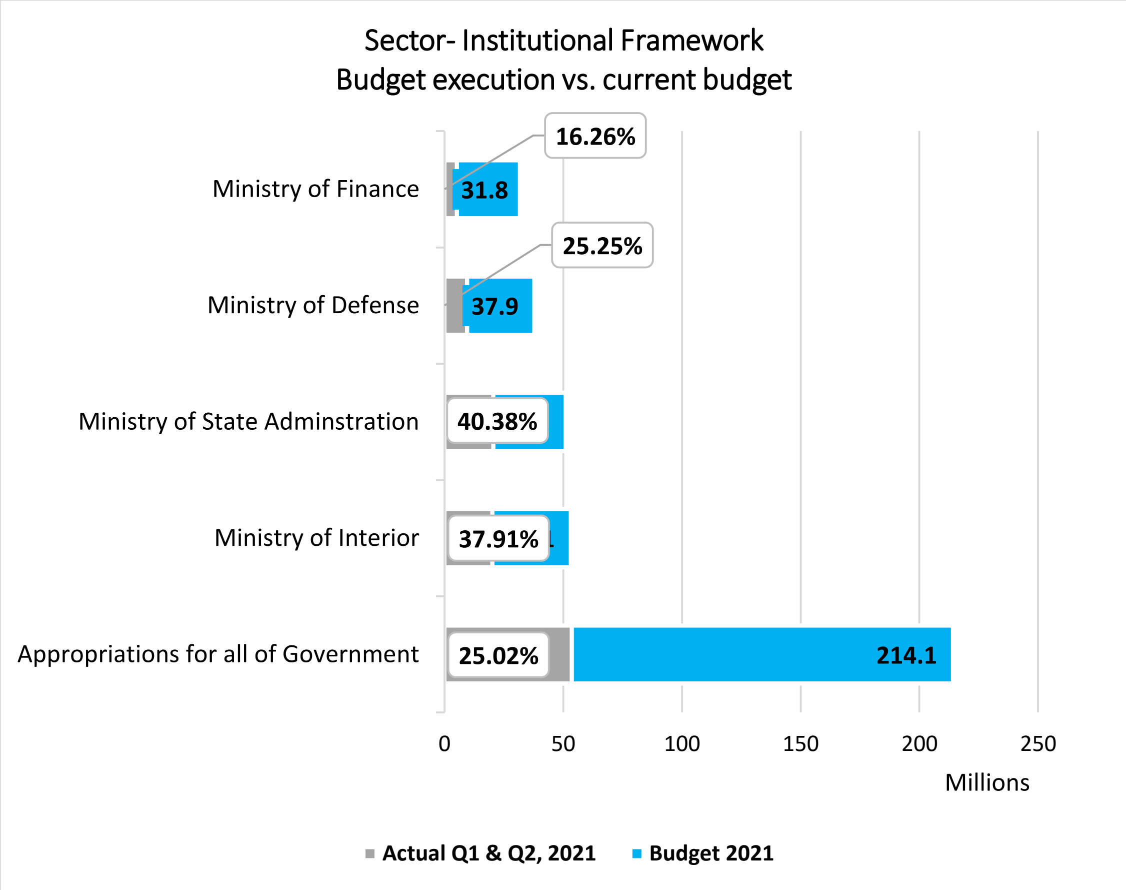
Figure 39: Q1 & Q2, 2021 execution for SDP Sector-Infrastructure Development



Source: IFMISU, Ministry of Finance, July 2021

This year Commission for Administration of the Infrastructure Fund (FI) has the highest budget allocation in the infrastructure development category. Nevertheless, it is the institution with the lowest execution rate at only 8.37%. Following FI, Ministry of Public Works is the second institution the second highest budget allocated to it and is the first institution with the highest execution rate close to 50% execution rate. Ministry of Planning and Territorial Ordering, Ministry of Transport and Communications and Administration of Ports of Timor-Leste are the other 3 institution with highest budget allocation after FI and Ministry of Public Works and their execution rate stood at 20,15% 22.90% and 18.13% respectively.

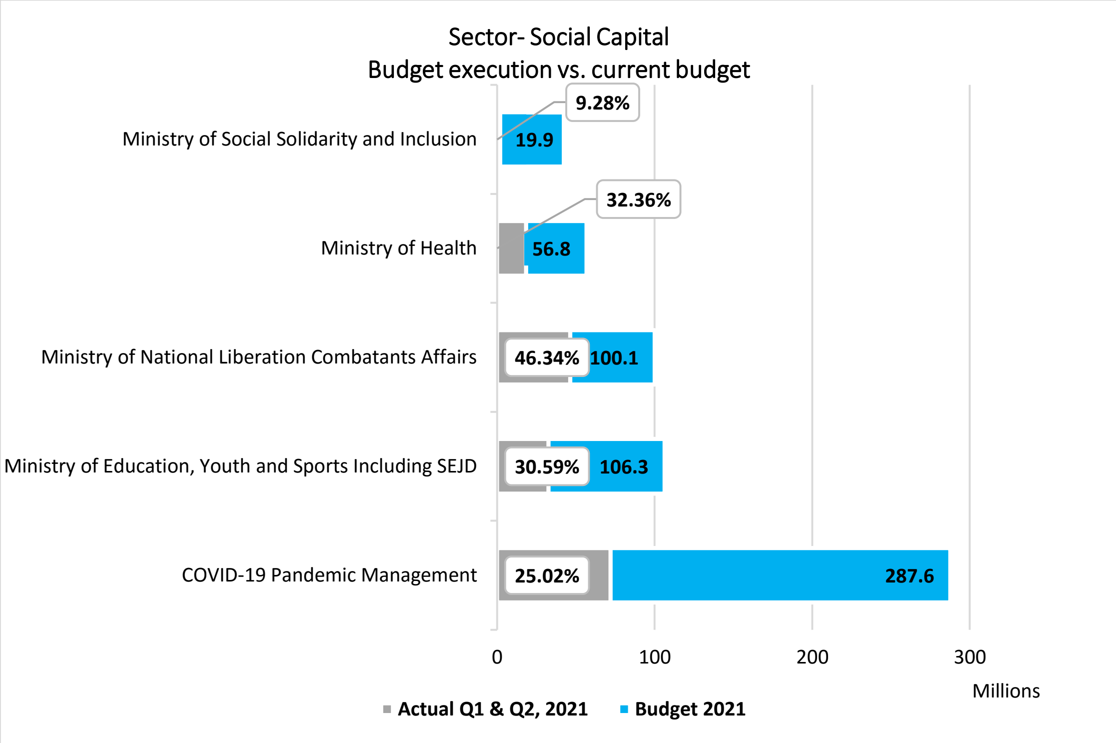
Figure 40: Q1 & Q2, 2021 execution for SDP Sector-Institutional Framework



Source: IFMISU, Ministry of Finance, July 2021

Appropriations for all of Government has the highest Institutional Framework allocation in OJE 2021 but has only executed just over a quarter of it. Ministry of State Administration is the institution with the highest execution rate reaching 40.38% though the budget allocation is in the third place following Ministry of Interior. Ministry of Interior is the second institution with the highest execution rate at nearly 40%. By far institutional framework is the sector with all institution has the highest execution overall at above 15% in the first semester.

Figure 41: Q1 & Q2, 2021 execution for SDP Sector-Social Capital



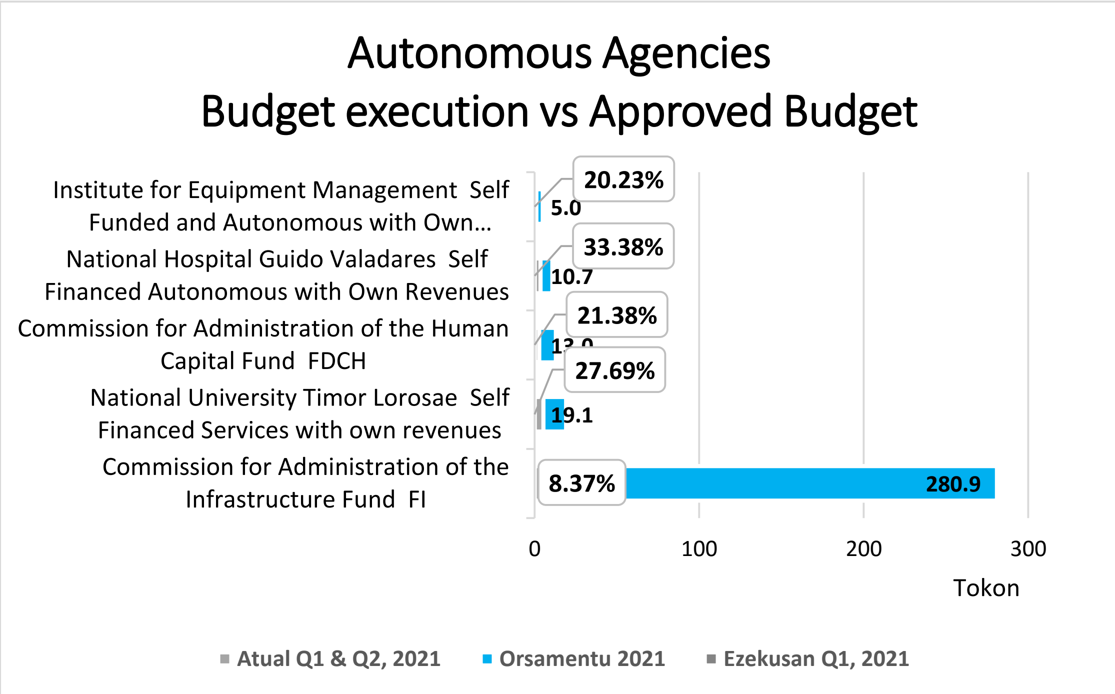
Sources: IFMISU, Ministry of Finance, July 2021

COVID-19 Pandemic Management/ COVID-19 Fund is the new category in social sector and has the highest allocation in 2021. Its budget is government spending in response to COVID-19 and includes pandemic health related needs and payment to front line workers including doctors, nurses, and other health officers as well as for economic recovery. Its execution rate still stands at second lowest at just over 25%. Ministry of National Liberation Combatants Affairs has the highest execution rate though its budget allocation is in the third place following Ministry of Education, Youth and Sports including SEJD.

5.2.2 Autonomous Agency Execution

For autonomous agencies, the Commission for Administration of the Infrastructure (FI) has the highest budget allocation reaching USD 280.9 million, however the execution rate only reach 8.37% in semester 1. The agency with the highest execution rate is National Hospital Guido Valadares with execution rate of 33.38%. Three other institution including National University of Timor-Leste, FDCH and Institute for equipment management have executed their budget over 20%.

Figure 42: Q1 & Q2, 2021 execution for Autonomous Agencies

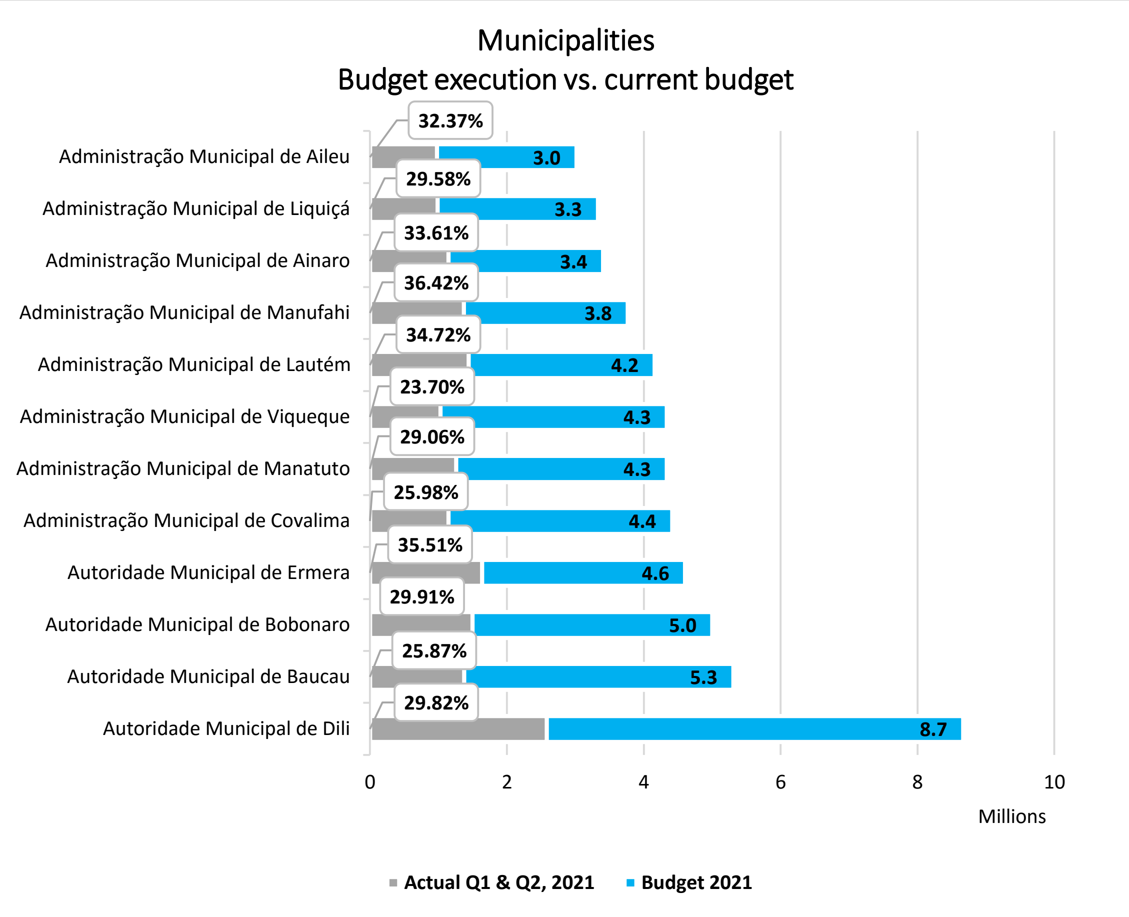


Sources: IFMISU, Ministry of Finance, July 2021

5.2.3 Municipalities Execution

Dili is the municipality with the highest budget allocation. This year's budget allocation to Autoridade Municipal de Dili is 8.7 million with execution rate nearly 30% in one semester. Other municipalities' budget allocation are ranged from USD 3 to 5 million where Autoridade Municipal de Baucau got allocated budget of USD5.3 million following Dili and Administracaun Munisipal de Aileu with the lowest budget allocation among municipalities at USD 3 million. Administrasaun Munisipal de Manufahi is the municipality with the highest execution rate reaching 36.42% followed by Autoridade Munisipal de Ermera at 35.51%.

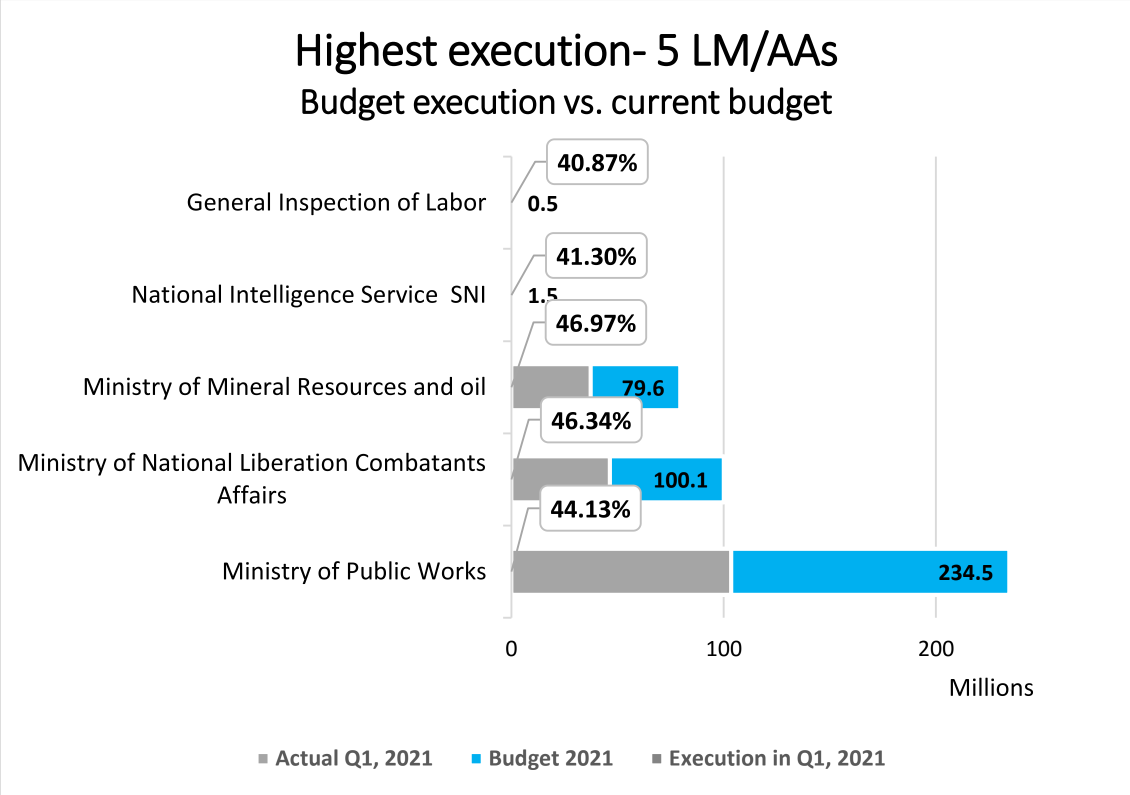
Figure 43: Q1 & Q2, 2021 execution for Municipalities



Sources: IFMISU, Ministry of Finance, July 2021

5.2.4 Top 5 highest execution across LM/AAs

Figure 44: Q1 & Q2, 2021 execution for top 5 highest execution across LM/AAs

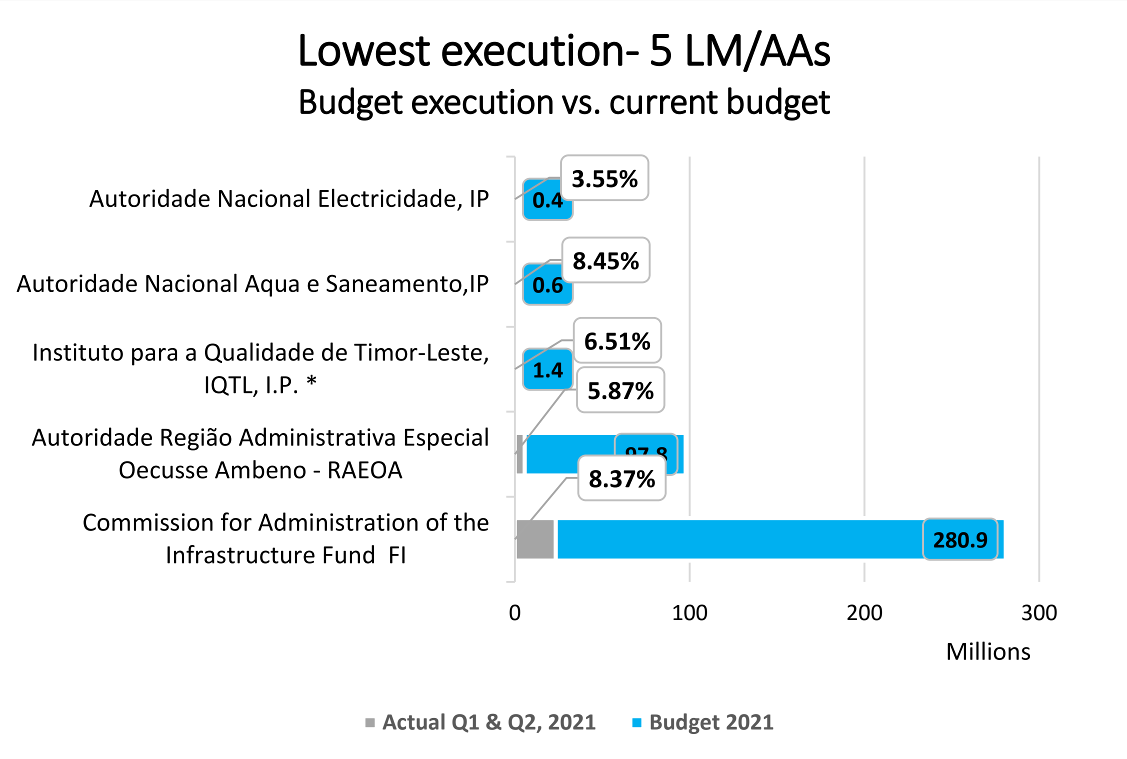


Sources: IFMISU, Ministry of Finance, July 2021

The top 5 institution with the highest execution rate include Ministry of Mineral Resources and Oil, Ministry of National Liberation Combatants Affairs, Ministry of Public Works, National Intelligence Service SNI and General Inspection of Labor at 46.97%, 46.34%, 44.13%, 41.30% and 40.87% respectively. Ministry of Public Works is the institution with the highest budget allocation in this category.

5.2.5 Bottom 5 lowest execution across LM/AAs

Figure 45: Q1 & Q2, 2021 execution for bottom 5 lowest executions across LM/AAs



Sources: IFMISU, Ministry of Finance, July 2021

The graph above indicates 5 institutions with the lowest ranging from 3% to 8%. These institutions include Autoridade Nasional Eletrisidade, Autoridade Rejiaun Administrativa Espesial Oecuse Ambeno-Raeoa, Institutu para Kualidade de Timor-Leste, Autoridade Rejiaun Agua e Saneamentu and Comisaun Administrasaun de Infraestrutura at 3.55%, 5.87%, 6.51%, 8.37% and 8.45% respectively.

6 Government Priorities and Budget Proposal

6.1 Government Priorities and New Measures

In June 2021 the Council of Ministers approved the ceiling for the draft 2022 General State Budget (GSB), set at $1.57bn, and its disaggregation to Line Ministries, SFAs, Municipal Authorities and other relevant institutions. Both the ceiling and its disaggregation are preliminary and may undergo amendments through the Budget Review Committee assessment, the Parliamentary debate and the Presidential evaluation. The approved draft Budget aims to finance the VIII Constitutional Government's Program for the 2022 fiscal year. Six area are defined as priorities for the 2022 Budget and of the remainder of the Government's mandate, 2021-2023:

Table 10: Priorities of the VIII Government, 2022

No.	Priorities 2022
1.	Development of Human Capital (Education, Training and Health)
2.	Housing and Social Inclusion
3.	Productive Sectors (Agriculture, Tourism), Environment and Connectivity
4.	Private Sector Development
5.	Rural Development
6.	Good Governance

Source: National Directorate of Economic Policy, Ministry of Finance, August 2021.

The proposed Budget allocations aim to reflect, therefore, such priorities. The aggregate allocation to each Pillar and their respective new measures are described below. Please note all sectoral allocations described below are preliminary and do not include final budgets for new measures.

Development of Human Capital (Education, Training and Health)

- Create education and training opportunities which are of quality, inclusive and which respond to the needs of the economy.
- Continue to prepare the health sector in terms of quality and service delivery especially in response to the COVID-19 pandemic and continue vaccination roll out.
- Continue professional development of professionals within the health and education sectors.

Housing and Social Inclusion

- Improve access to clean water.
- Continue to focus on basic sanitation.
- Continue to develop access to electricity in sukos.
- Investing in housing programs, both new and on-going.

Productive Sectors (Agriculture, Tourism), Environment and Connectivity

- Diversify the economy and increase the growth rate in an inclusive and sustainable manner.
- Increase agricultural productivity and food security by improving and creating new infrastructure, distribution channels and storage of agricultural products.
- Develop training to support hospitality industry.
- Promote sustainable behaviour and emphasise the principle of reduce, reuse and recycle.

Private Sector Development

- Focus on recovery of the economy following the economic downturn due to the impacts of COVID-19 and confinement in 2020 and 2021.
- Facilitate investment in the private sector, prioritising small and medium size enterprises.
- Create employment options to increase national productivity and opportunity for all.

Rural Development

- Continue decentralization agenda as a tool for promoting local development, promote national identity and territorial cohesion.
- Establishing strong institutions and capacity at all levels of government to ensure the delivery of quality public services to improve efficiency, accountability and transparency.
- Reduce inequalities between regions and make sure vulnerable or minority groups' voices are heard and no one is left behind.

Good Governance

- Introduce medium term plan for all public entities.
- Develop key indicators for national government
- Continue Public Financial Management reform to prioritise Fiscal Reform and Fiscal Sustainability.

6.2 Economic Recovery Package (ERP)

On 29th July 2020, the Council of Minsters approved short term measures to be taken in 2020 to mitigate the impact of the economic crisis due to COVID-19. The principal objective of these measures were of aiding citizens to meet basic needs, assist those workings in the informal sector, secure jobs posts and income and assist businesses.

On the 12th August 2020, the Council of Minsters approved a $104.6m Economic Recovery Package of 71 measures with the objective of aiding the recuperation of the economy post COVID-19 between 2021 and 2023.

The plan has 3 clear objectives:

1) Increasing employment: ensuring all jobs are both productive and dignified

2) Realisation and consolidation of public social investment programmes (Education, Health, Housing or Social Protection)
3) Review productive sectors and promote areas that contribute to economic growth

Nearly 90% of the 71 measures in 2021 were included in the ongoing activities integrated in the Dalan Ba Futuru Timor-Leste (DBFTL) system. The cost of these activities were included in the allocations given to LM/SFA/Ms. Some LM/SFAs received some additional funding for new economic recovery measures provided that they supported essential services/contribute to essential activities. The Ministry of Finance through DGGMRE (Directorate-General for Resource Management and External Mobilization) also mapped the existing/new donor support received which will be detailed in Budget Book 5 2021.

Only 4 new measures (those not in line with existing activities) were introduced. These were:

1. Reinforcing support for projects such as "Quinta Portugal" or others of a similar nature, to increase technical assistance to coffee and other agricultural producers (measure number 9);
2. Create a state-owned company to boost the Tourism sector for the implementation of the tourism policy (measure number 10)
3. Construction of public fountains (measure number 23)
4. The acceleration of the entire process of installing optical fiber through the submarine cable that connects Timor-Leste with the rest of the world (measure number 70)

In 2021, the ERP's biggest measures were related to management of COVID-19 crisis ($110m) including management of quarantine facilities, conducting contract tracing and training to front line staff. In addition to this other measures included distribution of the Cesta Basica (Basic Basket) ($7m), household subsidy ($7.3m) as well as policy for creating jobs for young people ($1.9m). The total amount allocated in 2021 for the ERP was $316m (originally $310m due to virements.

The programmes supported by the ERP in the 2022 budget will be highlighted in OJE 2022 Budget Book 1 given its dependence on the submission of the Line Ministry budget proposals.

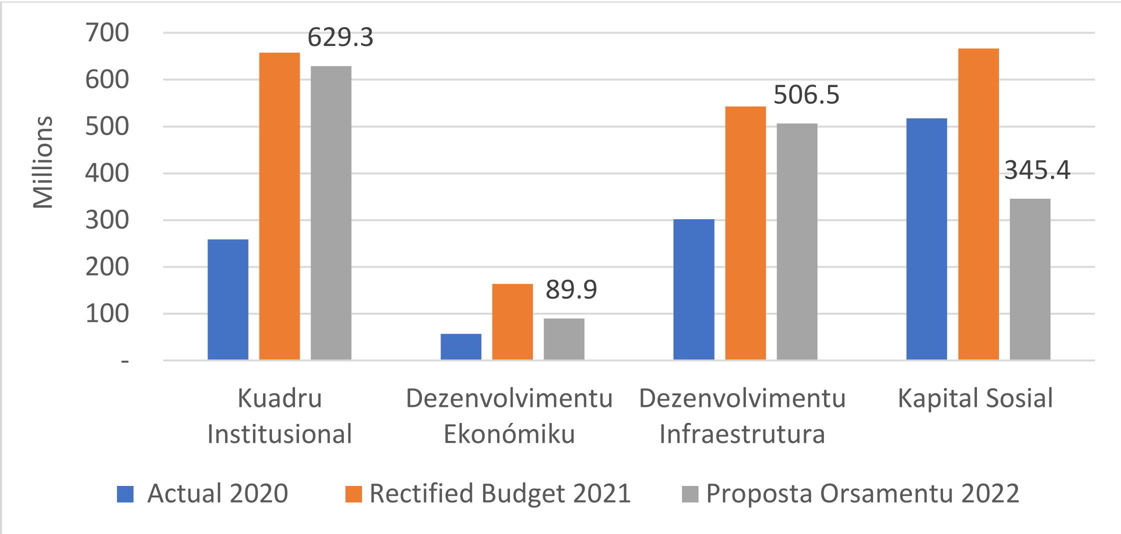
6.3 Analysis of the 2021 Proposed General State Budget

Analysis of the 2022 Proposed General State Budget by Sector

Timor-Leste's 2011-2030 Strategic Development Plan (PED) is organized around four pillars: Institutional Framework, Social Capital, Economic Development and Infrastructure Development, where the last three have been designed as priority in the VIII Constitutional Government's mandate.

The proposed 2022 Budget allocates the largest share of the budget to the Institutional Framework pillar, followed by Infrastructure Development, Social Capital and Economic Development. The figures include loan disbursements and transfers to ZEESM-RAEOA.

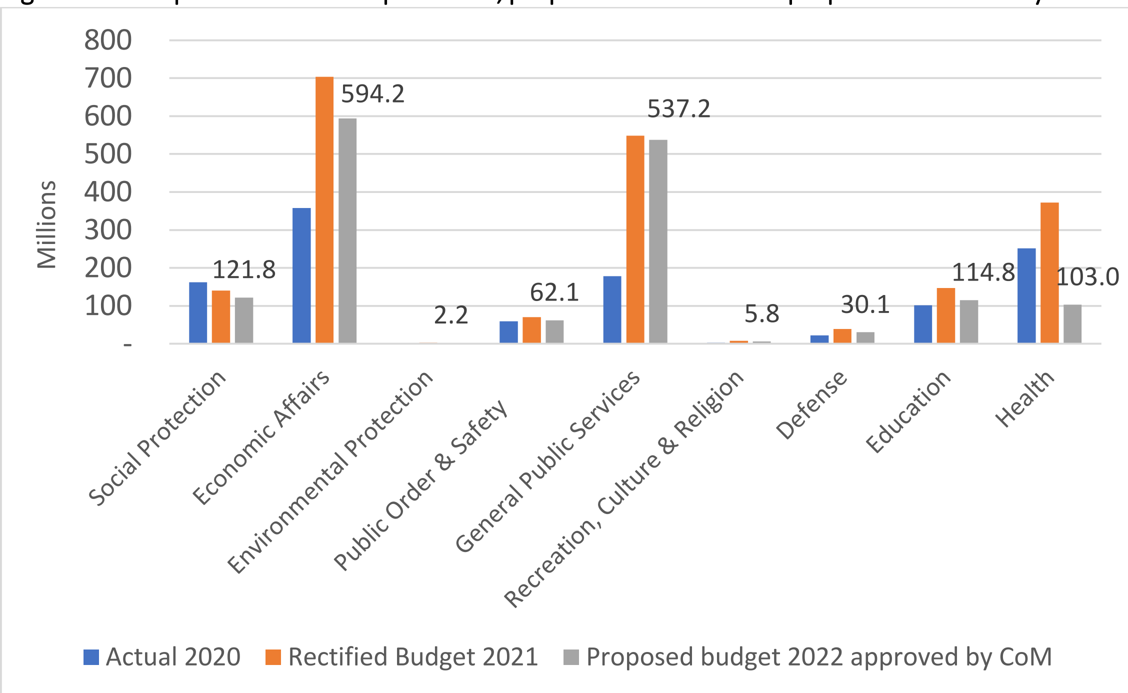
Figure 46: Comparison of 2020 Expenditure, proposed 2021 GSB and proposed 2022 GSB by PED



Source: General Directorate of Planning and Budget, Ministry of Finance 2021.
Please note that all 2022 Infrastructure Fund allocations are preliminary and may change.

Following instead the international sectorial and more detailed classification COFOG (Classification of the Functions of Government), it can be observed that the Economic Affairs sector remains the largest, in line with previous year, followed by General Public Services. Heath sees a significant fall compared to last year, given the fall in budget allocation to the COVID-19 Fund.

Figure 47: Comparison of 2020 Expenditure, proposed 2021 GSB and proposed 2022 GSB by COFOG



Source: General Directorate of Planning and Budget, Ministry of Finance 2021.
Please note that all 2022 Infrastructure Fund allocations are preliminary and may change.

6.4 2022 General State Budget (GSB) Proposal

The VIII Constitutional Government has approved a Budget ceiling of $1.57bn, whose disaggregation according to spending categories is reported in the table below. This represents a 23% fall in government spending compared to the current budget.

Table 11: Proposed 2021 Budget by Appropriation Category, $ Millions

Appropriation Category	Proposed 2022 Budget
Salary and Wages	229.4
Goods and Services	390.7
Public Transfers	459.3
HCDF	10.0
RAEOA (Recurrent)	39.1
Total Recurrent Expenditure	**1,128.5**
Minor Capital	5.7
Capital and Development (IF includ. loans)	**331.7**
Capital and Development (LM, PDIM)	105.7
Total Capital Expenditure (including loans)	**443.1**
Loan Disbursements (included in IF above)	69.0
Support from DBS (included in app cat above)	15.6
Total Budget Ceiling	**1,571.6**

Source: General Directorate of Planning and Budget, Ministry of Finance 2021.

Recurrent expenditure amounts to $1.129 billion. This is a -27% change with the final 2021 budget. Salaries and wages are maintained at a similar level, declining less than 1%. Goods and Services and Public Transfers see significant changes, falling 29.1% and 35.6% respectively. RAEOA is set to receive $84.4 million in 2022 in comparison to $97.8 million in the rectified 2021 budget.

The Capital and Development fiscal ceiling is preliminarily set at $437.4 million, including loan disbursements of $69.0 million. This amount is to be allocated according to Table 5, where 75.8% falls under the Infrastructure Fund management and includes the budget for loan disbursements, and the rest is allocated to Line Ministries, SFAs and Municipalities. New capital measures will be discussed and presented in the expedited Budget Review Committee.

Table 12: Proposed Allocation of the Capital and Development 2021 Budget by Institution, $ Millions

Institution	Proposed 2021 Budget
Infrastructure Fund (New and Ongoing Measures)	262.7
Infrastructure Fund (Loans)	69.0
Line Ministries, Autonomous Agencies (New and Ongoing Measures)	104.2
Integrated Municipal Development Plan (Only ongoing projections)	1.5
Total	**437.4**

Source: General Directorate of Planning and Budget, Ministry of Finance 2021.

The sources of financing of the proposed GSB are outlined in the table below. 45.2% of the proposed fiscal ceiling will be financed through *sustainable* domestic sources i.e. non-oil domestic revenue and the Estimated Sustainable Income of the Petroleum Fund; 54.8% come from oil and external sources, specifically excess withdrawals from the Petroleum Fund (30.8%). Cash balances from Treasury and RAEOA/ZEESM are forecast to contribute 18.6%, largely due to the low rates of execution of the current year's budget. Loan disbursements (4.4%) and Direct Budget Support from the EU and Australia (1.0%) make up the remaining amount.

It is import to note that even under current expenditure levels, the expected total withdrawals (ESI and excess withdrawals) from the Petroleum Fund is $1,047 million. This is already exceeding the $1 billion cap on total annual withdrawals.

Timor-Leste's remains highly dependent on both oil-derived (ESI and Excess Withdrawals) and external (loan disbursements) financing streams. Fiscal Sustainability analysis on the proposed ceiling predicts that the Petroleum Fund could be depleted by the year 2034, at historic baseline assumptions of medium- and long-term revenue, expenditure and GDP growth, and excluding the costs or benefits from the Greater Sunrise development.

Expanding the sustainable, domestic and non-oil revenue base remains key to ensure the country's long-term sustainability and development.

Table 13: Revenue and Financing Source of the Proposed 2021 General State Budget*, $ Millions

	Proposed 2021 Budget
Government Expenditure	**1,571.6**
Revenue	**710.4**
Domestic Revenue	148.0
Estimated Sustainable Income	562.4
Fiscal Balance	**(861.2)**
Financing	**861.2**
Excess Withdrawals from the Petroleum Fund	484.8
Loan Disbursements	69.0
Cash Balance	291.7

	Proposed 2021 Budget
From Treasury	*207.3*
From RAEOA/ZEESM	*84.4*
Direct Budget Support	15.6
From EU	*9.0*
From Government of Australia	*6.6*
Development Partner Commitments (not included in government expenditure)	**155.1**

*Source: General Directorate of Planning and Budget, Ministry of Finance 2021. *Please note that all figures will be recalculated before the final budget proposal.*

Disaggregation of the proposed 2022 General State Budget by receiving Public Entity

The tables below present the proposed 2022 GSB divided by Line Ministries and SFAs and Municipal Authorities' allocation, comparing it with actual expenditure in 2020 and the approved rectified 2021 GSB.

Nearly all Line Ministries see a reduction in their budgets compared to 2021. This is not unexpected given the significant decline in the overall budget ceiling. However 3 Line Ministries see their budget allocations increase in real terms, Ministry of Tourism, Commerce and Industry (+21%), Ministry of Interior (+8%) and Ministry of Parliament Affairs and Social Communications (+0%). Appropriations for all of Government also rise 17%. Ministries that see the largest decrease in real terms are Ministry of Mineral Resources and Oil (-70%), Ministry of Planning and Strategic Investment (-47%) and Ministry of Agriculture & Fisheries (-40%).

When comparing to actual spending in 2020, the changes are more mixed. Some Line Ministries see a more than doubling of their budgets. These are Appropriations for all of Government (+337%), Ministry of State Administration (+206%), Ministry of Agriculture & Fisheries (+149%), Secretariat for State for Environment (+113%), Ministry of State, Coordinator of Economic Affairs (+106%) and Secretariat of State for Youth and Sport (+105%). However on the other hand, some see significant falls including Ministry of Social Solidarity and Inclusion (-65%), Ministry of Defense (-58%), Ministry of Interior (-57%) and Ministry of Planning and Strategic Investment (-40%).

Table 14: Proposed Allocation to Line Ministries, $

Sector	Name	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
SOCIAL CAPITAL	Secretariat of State for Equality and Inclusion	933,199	2,390,650	1,812,500	**94%**	**-24%**
	Ministry of Health	39,978,292	56,767,506	50,021,285	**25%**	**-12%**
	Ministry of Education, Youth and Sports including SEJD	73,980,512	106,341,251	81,560,174	**10%**	**-23%**
	Secretariat of State for Youth and Sport	2,835,885	7,452,628	5,822,048	**105%**	**-22%**
	Ministry of Higher Education, Science	5,017,234	6,133,915	4,854,459	**-3%**	**-21%**

Sector	Name	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
	and Culture Including SEAC					
	Ministry of Social Solidarity and Inclusion	53,440,106	19,942,903	18,450,325	**-65%**	**-7%**
	Ministry of National Liberation Combatants Affairs	97,571,833	100,117,580	88,558,054	**-9%**	**-12%**
INSTITUTIONAL FRAMEWORK	Prime-Minister	6,329,814	11,676,232	8,169,024	**29%**	**-30%**
	Minister of State for the Presidency of the Council of Ministers	3,959,663	5,022,647	4,230,677	**7%**	**-16%**
	Ministry of Finance	13,259,405	31,831,990	24,720,669	**86%**	**-22%**
	Appropriations for all of Government	57,135,832	214,124,357	249,507,471	**337%**	**17%**
	Ministry of Foreign Affairs and Cooperation	20,003,558	26,365,811	22,498,606	**12%**	**-15%**
	Ministry of Justice	11,666,825	14,842,589	11,851,374	**2%**	**-20%**
	Ministry of State Administration	14,737,606	51,099,342	45,116,473	**206%**	**-12%**
	Ministry of Defense	20,908,780	12,731,414	8,741,811	**-58%**	**-31%**
	Ministry of Interior	46,227,447	18,251,846	19,798,398	**-57%**	**8%**
	Ombudsman for Human Rights	1,176,747	1,857,468	1,536,148	**31%**	**-17%**
	F-FDTL		25,171,729	20,527,233	**n/a**	**-18%**
	PNTL		34,892,529	28,905,285	**n/a**	**-17%**
	Autoridade Região Administrativa Especial Oecusse Ambeno - RAEOA		97,756,688	84,436,784	**n/a**	**-14%**
	Ministry of Parliament Affairs and Social Communications	4,534,424	8,013,016	8,013,019	**77%**	**0%**
INFRASTRUCTURE DEVELOPMENT	Ministry of Planning and Strategic Investment	13,029,517	14,833,713	7,875,051	**-40%**	**-47%**
	Ministry of Public Works	143,788,853	234,511,942	157,140,777	**9%**	**-33%**
	Ministry of Transport and Communications	6,524,745	11,806,256	8,568,753	**31%**	**-27%**
ECONOMIC DEVELOPMENT	Ministry of State, Coordinator of Economic Affairs	705,976	1,993,485	1,451,069	**106%**	**-27%**
	Secretariat of State for Vocational	3,739,372	5,927,796	4,792,921	**28%**	**-19%**

Sector	Name	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
	Training Policy and Employment					
	Secretariat of State for Cooperative Sector	2,300,860	7,137,481	4,583,667	**99%**	**-36%**
	Secretariat for State for Environment	1,036,702	2,875,000	2,207,756	**113%**	**-23%**
	Ministry of Tourism, Commerce and Industry	4,233,652	11,230,248	13,549,556	**220%**	**21%**
	Ministry of Agriculture and Fisheries	7,046,584	29,479,242	17,544,443	**149%**	**-40%**
	Ministry of Mineral Resources and Oil	27,485,988	79,583,158	24,242,721	**-12%**	**-70%**

Source: General Directorate of Planning and Budget, Ministry of Finance 2021.

For self-funded agencies, the vast majority also see a fall in their budget ceilings when comparing the proposed 2022 budget to the rectified 2021 budget. The only exceptions are Centro de Logistico Nacional (+183%), Commission for Administration of the Infrastructure Fund (FI) (+18%) and National Parliament (+3%).

When comparing to actual 2020 expenditure, nearly all self-funded agencies see a rise, with the only exceptions the COVID-19 Pandemic Management Fund (-84%), National Defence Institute (-32%), Prosecutor-General of the Republic(-6%) and Council for Definitive Delimitation of Maritime Boundaries (-5%).

Table 15: Proposed Allocation to SFAs in GSB 2021, $

SDP Sector	SFA	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
Economic Development	Institute of Support for Enterprise Development (Self-Financed Autonomous with Own Revenues)	667,489	1,228,000	**961,319**	**44%**	**-22%**
	Specialized Agency for Investment (Self-Financed Autonomous with Own Revenues)	649,241	1,036,354	**754,754**	**16%**	**-27%**
	Registry and Business Verification Services (Self-Financed Autonomous with Own Revenues)	920,578	2,303,997	**1,537,259**	**67%**	**-33%**
	Bambu (Self-Financed Autonomous with Own Revenues)	300,754	623,971	**416,420**	**38%**	**-33%**

SDP Sector	SFA	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
	Training Center SENAI (Self-Financed Autonomous with Own Revenues)	272,546	728,762	**543,887**	**100%**	**-25%**
	Centro de Logistico Nacional	887,633	2,338,460	**6,609,345**	**645%**	**183%**
	Autoridade de Inspeção Alimentar e Fiscalização da Atividade Económica, Sanitária e Alimentar (Serviço e Fundo Autónomo)	725,417	1,608,427	**817,820**	**13%**	**-49%**
	Centro Nacional de Emprego e Formação Profissional - Tibar	504,865	1,643,458	**992,594**	**97%**	**-40%**
	Instituto Nacional do Desenvolvimento de Mão-de-Obra	243,037	650,060	**494,529**	**103%**	**-24%**
	Commission for Administration of the Infrastructure Fund (FI)	138,738,092	280,891,554	**332,459,769**	**140%**	**18%**
	General Inspection of Labour		470,472	**423,972**	**n/a**	**-10%**
	East Timor Civil Aviation Authority		879,645	**575,926**	**n/a**	**-35%**
	Instituto para a Qualidade de Timor-Leste		1,378,069	**1,038,658**	**n/a**	**-25%**
Infrastructure Development	Institute for Equipment Management (Self-Funded and Autonomous with Own Revenues)	2,547,426	5,014,481	**2,549,644**	**0%**	**-49%**
	Administration of Ports of Timor-Leste (Self-Funded and Autonomous Service with Own Revenues)	2,004,575	3,896,457	**2,947,650**	**47%**	**-24%**
	National Communications Authority (Self-Funded and Autonomous Service with Own Revenues)	676,182	1,311,118	**841,739**	**24%**	**-36%**

SDP Sector	SFA	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
	Autoridade Nacional Electricidade, IP		443,000	**443,000**	**n/a**	**0%**
	Autoridade Nacional Aqua e Saneamento, IP		556,000	**492,000**	**n/a**	**-12%**
Institutional Framework	Presidency of the Republic	5,143,612	8,461,486	**9,956,413**	**94%**	**18%**
	National Parliament	10,924,505	14,484,066	**14,909,224**	**36%**	**3%**
	Courts	4,439,303	8,388,940	**6,391,277**	**44%**	**-24%**
	Prosecutor-General of the Republic	3,731,314	4,787,430	**3,516,270**	**-6%**	**-27%**
	Anti-corruption Commission	1,096,699	1,783,860	**1,414,230**	**29%**	**-21%**
	Public Service Commission	1,912,814	3,175,411	**2,641,691**	**38%**	**-17%**
	Forensic Police of Criminal Investigation (Self-Financed Autonomous with Own Revenues)	1,421,134	2,035,164	**1,463,893**	**3%**	**-28%**
	National Defence Institute (Self-Funded and Autonomous with Own Revenues)	1,217,180	1,218,155	**829,149**	**-32%**	**-32%**
	National Intelligence Service	1,046,740	1,479,095	**1,158,390**	**11%**	**-22%**
	State Inspectorate General	530,088	997,731	**815,724**	**54%**	**-18%**
	National Institute of Public Administration	470,817	1,097,712	**813,635**	**73%**	**-26%**
	National Electoral Commission	7,778,714	8,368,892	**7,797,516**	**0%**	**-7%**
	Council for Definitive Delimitation of Maritime Boundaries (Administrative and Financial Autonomy without Own Revenues)	823,117	1,043,686	**782,765**	**-5%**	**-25%**
	Agencia de Technologias da Informacao e Comunicacao Timor I.P.		4,014,802	**1,737,281**	**n/a**	**-57%**
	National Center Arrives		3,165,703	**2,456,571**	**n/a**	**-22%**

SDP Sector	SFA	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
	Imprensa Nacional de Timor-Leste, I.P.		447,822	**362,006**	**n/a**	**-19%**
	TATOLI - Agência Noticional de Timor-Leste, I.P.		679,992	**447,806**	**n/a**	**-34%**
Social Capital	National University Timor Lorosae (Self-Financed Services with own revenues)	12,917,890	19,054,500	**16,514,893**	**28%**	**-13%**
	Archive and Museum Resistência Timorense	1,133,938	2,476,356	**1,681,767**	**48%**	**-32%**
	Press Council (Self-Financed Autonomous with Own Revenues)	524,927	977,448	**766,285**	**46%**	**-22%**
	National Hospital Guido Valadares (Self-Financed Autonomous with Own Revenues)	7,105,334	10,700,915	**10,063,485**	**42%**	**-6%**
	SAMES (Self-Financed and Autonomous with Own Revenues)	6,690,191	10,740,000	**7,966,000**	**19%**	**-26%**
	National Laboratory (Self-Funded and Autonomous with Own Revenues)	533,462	854,310	**732,685**	**37%**	**-14%**
	National Center for Rehabilitation (Self-Funded and Autonomous with Own Revenues)	586,203	1,200,000	**905,750**	**55%**	**-25%**
	Agência Nacional para Avaliação e Acreditação Académica (Autonomia Administrativa e Financeira com Receitas Próprias)	205,304	426,865	**271,426**	**32%**	**-36%**
	Institute of Health Sciences (Autonomia Administrativa e Financeira com Receitas Próprias)	376,825	1,222,500	**948,392**	**152%**	**-22%**

SDP Sector	SFA	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
	Commission for Administration of the Human Capital Fund (FDCH)	8,849,610	12,995,000	**10,000,000**	**13%**	**-23%**
	National Institute of Sciences and Technology		573,591	**417,324**	**n/a**	**-27%**
	Politecniko Betano Institute		1,340,925	**1,146,441**	**n/a**	**-15%**
	COVID-19 Pandemic Management Fund	194,689,088	287,641,793	**30,274,786**	**-84%**	**-89%**
	Servisu Nasional Ambulansias no Emerjensia Medika		950,000	**615,141**	**n/a**	**-35%**

Source: General Directorate of Planning and Budget, Ministry of Finance 2021.

Regarding municipalities, all see a reduction in comparison to the current year budget with the largest fall for Administração Municipal de Viqueque (-19%) and the smallest Administração Municipal de Aileu (-10%). However in comparison to actual spending in 2020, all municipalities see significant rises. The Autoridade Municipal de Ermera has the largest increase (+ 78%) while the smallest rise is Autoridade Municipal de Dili (+40%).

Table 16: Proposed Allocation to Municipal Authorities, $

Municipal Authority	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
Administração Municipal de Aileu	1,641,520	3,015,344	**2,701,414**	**65%**	**-10%**
Administração Municipal de Ainaro	1,866,285	3,407,826	**2,906,048**	**56%**	**-15%**
Administração Municipal de Covalima	2,062,047	4,414,282	**3,652,651**	**77%**	**-17%**
Administração Municipal de Lautém	2,320,098	4,157,022	**3,499,510**	**51%**	**-16%**
Administração Municipal de Liquiçá	1,613,606	3,329,831	**2,846,751**	**76%**	**-15%**
Administração Municipal de Manatuto	2,093,441	4,338,238	**3,502,252**	**67%**	**-19%**
Administração Municipal de Manufahi	2,068,132	3,766,851	**3,277,950**	**58%**	**-13%**
Administração Municipal de Viqueque	2,146,193	4,337,502	**3,531,666**	**65%**	**-19%**
Autoridade Municipal de Baucau	2,957,988	5,309,123	**4,355,085**	**47%**	**-18%**
Autoridade Municipal de Bobonaro	2,477,479	5,002,575	**4,264,034**	**72%**	**-15%**
Autoridade Municipal de Dili	5,203,552	8,667,122	**7,279,981**	**40%**	**-16%**
Autoridade Municipal de Ermera	2,248,300	4,605,438	**3,995,639**	**78%**	**-13%**

Source: General Directorate of Planning and Budget, Ministry of Finance 2021.

When looking at the budget composition, it is possible to see the total percentage of the budget allocated to Line Ministries has increased compared to the previous year, with the main beneficiaries Appropriations for all of Government, the Ministry of National Liberation Combatants Affairs, Autoridade Região Administrativa Especial Oecusse Ambeno – RAEOA, Ministry of Health and Ministry of Interior. The budget allocation for municipalities also rose, with most of the decline targeted at total government expenditure on self-funded agencies.

Table 17: Comparison of 2020 Expenditure, proposed 2021 GSB and proposed 2022 GSB by Budget %

Name	**Actual 2020**	**Supplementary 2021**	**Proposed 2022**	**Change from 2020 Actual**	**Change from Supplementary 2021**
Secretariat of State for Equality and Inclusion	0.1%	0.1%	0.1%	**0.0%**	**0.0%**
Ministry of Health	3.5%	2.8%	3.2%	**-0.3%**	**0.4%**
Ministry of Education, Youth and Sports including SEJD	6.5%	5.2%	5.2%	**-1.3%**	**0.0%**
Secretariat of State for Youth and Sport	0.2%	0.4%	0.4%	**0.1%**	**0.0%**
Ministry of Higher Education, Science and Culture Including SEAC	0.4%	0.3%	0.3%	**-0.1%**	**0.0%**
Ministry of Social Solidarity and Inclusion	4.7%	1.0%	1.2%	**-3.5%**	**0.2%**
Ministry of National Liberation Combatants Affairs	8.6%	4.9%	5.6%	**-3.0%**	**0.7%**
Prime-Minister	0.6%	0.6%	0.5%	**0.0%**	**-0.1%**
Minister of State for the Presidency of the Council of Ministers	0.3%	0.2%	0.3%	**-0.1%**	**0.0%**
Ministry of Finance	1.2%	1.6%	1.6%	**0.4%**	**0.0%**
Appropriations for all of Government	5.0%	10.5%	15.9%	**10.8%**	**5.3%**
Ministry of Foreign Affairs and Cooperation	1.8%	1.3%	1.4%	**-0.3%**	**0.1%**
Ministry of Justice	1.0%	0.7%	0.8%	**-0.3%**	**0.0%**
Ministry of State Administration	1.3%	2.5%	2.9%	**1.6%**	**0.4%**
Ministry of Defense	1.8%	0.6%	0.6%	**-1.3%**	**-0.1%**
Ministry of Interior	4.1%	0.9%	1.3%	**-2.8%**	**0.4%**
Ombudsman for Human Rights	0.1%	0.1%	0.1%	**0.0%**	**0.0%**
F-FDTL	0.0%	1.2%	1.3%	**1.3%**	**0.1%**
PNTL	0.0%	1.7%	1.8%	**1.8%**	**0.1%**
Autoridade Região Administrativa Especial Oecusse Ambeno - RAEOA	0.0%	4.8%	5.4%	**5.4%**	**0.6%**
Ministry of Parliament Affairs and Social Communications	0.4%	0.4%	0.5%	**0.1%**	**0.1%**
Ministry of Planning and Strategic Investment	1.1%	0.7%	0.5%	**-0.6%**	**-0.2%**
Ministry of Public Works	12.7%	11.6%	10.0%	**-2.7%**	**-1.6%**
Ministry of Transport and Communications	0.6%	0.6%	0.5%	**0.0%**	**0.0%**
Ministry of State, Coordinator of Economic Affairs	0.1%	0.1%	0.1%	**0.0%**	**0.0%**

Name	Actual 2020	Supplementary 2021	Proposed 2022	Change from 2020 Actual	Change from Supplementary 2021
Secretariat of State for Vocational Training Policy and Employment	0.3%	0.3%	0.3%	**0.0%**	**0.0%**
Secretariat of State for Cooperative Sector	0.2%	0.4%	0.3%	**0.1%**	**-0.1%**
Secretariat for State for Environment	0.1%	0.1%	0.1%	**0.0%**	**0.0%**
Ministry of Tourism, Commerce and Industry	0.4%	0.6%	0.9%	**0.5%**	**0.3%**
Ministry of Agriculture and Fisheries	0.6%	1.5%	1.1%	**0.5%**	**-0.3%**
Ministry of Mineral Resources and Oil	2.4%	3.9%	1.5%	**-0.9%**	**-2.4%**
Total Line Ministries	**60.2%**	**61.7%**	**65.6%**	**5.4%**	**3.9%**
Total SFA	**37.3%**	**35.6%**	**31.5%**	**-5.8%**	**-4.2%**
Total Municipalities	**2.5%**	**3%**	**2.9%**	**0.4%**	**0.2%**
Total	**100.0%**	**100.0%**	**100.0%**	**0.0%**	**0.0%**

Source: General Directorate of Planning and Budget, Ministry of Finance 2021.

7 Loans and Public Private Partnerships

7.1 Loans

The Government currently still depends on foreign loan to meet its borrowing needs for concessional loans. As established in the Strategic Development Plan 2011-2030 and regulated by public debt regime law No.13/2011, the primary objective of taking concessional loans should be related to the construction of strategic infrastructure for the development of the country.

7.1.1 Terms of Loans

At present, external loans are mainly provided by international multilateral banks such as Asian Development Bank and World Bank including one bilateral loan from JICA. By creditor category, ADB is currently the major lender to TL and its loans accounts for nearly 53% of the total loan amount followed by WB and JICA. Below are the terms of the loans:

Table 18: Terms of Loans

Creditor	Currency	Approved loan (million USD)	Grace Period (year)	Initial Amortization (year)	Year Complete	Interest rate FY 2020
ADB	USD, SDR	271.65	5.3	20	2044	1.89%
WB	USD, SDR	174.20	8	20	2060	2.72%
JICA	JPY	68.72	10	20	2042	0.71%
Total		**514.58**				

Source: DNPME, Ministry of Finance, June 2021.

These are loans that have a considerable degree of concessionality and compare favourably to the opportunity cost of withdrawing funds from the petroleum fund. A key advantage is that the financial cost of concessional borrowing (2.03%) is currently lower than the return on the Petroleum Fund (4.84%) ensuring that the future debt repayments remain well within the country's capacity to pay.

Table 19: **Cost of borrowing vs PF return**

Description	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
Cost of borrowing (effective rate)				1.02%	1.42%	1.68%	2.06%	2.34%	2.03%
PF historical return	4.1%	4.4%	4.2%	3.8%	3.8%	4.4%	3.8%	4.5%	4.84%

Source: DNPME, Ministry of Finance, June 2021.

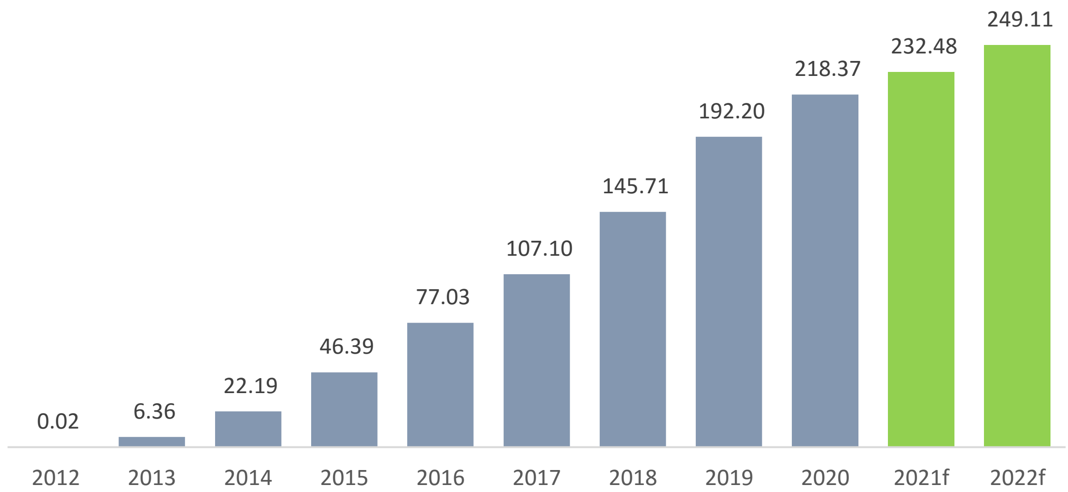
7.1.2 Portfolio Management

The management of public debt plays a critical role in determining the sustainability of fiscal policy. Due to poor macro-fiscal outlook, TL's debt carrying capacity is now rated lower than previous year by the IMF article IV mission held in 2021 from medium to weak leading to lower debt burden thresholds. Similarly, risk of external debt distress was also increased from low to moderate.

Changes in External Debt Stock

As end of the fiscal year, the stock of external debt increased to USD 218.37m in 2020 from $192.20 at the end of 2019. The 14% increase is attributable to the total new disbursement of $30.10m from multilateral and bilateral institutions including ADB, WB and JICA for ongoing and new projects. Interest and other fee related payments declined slightly from $3.93 in 2019 to $3.90m as at end of 2020. This amount is relatively small compared to the amount currently the Government owes to these lenders.

Figure 48: Stock of External Debt, $ millions



Source: DNPME, Ministry of Finance, June 2021.

Considering the impact of Covid-19 outbreak, particularly delaying a number of key capital projects, a fall in disbursements is expected in 2021. Compared with the previous year, disbursement in 2021 is expected to fall by 27%. However a slight recovery is expected in 2022, with loan disbursements forecast to reach $30 million, making the total debt stock estimated to be $249.11 million by the end of 2022.

Debt Indicators

TL's debt ratios increased over the years, marginally. Despite this, total public debt remained sustainable over the year reflecting the Government's prudent management of the debt.

Table 20: **External Debt Indicators for the period 2016-2021, % of GDP and Revenue**

External Debt Indicators for the period 2016-2021
(In percent of GDP and Revenue)

Total Debt to GDP (%)	**2016**	**2017**	**2018**	**2019**	**2020f**	**2021f**
External Debt to GDP	3.07	6.78	9.32	12.07	14.85	15.27
Total Debt Service to Revenue						
External Debt Service to Revenue	0.07	0.27	0.42	1.00	0.97	2.05
External Debt Service to GDP	0.03	0.11	0.20	0.45	0.53	1.03

Source: DNPME, Ministry of Finance, June 2021.

External Debt to GDP - The size of external debt to GDP during the period was relatively small when compared to the debt burden threshold and benchmarks as established under the debt sustainability frameworks for low income countries[4]. While the ratio constantly increased marginally from 3.07% percent in 2016 to 15.27 percent in 2021, the values are far below 30%. This marginal increase was due to an increase in disbursement and external downward growth trend in GDP. While there was a slight recover during 2017-2018, the percentage increase in external debt was still higher than GDP growth, hence, higher external debt to GDP ratio.

Debt Service to Revenue – The debt service to revenue ratio started to increase more than two times in 2015. This increase was primarily due to an increase in debt service payments while revenue declined from 2017-2018. Repayment of principal started in September 2017 for ADB loan 2857. Despite the increase from 0.97 in 2020 to 2.05 percent in 2021, this percentage of debt service to revenue is still well-under the threshold 14 percent.

Debt Service Forecast – Annual debt service is calculated on each loan to cover the repayment of principal, interest and other miscellaneous charges on a debt for a particular period.

Table 21: **Debt Service Forecasts, $m**

Year	**2021**	**2022**	**2023**	**2024**	**2025**
Debt Service	15.61	19.29	23.12	24.44	25.63

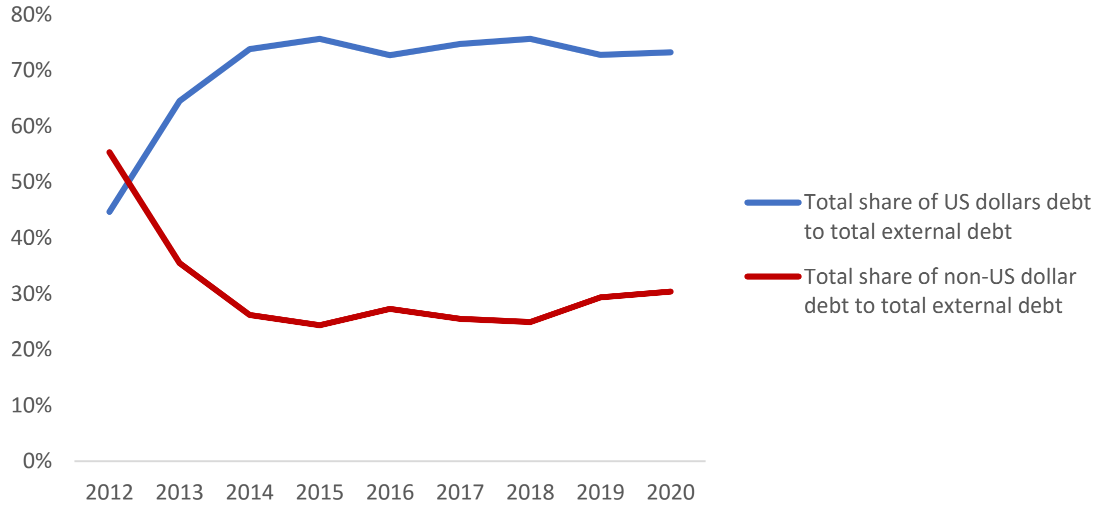
Source: DNPME, Ministry of Finance, June 2021.

Risk Indicators

Foreign Exchange Risk – Complying with the loan policy note, the US dollar has remained the dominant currency in the Government's external debt portfolio. Given the country's highly dollarized economy, the large share of US dollar currency debt in the portfolio 73 percent in 2020 cushioned the Government from extreme exchange rate movements. The policy to retain a larger share of US dollars debt continues at least in the short to medium term.

[4] Further reference on this subject: "Guidance Note the Bank-Fund Debt Sustainability Framework for Low Income Countries", February 2018.

Figure 49: US dollars debt vs non-US dollars Debt

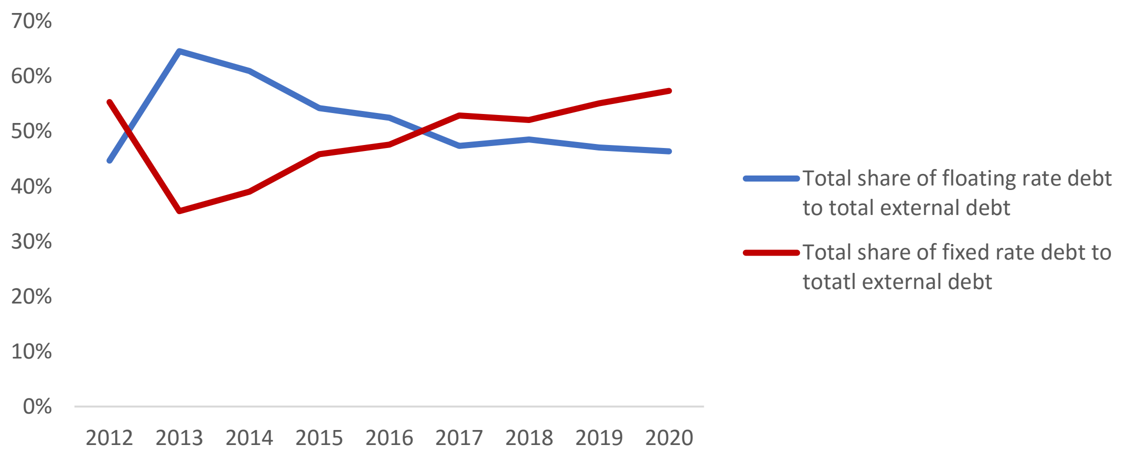


Source: DNPME, Ministry of Finance, June 2021

Interest rate risk – From 2013, the total share of fixed rate debt started to increase until it comprised the majority share of the debt portfolio, in 2017 and 2018 consecutively. The change occurred as a result of the ability of the Government in managing interest rate risk independently by converting the priority for disbursement from variable rate to fixed rate taken into account market interest rate fluctuation.

The cost of borrowing is expected to continue to rise as TL is now classified as a blend country[5] and is slowly being phased out from concessional financing by its external creditors. To limit the exposure to interest rate shocks, there needs to expand the use of more concessional financing from bilateral loan providers.

Figure 50: Fixed vs Floating Debt



Source: DNPME, Ministry of Finance, June 2021.

[5] Being a blend country, TL has a limited access to concessional lending with a fixed interest rate.

7.1.3 Current Project Status

There are currently 15 ongoing road projects funded by concessional loans of which 9 projects had already been completed. These include roads connecting Tibar-Liquica/Tibar-Gleno, Manatuto-Laclubar junction, Laclubar junct.Natarbora, Manatuto-Baucau, Solerema-Ainaro corridor and Hera-Manatuto. Other projects that most likely to be concluded by 2020/2021 are roads from Tasitolu-Tibar,Baucau-Lautem, and Maubara-Karimbala+ Atabae- Motaain , bringing the total numbers of projects completion to 80% by end the year.

Total capital contribution made by this investment is 429.85 m which is by a ratio of total investment, concessional loans accounted for approximately 63%. Of this, $185.61 m has been disbursed leaving a balance of $80.79 m to be spent for next 1-2 years in accordance with project construction periods. On the other hand, state contribution to the overall budget of Civil Works contract was $163.45m with an estimated remaining $35.08 for further disbursement.

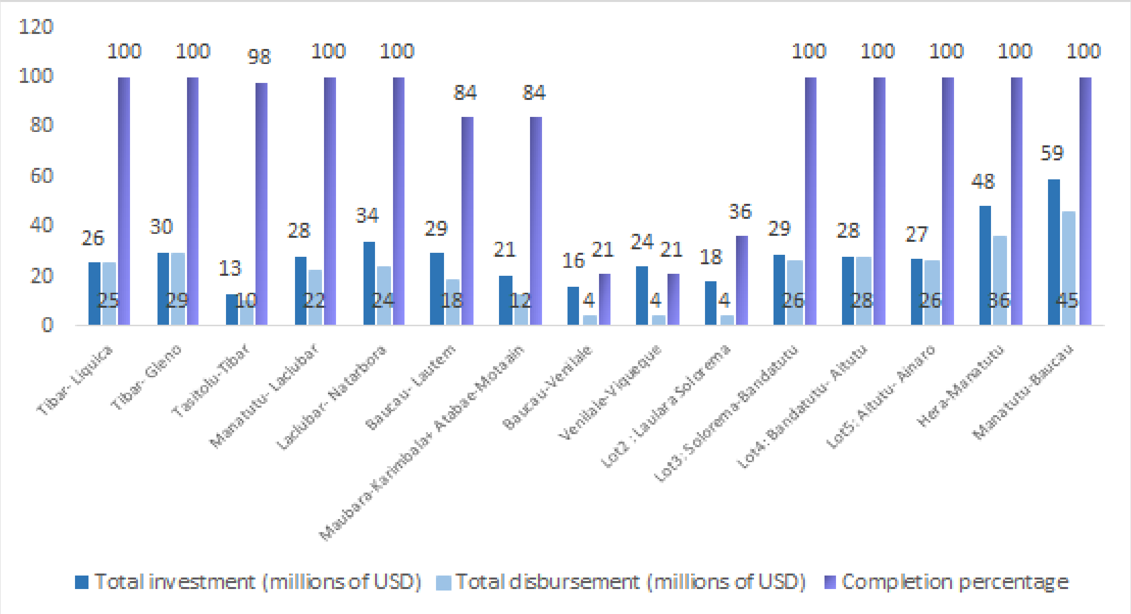
New projects included Gleno-Letefoho-Hatubuilico road section, Water Supply and Sanitation for Baucau municipality and Basic Education Strengthening and Transformation (BEST). The key challenges in project implementation were mainly relating to the release of social safeguard documents by relevant line ministries including delay in environmental licensing and resettlements and payment delays. As for the latter, it explained the trends illustrated in the graph below, in which projects progress was relatively high, in comparison to disbursements.

Table 22: Total investment in Civil Works

Source of Fund	Total Investment in Civil Works (USD million)	Disbursement as at 30 June 2021(USD million)	Contract Balance (USD million)
Loan Fund	266.40	185.61	80.79
State Contribution	163.45	128.36	35.08
Total	**429.85**	**313.98**	**115.89**

Source: DNPME, Ministry of Finance, June 2021.

Figure 51: By Project, Civil Works Progress as at June 2021, Disbursement, and Contract Price



Source: DNPME, Ministry of Finance, June 2021.

There is about $40 million loan saving from ADB ongoing loan -funded projects. The cost reduction increases year by year as a result of the number of participating bidders also increases in public procurement; hence, bringing down the co prices . This includes surplus in civil works, consulting services and unallocated loan contingencies. By projects, Baucau-Lautem/Maub-Karim/Atab-Motain contributed over $20.04 in saving while other projects such as Manatuto-Natabora, Baucau-Viqueque, Manatuto- Baucau, and Tacitolu-Tibar accounted for the remaining balance.

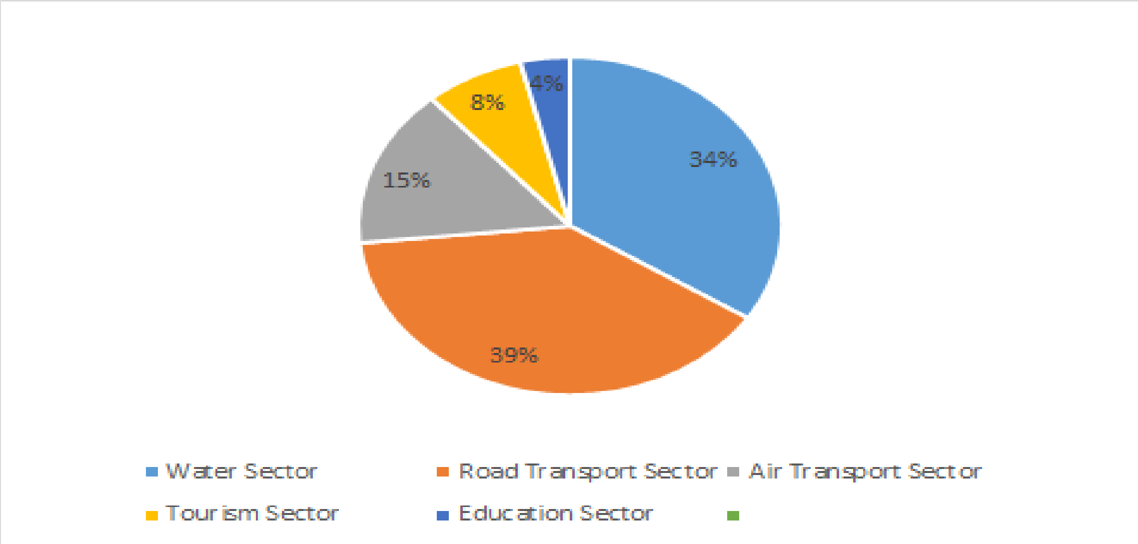
As a borrower, the Government can decide whether to fully utilise the saving or simply cancel the amount by complying with public debt law No.13/2011 and other relevant laws. For this purpose, the Government has already requested ADB to maximise the use of some of this saving to fund for the construction of three (3) bridges: Seical Bridge, Borouai causeway and Malailada causeway with a total estimated cost at $14m a long Baucau-Lautem road section and mitigate the pressure on the state budget. Some amount have also been allocated to pay for detailed design for Lospalos –Viqueque road section project.

7.1.4 Future Loans

Infrastructure development would remain to play a key role in the country's economic development success in the medium term. New strategic sectors such as water, education, telecommunication, and air transports should receive concessional financing. This would help unleash the growth potential of other key economic activities; hence, inclusive economic growth and poverty reduction.

In this respect, annual loan ceiling is required for parliamentary approval, in the context of the State Budget Law, prior to implementing all these programs. The amount is set according to project cost estimates and debt sustainably analysis. On the DSA, based on the MOF internal analysis, the country's external debt stock to GDP remained relatively low in 2018 which is 9.2%. IMF staff completed the country's 2019 article IV consultation by stressing the need for making effective use of concessional borrowing for continued investment in infrastructure. In light of all the above, the Government is therefore, proposing a ceiling of $395m for new concessional foreign loans to be negotiated in 2022.

Figure 52: Sectoral Allocation of Proposed Loan Ceiling for 2022



Source: DNPME, Ministry of Finance, June 2021.

7.2 Public Private Partnerships

7.2.1 Overview of Public Private Partnerships in Timor-Leste

In general terms, the Public Private Partnership (PPP) refers to arrangements in which the private sector build infrastructure assets and provides services that traditionally have been provided by the State.

DL 8/2014 stipulates the formation of PPPLU, a PPP facilitation agency under the Ministry of Finance to take on the tasks of managing and implementing the PPP Project Cycle in coordination with line ministries and Council for Administration of Infrastructure Fund (CAFI). An important role of the PPPLU is to promote and create environment for attracting foreign direct investment (FDI) through PPP modality, while at the same time looking for ways of encouraging local private sector involvement in PPP projects by pursuing policies that will allow for development of small to medium scale PPPs. One Sector that have high potential for this is the Tourism Sector.

Tourism is thought to be one of several strategic sectors with potential to further diversify Timor-Leste's economy. Due to its close linkages to other sectors, improvement to the tourism sector requires wide range of intervention, e.g. in transport infrastructure, water and sanitation, agriculture, health infrastructure and education and training.

7.2.2 Existing PPPs Projects

Currently, one PPP project is in **Implementation and Operation Stage** (Tibar Bay Port PPP), one in **Procurement and Negotiation Stage** (Medical Diagnostics) while others are in **Feasibility Stage** (Affordable Housing, Cristo Rei and Presidente Nicolau Lobato International Airport).

Tibar Bay Port PPP Project

The PPP modality chosen for Tibar Bay Port was a 30-year concession, including the design, partial financing, construction, operation and maintenance of the port infrastructure. The project was awarded to a consortium comprised by Bolloré Africa Logistics and SDV East Timor through an international competitive bidding which formed Timor Port SA (Concessionaire) to implement it.

The concession agreement was signed on 3rd June 2016 between the GoTL and the TPSA and the concession was awarded for 30 (thirty) years including a construction period which started on 30 August 2018 and expected to be completed by May 2022. The construction progress until end of May 2021 was 52.99%.

The Environmental License was awarded on 15 March 2018 and currently extended until 15 March 2022. So far there is record of environmental impacts resulting from the construction of Tibar Port.

The capital expenditure of the Phase-I is around USD 300 million. The Concessionaire will fund the majority of the amount by means of equity and debt and the GoTL has allocated an amount of USD 129, 45 million as Viability Gap Funding (VGF) to the Concessionaire. Until end of June

2021, the total amount disbursed from VGF was USD 64.72 million and total expenses of the project was USD 148.73 million.

Medical Diagnostics PPP

Medical diagnostics PPP is currently in preparation of tender documents and other necessary structures (e.g. accessible data room) which are the early steps in the **Procurement and Negotiation Stage**. Previously, the Feasibility Study and Transaction Structuring Report (TSR) have been approved by CAFI on 11 July 2019 after clearance from the Ministry of Health in June 2019. The TSR recommended that the project upgrade imaging and laboratory diagnostic services in the National Hospital, all referral hospitals and 8 Community Health Centres (CHCs) to achieve a demand coverage of 98.2% of the total population. Concession period is recommended at 11 years to consist of 1 year of upgrading and construction of selected facilities and 10 years operation period. Potential bid parameter and bid evaluation criteria have also been recommended. The estimated Government contribution will be about USD 10 million during initial year of operation and maintenance and will increase up to USD 17.9 million in the year 3 of the project to achieve coverage of the population in the territory of Timor-Leste. It is estimated that the contribution of private sector will be around USD 11 million for the upgrading or construction of facilities, operate and maintain Laboratory and Imaging centres and provide quality diagnostic services to patients in Timor-Leste. In addition, private sector also will employ and train diagnostic services staff, comply with local regulation and international best practices in health care service delivery. Signing the extension of Financial Advisory Service Agreement between GoTL and IFC have completed. Both parties are now adjusting their work program and timetable for the finalization of the project accordingly.

Affordable Housing

With the signing of FASA agreement between the Government and IFC in December 2020, the Affordable Housing PPP is now undergoing the Feasibility Study and Transaction Structuring phase. The IFC has been able to mobilize its technical, legal, environmental and social safeguarding team for the due diligence study. Currently, works are on-going especially conducted by IFC consultant’s local counterpart for data collection. Site for the project has been secured and assigned for the affordable housing project to Ministry of Public Works.

Affordable housing under a PPP model has been proven to be successful in several countries. Under a PPP modality, the Government is usually responsible for the provision of land and trunk infrastructure while private developer takes the responsibilities of the design, finance and construction of the housing project. Depending on the revenues expected to be generated from the sale of the property, upfront Government subsidy and/or a cross subsidy from provision of developer-owned areas may be needed to ensure bankability and private sector interest in the project. Full or partial amount of the upfront subsidy can later be recovered through sale of the Government-owned units. The transaction structure with potential fiscal impacts to the Government will be clearer once the results of feasibility study are available.

Cristo Rei PPP

In 2020, DNPPP with assistance from development partner, in this case, USAID’s Tourism for All (TFA) is embarking in a small and medium sized PPP undertaking in the Tourism sector, the Cristo Rei PPP. Cristo Rei is a government asset which is also the icon of the City of Dili and one of the most visited tourism sites in the country. It is also a popular destination among visitors coming from through cruise ships which started to make the call to Dili since 2016.

The objective of Cristo Rei PPP is the creation of a destination to relax and enjoy views for tourists, religious pilgrims, runners and walkers as well as family picnickers. Pre-Feasibility study for this project was finalized in 2020 and approval of CAFI to enter into the PPP project cycle was secured in November 2020. The project is currently in Feasibility Study and Transaction Structuring phase with preliminary results already shared to members of Project Evaluation Team (PET) in July 2021.

Presidente Nicolau Lobato International Airport Development

The Master Plan for the development of Presidente Nicolau Lobato International Airport Development ("the Airport") was approved in October 2019 by the Council of Ministers (CoMs). The implementation of the project has been initiated following the approved Hybrid PPP modality which deems as the combination of investment between public through engineering procurement and construction and private through PPP partner participation. The key components of the Airport includes **(i)** the extension of runway of 2.1 km, aprons, parallel taxiways and control tower; **(ii)** passenger terminal; **(iii)** VIP terminal and **(iv)** other support infrastructures. The project involves multiple stakeholders such as Asian Development Bank (ADB), International Finance Corporation (IFC), Department of Foreign Affairs and Trade (DFAT) and World Bank (WB).

The Feasibility study for several airport key components such as runway, aprons, parallel taxiways and control tower have been completed, and this will be financed through ADB loan of $165 million inclusive Government Timor-Leste (GovTL) counterpart. The loan negotiation between GovTL and ADB has been concluded in May 2021, and it is expected to be signed in August 2021. The project is now reaching the preparatory work for the procurement of Design-build (DB) contractor, Project Management Consultancy (PMC) and Construction Supervision Consultant (CSC). In parallel, the feasibility study for development of the Airport according to Financial Advisory Service Agreement (FASA) between IFC and GovTL, is currently achieving the transaction structuring report stage in which GovTL will decide the suitable PPP option that meets GovTL's aspiration prior to tender. As for the passenger terminal, the preparatory study will be initiated once the loan agreement is signed between GovTL and ADB and the financing for this component will be through grant of $44 million from JICA. Other support facilities are on discussion with DFAT and World Bank with good progress.

Another important aspect is Land Acquisition, Compensation and Support Plan (LACSP) in which the data collection and verification for phase 1 have been completed and approved by the Inter-ministerial Commission (IMC). Several LACSP's related activities need to be completed prior to execution and payment which is anticipated to fall in mid Q3 2021 and terminate in Q1 2022.

Dili Port PPP

Another recent initiative which is currently in preliminary stage is Dili Port PPP or also known as Dili Port Redevelopment and Commercialization. Upon the start of operation of Tibar Bay Port, which is planned for May 2022, handling of all international cargo will need to move to Tibar Bay Port. As such, Dili Port will be vacant and will solely be used for the handling of domestic cargo and passenger port.

Dili Port is a historic as well as prime site within Dili. The port and its surrounding areas are centrally located and an icon of the wonderful waterfront that define the City of Dili. Moving the handling of international cargo away present an opportunity to revitalize the area while also realizing the many potentials that the City has in terms of coastal tourism. For example, before it was closed due to Pandemic, the trend for cruise ship calling to Dili is in the upswing with numbers of passengers making landing to Dili increase from 2022 in 2016 to 3467 and 6172 in 2018 and 2019 respectively. Other potential activities that can be pursued is Dili becoming host to international yacht race as well as other marine tourism excursions such as whale and dolphin watching and others.

As a historic site, on the other hand, the development of Dili Port should be planned carefully as not to ruin its characters. Currently, the project has been prepared with the following objectives:

(ii) Matching the project "vision" with the site development potential and market opportunities;

(iii) Maximize the waterfront as a commercial, residential, recreational and cultural hub for residents and tourists;

(iv) Create a mixed-use urban cluster with job creation and economic growth dynamics; and

(v) Remain consistent with APORTIL's port operation and transportation mandate.

New PPP Initiatives

DNPPP will continue to take the lead in the monitoring and preparation of viable PPP projects while pursuing strategic policies that will open space for the involvement of national private companies in future PPPs especially for small and medium sized PPP projects in certain sector found to be conducive for such undertaking. This policy is pursued within the context of economic diversification where sectors such as tourism become one of Government priorities. For this purpose amendment to PPP legal framework might be pursued based also on inputs from international consultants especially those working on tourism PPP. The aim is to create a simpler yet still robust preparatory regime for small and medium sized projects focusing on quality projects with clear feasibility that will contribute to economic diversification in the country. Analysis of the projects will still focus on **Value for Money** for Government's investment in the projects. Close coordination will continue to be pursued with relevant line ministries on the new initiatives.

7.2.3 Budget Estimate

Tibar Bay Port PPP project involved the provision of Viability Gap Funding (VGF) of $129.5m in 2016 (recorded as 2016 expenditure) for earthwork, construction and equipment purchase. Private sector contribution to this project is around $153.87m meaning that the Government's VGF contribution stood at about 45% of total project cost.

To hold the VGF until disbursement, the Government was contractually required to deposit the full amount in an Escrow Account. For this purpose, a three party Escrow Agreement was reached between the Government, Timor Port SA and the United Overseas Bank (UoB) of Singapore in November 2016. First disbursement from the Escrow Account occurred in the third quarter of 2019.

The Escrow Account is earning interests. As of June 2021, interest earned amounted to **$8.63m**, deposited in the Escrow Interest Account. The Escrow Agreement stipulated that the interest earned can only be transferred to the Government after the closing of the account and/or termination of the Escrow Agreement.

Actual expenditure for 2017, 2018, 2019 and 2020 for PPP projects consisted of budget for the DNPPP and Tibar Bay Port Project Management Unit (TBP PMU), payment of Financial Advisory Service Agreement for TBP PPP, medical diagnostics and Dili water supply PPPs, payment for Independent Engineer service as well as studies for the development of roundabout for Port access and upgrading of EDTL Liquiça substation for electricity connection to TBP. The 2021 budget contains similar provisions (except for operational Budget of DNPPP and PMU TBP is not reported as it was centralized in the DGCS) with addition including operational budget for IPMU Dili Airport, PMU for Cristo Rei PPP, site clearance for PPP Cristo Rei, capital expenditure for the construction of roundabout, upgrading of EDTL Liquiça substation and Medical Diagnostic service payment.

Estimated budget for 2022 contains a rapid increase due to the inclusion of capital expenditure for the Dili Airport, Affordable Housing and Dili Port PPP Project. In addition, due to the promulgation of Ministry of Finance organic law in 2020, the PPP and Loan programs are now structurally separated national directorates. Therefore, 2021 onward budget for the PPP and Loan has been separated and centralized in the DGCS. In the near future, especially for DNPPP, increase in budget is also projected for 2023 for affordable housing PPP, Dili Airport and Service Payment for Health PPP. New initiatives in transport sectors are likely to require allocation of budgets from 2022 onward.

The following are actual expenditure for 2017 to 2019, estimated expenditure for 2020 and 2021, and estimated budget allocation for 2022 onward.

Table 23: Actual, 2021 Budget and Estimated Budget for 2023 – 2026, $ Millions

	2017 Actual	2018 Actual	2019 Actual	2020 Actual	2021 Est.	2022 Est.	2023 Est.	2024 Est.	2025 Est.	2026 Est.
Combined Sources Budget	**1.21**	**1.28**	**1.55**	**2.81**	**21.88**	**54.72**	**33.37**	**36.34**	**47.4**	**47.4**
Dotação *Todo Governo*										
PMU Cristo Rei Project					**0.02**	**0.14**	0.10	0.10	0.10	0.10
PMU Dili Aipoirt Project					**0.65**	**1.93**	1.85	1.85	1.85	
Medical Diag. – Service Payment					**1.50**	**10.00**	10.00	10.00	17.90	17.90
SUB TOTAL	**0.00**	**0.00**	**0.00**	**0.00**	**2.17**	**12.06**	**11.95**	**11.95**	**19.85**	**18.00**
Infrastructure Fund										
TBP PPP										
PT FASA*	0.15	0.15								
IE* payment		0.31	0.32	0.32	**0.43**	**0.38**	0.21			
Roundabout				0.25	**3.00**	**1.50**				
EDTL substation				0.32	**1.50**	**0.75**				
SUB TOTAL	**0.15**	**0.46**	**0.32**	**0.89**	**4.93**	**2.63**	**0.21**	**0.00**	**0.00**	**0.00**
Medical Diag. PPP										
FS FASA & PT FASA*	0.10		0.20		**0.09**	**0.48**	0.10	0.30	0.30	0.30
IM* payment						**0.30**	0.30	0.30	0.30	0.30
SUB TOTAL	**0.10**	**0.00**	**0.20**	**0.00**	**0.09**	**0.78**	**0.40**	**0.60**	**0.60**	**0.60**
Affordable Housing PPP										
FS *FASA & PT FASA**				0.12	**0.26**	**0.40**	0.15			
Resettlement – Site Clearance						**0.50**				
Construction (VGF)					**0.00**	**2.00**	23.00			
SUB TOTAL	**0.00**	**0.00**	**0.00**	**0.12**	**0.26**	**2.90**	**23.15**	**0.00**	**0.00**	**0.00**
Tourism PPP										
FS, TSR* and Resettlement					**0.11**	**0.30**				
Construction (Capex & Opex PPP Cristo Rei)						**0.15**				
SUB TOTAL	**0.00**	**0.00**	**0.00**	**0.00**	**0.11**	**0.45**	**0.00**	**0.00**	**0.00**	**0.00**
President Nicolau Lobato International Airport Hybrid PPP										
FS & TSR*				0.60	0.56					
Runway extension 08/26 east/west- (GovTL counterpart funding to ADB loan)					0.36	**7.64**	7.00	7.00	6.00	2.00
Studies and construction- VIP terminal and its subcomponents (car park)					0.51	**1.00**	2.00	2.50		
Resettlement					5.00	**18.50**	9.10			
Project Management Consultancy (PMC)					0.70	**2.00**	2.00	1.80		
Demolition of existing airport infrastructure						**0.20**	0.20			
Studies & Construction - GSE Service Road, Perimeter Road & Fire Road								0.50	2.50	
Studies & Construction- Cark Parking/drop off zones								0.20	3.00	
Studies & Construction- Fire Fighting Infrastructures								0.20	1.50	
Others Support Infrastructure (Power Supply System, fencing, hangars)						**1.00**	0.50	0.50	0.20	
SUB TOTAL	**0.00**	**0.00**	**0.00**	**0.60**	**7.13**	**30.34**	**20.80**	**12.70**	**13.20**	**2.00**
Transporte PPP										
Restructuring and Commercialization of Dili Port (PPP - FS, TSR, PT and Resettlement - Site clearance)						**0.1**				
Restructuring and Commercialization of Dili Port P - Capex & Opex						**1**	27			
SUB TOTAL	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**1.10**	**27.00**	**0.00**	**0.00**	**0.00**

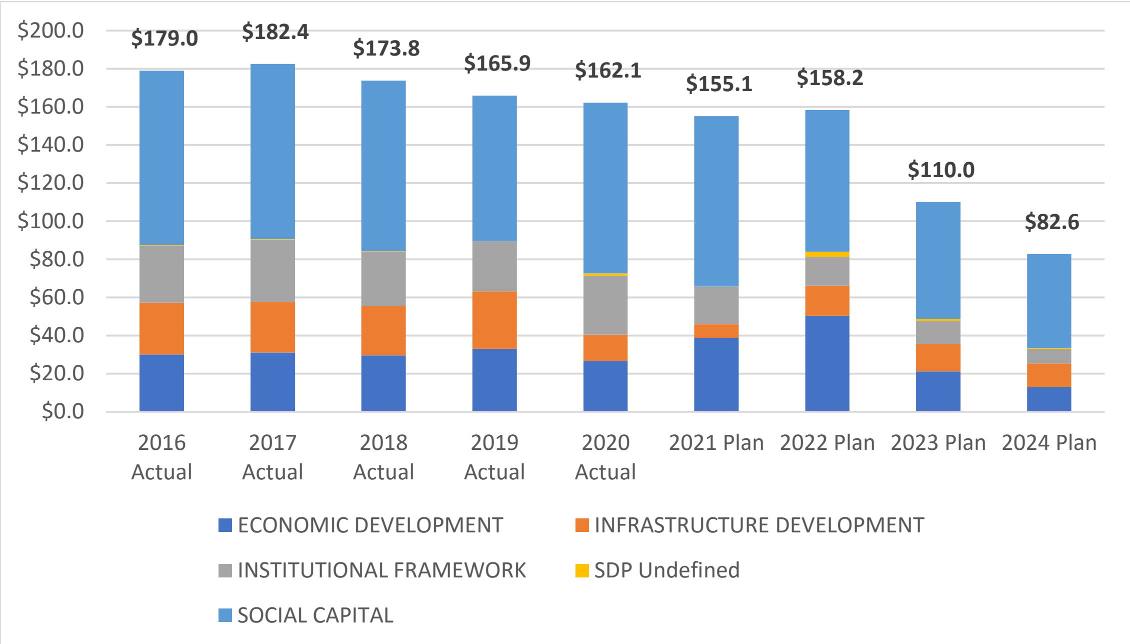
*Source: PPPU, Ministry of Finance, July 2020. PPPU = Public Private Partnership Unit, PMU TBP = Project Management Unit Tibar Bay Port, *PT FASA = Post Transaction Financial Advisory and Service Agreement; IE = Independent Engineer; FS FASA = Feasibility Study FASA; IM=Independent Monitoring; TSR = Transaction Structuring Report.*

8 Development Partners

8.1 Non-lending Forecasts

The graph below shows that there has been a steady decline in donor disbursements from 2017 on, totalling an on average yearly decline of 4.0% from 2017 to 2020. On average, Social Capital represents the highest concentration area of donor support, totalling 50.8% of all actual disbursements during this period. In addition, forward year estimates show a sharp decline in development partner non-lending assistance, however, two important points should be noted: (*i*) historically, development partner multi-year indicative future spending tends to be underreported; (*ii*) the Aid Transparency Portal collects information at the project level, meaning that if funds have not yet been committed to a project they will not be included in the analysis.

Figure 53: 2016-2022 Non-lending Donor Disbursements, $ Millions



Source: Aid Transparency Portal, report generated on July 13, 2021.

Table 24: Planned Disbursements by Donors group for 2022

Donor Group	2022 Planned
Australia	$40,077,243
World Bank	$28,314,075
Portugal	$17,418,957
United Nations	$16,717,412
European Union	$12,254,114
Japan	$11,558,253
United States of America	$8,265,075
Global Fund	$5,000,236
Green Climate Fund	$4,530,502
German Cooperation	$4,039,956
Korean International Cooperation Agency	$3,706,770

New Zealand	$2,829,588
Asian Development Bank	$2,300,000
Global Environment Facility Trust Fund	$1,122,639
TOTAL	**$158,134,820**

Source: Aid Transparency Portal, Ministry of Finance, July 2021.

Table 25: Planned Disbursements by SDP Sub-pillar and Pillar for 2022,

SDP	SDP Sub-pillar	2022 Planned
Social Capital	Education and Training	$31,693,566
	Health	$33,912,847
	Social Inclusion	$6,652,009
	Environment	$2,599,342
	Culture and Heritage	$156,720
Subtotal		**$75,014,483**
Infrastructure Development	Roads and Bridges	$13,322,324
	Sea Ports	$1,207,267
	Water and Sanitation	$704,789
	Electricity	$250,000
Subtotal		**$15,647,908**
Economic Development	Agriculture	$32,971,806
	Tourism	$2,880,804
	Rural Development	$12,760,501
	Private Sector Investment	$1,423,642
Subtotal		**$50,036,753**
Institutional Framework	Public Sector Management and Good Governance	$12,355,306
	Security	$1,184,459
	Justice	$1,741,794
	Foreign Affairs	$506,200
Subtotal		**$15,787,759**
SDP Undefined		$1,647,918
TOTAL		**$158,134,820**

Source: Aid Transparency Portal, Ministry of Finance, July 2021.

Table 26: Top 10 Projects 2019-2020, $ Millions

Project Title	Development Partner	SDP Sub-pillars	2022 Total in USD Millions
Timor-Leste: Sustainable Agriculture Productivity Improvement Project (SAPIP) - P155541 - TF0A2869 & TF0A0236	World Bank	Agriculture	$14.5
Timor-Leste Branch Roads Project (P155203)	World Bank	Roads and Bridges	$11.8
Australia - Timor-Leste Partnership for Human Development - Health Sector	Australia	Health	$10.2
5530-Escola Portuguesa Ruy Cinatti – Centro de Ensino e Língua Portuguesa	Portugal	Education	$8.1
Ai ba Futuru - Partnership for Sustainable Agroforestry Project (PSAF)	GIZ with EU and German Cooperation Funding	Agriculture	$6.9

Project Title	Development Partner	SDP Sub-pillars	2022 Total in USD Millions
Australian NGO Cooperation Program (ANCP)	Australia	-Agriculture -Health -Social Inclusion -Justice -Water and sanitation - Public Sector Management and Good Governance -Education and Training	$6.5
Partnership to Strengthen Village Development and Municipal Administration (PARTISIPA, formerly PNDS-SP)	Australia	Rural Development	$5.3
10383 - Escolas de Referência de Timor-Leste - Centros de Formação	Portugal	Education and Training	$5.1
Governance for Development	Australia	Public Sector Management and Good Governance	$5.0
Safeguarding rural communities and their physical assets from climate induced disasters in Timor-Leste.	UNDP with Green Climate Fund Funding	Rural Development	$4.5

Source: DPMU, Ministry of Finance, July 2021.

8.2 Policy Developments

The global pandemic created a different set of challenges and priorities and in some cases, worked to improve development partner and Government relationships. In response to the crises our nation experienced from the recent flooding and the global pandemic, several development partners sought the most efficient ways to channel their support. In many cases this resulted in funding being channelled directly through Government systems and programs.

It is our hope that this method of delivery of assistance continues into the future. Donors who have made use of this type of assistance include, the Government of Australia, the European Union, the International Labour Organization, and the Asian Development Bank.

8.3 Direct Budget Support

Timor-Leste has been receiving Direct Budget Support (DBS) from the European Union since 2014. The latest agreement was signed in 2016 under the 11th European Development Fund.

EU DBS is considered as a financing for 2021 State Budget because it uses Government system (the money is in a Treasury sub-account) and on-budget, where the money is used directly by the beneficiary ministries for the public financial management program (Ministry of Finance), Malnutrition (Ministry of Health) and decentralization (Ministry of State Administration).

In this context, the funds are directly given to the country's government without prior earmarking. However, a variable tranche depends on specific Key Performance Indicators (KPIs) agreed upon by the Ministry of Finance and the EU. While the funds are not separate or additional to the Ministry's core business, they must support clearly stated priorities and the Ministry's own planning framework.

Total amount of DBS from the EU for 2022 State Budget is currently forecast $8.96 million. Of this, $2,240,000 allocated to Ministry of Heath, $2,800,000 for Ministry of State Administration and $3,920,000 to the Ministry of Finance.

In 2021, the Government of Australia committed to $8.2 million in Direct Budget Support to be allocated over the next two years. The funding is linked to the National Village Development Program (PNDS) and the expansion of the Bolsa Da Mae social assistance programme to include pregnant women and early childhood (Bolsa Da Mae Jerasaun Foun) as approved in the Council of Ministers in February 2021.

The PNDS investment will focus on funding new community investment programmes, particularly those focused on improved sanitation, draining and irrational channels and local road rehabilitation. The Bolsa Da Mae Jerasaun Foun investment will concentrate on directly funding cash transfers as well as supporting the operational costs of the programme delivery. The indicative allocations imply that PNDS will receive $3.3m in 2022 while Bolsa Da Mae Jerasaun Foun will be given $3.3m in 2022 and $1.6m in 2023.

Total amount of DBS for 2022 State Budget is currently forecast at $15.6 million.

9 Public Financial Management

9.1 Program Budgeting

9.1.1 What is Programme Budgeting (PB)?

- Contrary to conventional budgeting, PB describes and gives the detailed costs of every activity or program that is to be carried out with a given budget (1 program will have 1 objective but may have a number of activities in order to achieve that goal). For example, expected results in a proposed program are described fully, along with its necessary resource, raw materials, equipment, and staff costs. The sum of all activities or program constitute the Program Budget. Thus, when looking at a Program Budget, one can easily find out what precisely will be carried out, at what cost and with the expected results.
- One of the key justifications for moving to program or output based budgeting is that traditional budgets are too focused on details and inputs. Budget documentation is often voluminous with many pages of tables detailing inputs for each of the budget entities. Performance based budget systems, on the other hand are designed to shift the focus from 'inputs' to 'outputs' or 'programs' - the services to be delivered by Ministries, the targeted results for these services, and the reporting on these results. In this framework, accountability for the use of government resources (taxpayer's funds) is separated so that:
    - the government becomes accountable for allocating appropriate levels of funding to the ministries to meet the results; and
    - the line Ministries become accountable for the achievement of these results, and the effective management of the inputs entrusted to them by the government through the budget.

9.1.2 History of PB in Timor-Leste

- 2015: The first phase of PB started in TL
- 2015-2019: TL remained still using organic and economic classifications
- 2020: VIII Government presented first GSB in programmatic format
- 2021: Implemented first OJE in programmatic form

9.1.3 Objective to improve Programme Budgeting Structure for GSB 2022

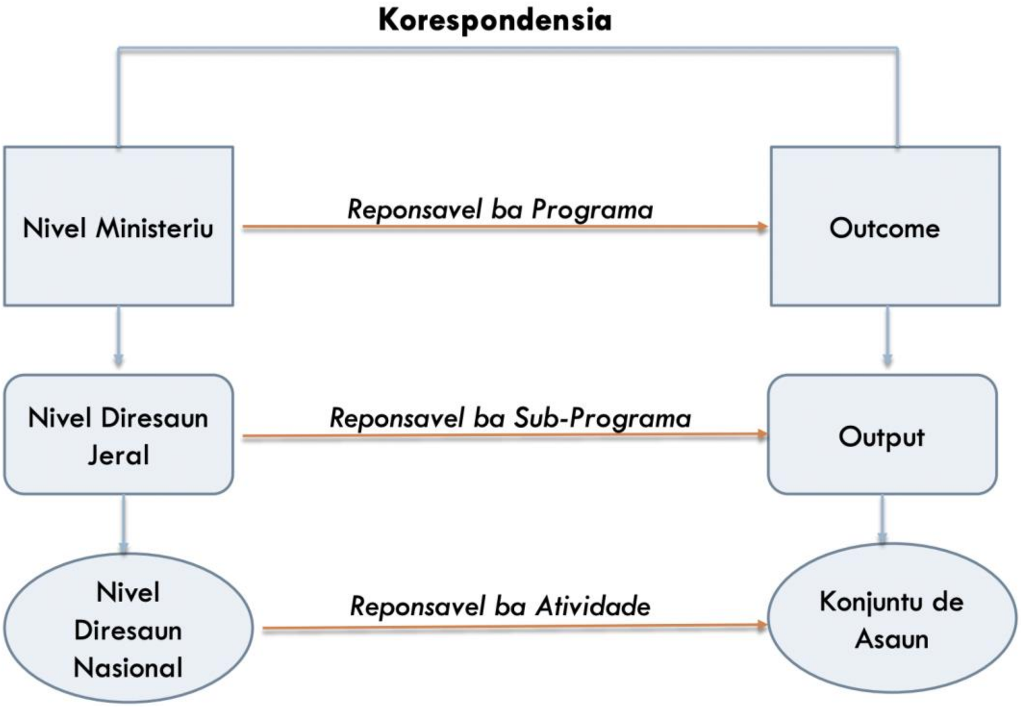
For GSB 2022 the entirety of government activity went through a rationalisation process to reduce the number of programmes from 145 to 43. The purpose of this being to:

- promote strategic investment;
- ensure public services efficient and fair;
- connect the Financial Management Information System (FMIS) system to Dalan Ba Futuru (government system to assist planning, monitoring, tracking and evaluation of public programmes);
- and record objectives,

- impacts and results of public spending;
- ensure monitoring of meeting goals and targets;
- focus based on results rather than execution rates;
- ensure alignment to government priorities;
- move from item budgeting to programme budgeting;
- shift focus onto results rather than execution;
- focus on few programmes to improve on quality and control.

The process for mapping programme structure onto organic structure and reducing the existing 145 to 43 programmes involved connecting the activity to a PED (Strategic Development Plan) subsector, analysing how the PED subsector is connected to LMs or institutions and remapping existing subprogrammes and activities. Municipality programmes and subprogrammes will automatically realign to the relevant ministry based on decree law no. 3/2016 and in line with the decentralisation process. Cross cutting programme include the Good Governance programme which are supported by more than 1 line ministry.

Figure 54: Mapping of Responsibility for Programmes, Sub-Programmes and Activities



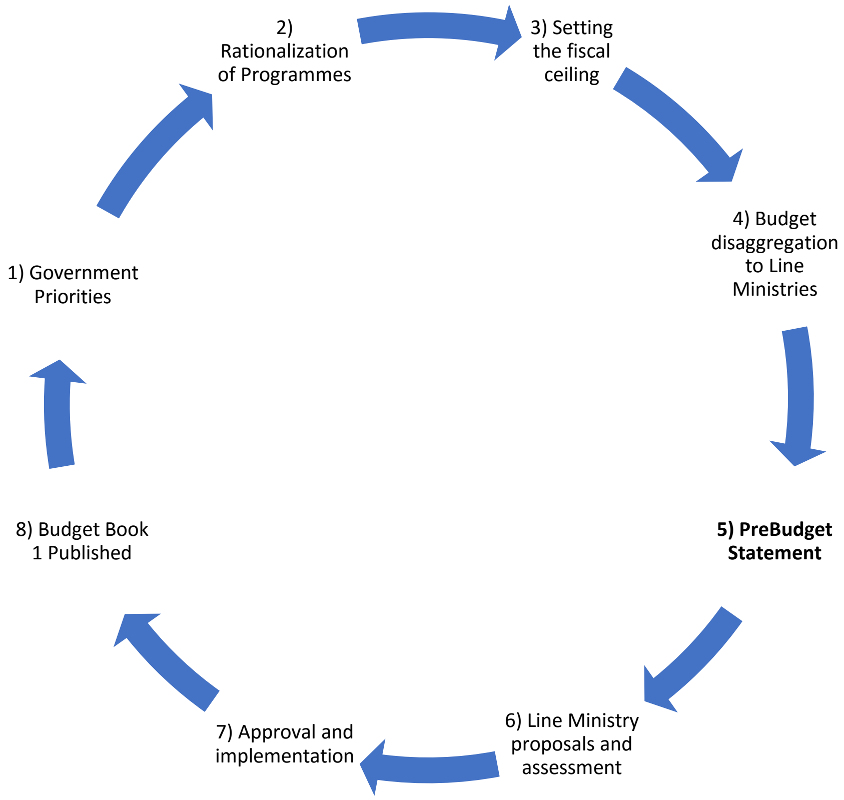
Source: Ministry of Finance & UPMA, June 2021

Table 27: Mapping Programmatic Structure to Organic Structure

ORGANIKA MAXIMU NO ESTRUTURA PROGRAMATIKA	ESTRUTURA ORGANIKA
Ministériu Finansas	
Programa 1	Ministériu
Sub-Programa 1	Diresaun Jerál 1
Atividade 1	Diresaun Nasionál 1
Atividade 2	Diresaun Nasionál 2
Sub-Programa 2	Diresaun Jerál 2
Atividade 1	Diresaun Nasionál 1
Atividade 2	Diresaun Nasionál 2

Source: Ministry of Finance & UPMA, June 2021

Figure 55: Current Budget Cycle



Source: General Directorate of Planning and Budget, Ministry of Finance, August 2021

Table 28: Rationalised List of Programmes for Budget 2022

LISTA PROGRAMA RASIONALIZADU BA OJE 2022	
N.S	KODIGU NO NARAN PROGRAMA
1	Ordenamento do Território e Desenvolvimento Rural e Urbano
2	Cultura e Património
3	Descentralização Administrativa e Poder Local
4	Educação e Formação
5	Estradas e Pontes
6	Finanças do Estado
7	Proteção e Conservação do Ambiente
8	Igualdade de Género e Inclusão Social
9	Investimento e Diversificação Económica
10	Reformas do Estado
11	Telecomunicações
12	Transportes
13	Turismo
14	Contingência
15	Estabelecer o Gabinete das Fronteiras Marítimas como um Centro de Excelência sobre Fronteiras Marítimas e jurisdição marítima de Timor-Leste - Economia Azul
16	Direitos Humanos e Boa Governação
17	Garantir o exercício das funções constitucionais do parlamento
18	Promover uma cultura de abertura e transparência no parlamento
19	Identidade Nacional
20	Estado de Direito Democrático
21	Relação Internacional e diplomática
22	Desenvolvimento Sustentável
23	Aproximar os serviços dos Tribunais da População
24	Dezenvolvimento e reforço de zonas com tratamento administrative e económico especial
25	Assegurar Fronteiras Terrestres e Marítimas permanentes com a Indonésia
26	Formação Profissional
27	Fomentar às relações internacionais e de cooperação do parlamento
28	Treinamento técnico
29	Bolsas de Estudo
30	Outros Tipos de Formação
31	Segurança Nacional
32	Defesa Nacional
33	Acesso à Justiça
34	Política Externa de RDTL
35	Gestão dos Recursos Petrolíferos e Minerais
36	Garantir à liberdade de expressão e acesso à informação

LISTA PROGRAMA RASIONALIZADU BA OJE 2022	
N.S	**KODIGU NO NARAN PROGRAMA**
37	Boa Governação e Gestão Institucional
38	Agricultura
39	Água e Saneamento
40	Energia Elétrica
41	Saúde
42	Aeroporto
43	Portos

Source: Ministry of Finance & UPMA, August 2021

9.2 Public Financial Management

9.2.1 What is Public Financial Management (PFM)?

PFM refers to the set of laws, rules, systems and processes used by sovereign nations (and sub-national governments) to mobilise revenue, allocate public funds, undertake public spending, account for funds and audit results. In simple terms, it's how governments manage public resources. This includes all phases of budgeting, processes and procedures related to expenditure management, resource mobilization, and debt management. It is the framework for governments to consider the medium- to long-term implications of today's policy decisions and assess potential risks. Strong PFM is essential because it boosts the public's confidence and trust in government. Poor PFM allows waste, encourages corruption, reduces the ability to collect taxes, and has an adverse impact on services, the rest of the economy and investor perceptions of the country.

9.2.2 Timor-Leste's PFM priorities Roadmap 2021-2023

The reform of public financial management has been a stated goal for successive national governments in Timor-Leste.

The reform of public finance management will be carried out through financial diversification in the areas of income and expenses, improving procurement and strengthening financial decentralization and budgeting based on the program.

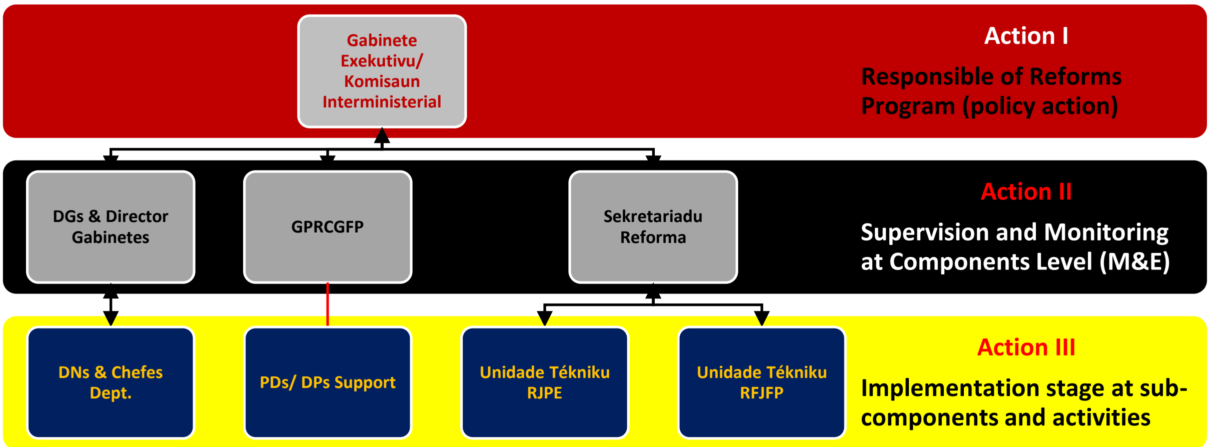
Timor's PFM Road Map priorities main goals are:

i) To enhance resource mobilization, improve planning and budgeting, improve budget execution, and strengthen accountability for quality, effective and efficient service delivery;

ii) To improve and strengthen efficiency and effective management of non-financial state assets in accordance with international standards.

Timor-Leste has committed to improving how it manages public resources and continues on a journey to progress them. We have already seen TL's journey for introducing programmes budgeting, in addition, TL has completed two public expenditure reviews with the World Bank to examine inefficiencies in the budgeting process and how to improve efficiency and service delivery. A commitment has also been made to move towards Medium Term Expenditure Frameworks, budgeting for multiple years, so far pilot workshops have been undertaken to assist line ministries in costing programmes in the medium term with the aim to be applied in all institutions by 2023. Timor's ambitious goals also include: improving the fiscal framework; developing fiscal rules; improving management of PPPs and reform of domestic revenue.

Figure 56: Flowchart of Responsibility of PFM Reforms



Source: PFM Reform Unit, Ministry of Finance, August 2021

9.2.3 Law on the Framework for the General State Budget and Public Financial Management

The Council of Ministers met in December 2020 and January 2021 and approved a draft of the new Framework Law on General State Budget (GSB) and Public Financial Management to present to Parliament. The proposed new law would replace and aims to improve on Law No 13/2009 which describes the processes for developing, enacting, executing and auditing the General State Budget. The proposed law should be enacted in time for the execution of OJE 2022.

Key features of new GSB and PFM law:

The current proposal has two objectives: to streamline public management and, at the same time, to increase transparency, responsibility, accountability and control of the services and entities of the Public Administrative Sector. The proposal now presented chooses to make substantial changes in some essential aspects of the fiscal framework and public financial management, while in other aspects where no need for change was identified, it will accept the existing law.

Key features of the proposal include:

- Enshrining program budgeting as a means of preparing and organising the General State Budget, adding substantial elements of planning to all phases of the budgetary process

- Adopting a “two-step” budget process, with a “Grand Planning Options” law approving the budget ceiling at the start of the budget process in May and the General State Budget law approving the budget allocations in October. This will allow the Parliament to have an early input on the budget ceiling and the main priorities of the budget, while giving the Government a general blueprint to prepare the more detailed General Budget Law. In addition, by locking the budget ceiling at the start of the budget process, it guarantees that the definition of the ceiling will be based on an assessment of the existing financial resources and fiscal sustainability considerations, and not solely on the needs and demands of LMs and institutions based on their needs.
- Establishing a new budget calendar, starting in May, and advancing the date of presentation of the General Budget Law from October 15 to October 1st, to avoid extending the previous year Budget Law, as it has happened four times in last six years.
- Setting new budget balance requirements and controls, namely on recurrent expenditures.
- Establishing new rules on execution of revenue and expenditure when a General Budget Law has not been approved by the Parliament, avoiding the existence of a fiscal cliff.

Table 29: Proposed Budget Calendar and Key Milestones according new GSB and PFM Law

Date	**New Calendar**
10/05	Government presents draft Grand Planning Options law
30/05	Parliament approves Grand Planning Options law
30/06	Jornada Orçamental
15/07	Government approves detailed budget ceilings
20/07	MoF issues circular on General Budget Law preparation
15/09	Government approves draft General Budget Law
01/10	Government present draft General Budget Law to the Parliament
15/11	Parliament approves General Budget Law

Source: Legal Unit, Ministry of Finance, August 2021