



Democratic Republic of Timor-Leste
Ministry of Finance



Pre-Budget Statement

2023

Including the 2022 Mid-Year Report

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Abbreviations

Appropriation Category	AppCat
Asian Development Bank	ADB
Autonomous Agencies	AA
Autonomous Service Of Medicines And Health Equipment	SAMES
Capital Development	CD
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)
Democratic 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

Preface

Now in its fourth year of publication, Timor-Leste's Pre-Budget Statement, including the Mid-Year Report, represents an important part in Ministry of Finance's mission of strengthening public financial management reform.

There have been significant strides forward in the area of public financial management and this document highlights the deepening of programme budgeting and the new Budget and PFM law. This document reports on the government priorities for the next fiscal year and for the medium term, as set out in the Grand Options, describing their alignment to the proposed General State Budget. It details the proposed budget strategy for 2023, highlighting allocations to the various institutions and fiscal sustainability implications. It also outlines the macroeconomic and fiscal context, their key developments, risks and forecasts over the medium term. The issue also covers trends and projections for other sources of financing i.e. Petroleum Fund's revenues and returns, loans, development partner grants and direct budget support. Part of the Pre-Budget Statement is also dedicated to historical trends of government spending over the last 5 years and execution up until the end of June 2022.

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 certain that the 2023 Pre-Budget Statement will increase civic engagement, public awareness and understanding of the Government's financial management and stimulate public discussion on the topics that are crucial for the development of this country.

I wish to express my appreciation to the Directorates and Units of the Ministry of Finance whose hard work and dedication have gone into this report.

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 via email to the General Director of Planning and Budgeting- Jose Alexandre de Carvalho jcarvalho@mof.gov.tl, National Director of Budget- Salomao Yaquim syaquim@mof.gov.tl, National Director of Planning Luisa Albertina Fraga- lfraga@mof.gov.tl National Director of Economic Policy- Epifanio Martins epmartins@mof.gov.tl.



1 Technical Disclaimer

Timor-Leste's 2023 Pre-Budget Statement, including the Mid-Year Report, is published prior to the 2023 General State Budget Book. For this reason, all economic projections contained in this statement are preliminary in nature and may be amended in the 2023 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. 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.

The proposed 2023 budget ceiling is set at \$3,276.6 million (including development partner commitments) and its split across the funding sources as in the table below.

Table 1: Combined Sources Budget 2021-2023, \$ Millions

	2021 Actual	2022 Original Budget	2022 Rectified Budget	2023 Budget Proposal
Combined Sources Budget	1,786.3	2,111.4	3,581.9	3,276.6
Government Expenditures by Fund	1,631.2	1,943.9*	3,414.4**	3,155.7***
CFTL (excl. loans, inc. social security, inc. DBS)	1,547.5	1,881.1	3,351.6	3,063.9
European Union - Direct Budget Support	9.1	9.0	9.0	3.3
Australia - Direct Budget Support		6.6	6.6	1.6
HCDF	13	12	12	17.7
Borrowing/Loans (disbursements)	70.7	50.8	50.8	74.1
Development Partner Commitments	155.1	167.5	167.5	120.0

Source: National Directorate of Budget and Development Partnership Management Unit, Ministry of Finance, 2021. * 2022 original Budget (including loans but excluding social security excess) *2022 rectified Budget excluding the social security amounts to \$3.2bn as is referred to later in this document. *** 2022 Rectified & 2023 including social security fund as the 2023 GSB proposal included the Social Security sector in the disaggregation of the budget ceiling to increase the transparency of the budget cycle. All figures as of July 2022 and are subject to revision before the final budget.

Impact of COVID-19 and Cyclone Seroja

Over the last two years the government has mobilised significant resources to respond to the COVID-19 pandemic and Cyclone Seroja. Timor-Leste recorded its first COVID-19 case on 21st March 2020 and following this President Lu-Olo declared a State of Emergency to run from 28th March which was subsequently extended numerous times. 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). Following the approval of Budget 2020 in October, a further \$350m was withdrawn. 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.

The first cases of community transmission were declared on the 26th of February 2021 as a result of mass testing. As a result 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) which were focussed 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

On Easter Sunday 4th April 2021, 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.

The government originally allocated \$2,2m in response. These funds were for clean water and food, construction materials, temporary wall protection for water and rivers. The final rectified budget in 2021, which was approved by approved by Parliament on the 27th April 2021, included further funds in response to both cyclone Seroja and the COVID-19 pandemic.

In the 2021 final rectified budget \$34.5 million was allocated to Ministry of Health to implement the COVID-19 vaccination program, increase quarantine facilities, purchase PPE equipment and extend 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. \$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).

In 2022 the country has begun to see signs of economic recovery from the effects of Cyclone Seroja and COVID-19. This is evidenced by projected increases in domestic revenue collection and GDP growth as explained below.

Petroleum Fund Revenue

The Government's General State Budget is largely financed by withdrawals from the Petroleum Fund. The projections used in this Pre-Budget Statement are adjusted to reflect the actual information available for 2020, 2021 and first half of 2022, as well as the Grand Plan Options approved in May 2022. Projections for 2023 are still subject to changes and will be revised in the final 2023 Budget.

For 2022, petroleum revenue was estimated at \$45.6 million. As of May 2022, receipts from the sale of oil and gas amounted to \$568.3 million, eight times higher than the projection in the Budget 2022 due to higher than anticipated increases to oil and gas prices. The Fund's year-to-date investment return is negative 6.3%, which translates to loss of \$1,431.2 million. The 2022 ESI remains at \$554.1 million as in the 2022 Budget and the proposed total withdrawal for 2022 increases to \$2,552.6 million (\$2.5 billion) following the approval of the Rectification Budget 2022 by the Parliament in May 2022. Up until May 2022, transfers to the State Budget amounted to \$450 million and the balance of the Petroleum Fund is \$18.3 billion.

Taking into account the recent changes in the Petroleum Fund, the preliminary estimates for the 2023 ESI is \$483.6, slightly lower than the previous estimation in the Rectification Budget 2022. Note that the final number will be presented in the Budget 2023 submission in October.

Macro-Fiscal Overview

Economic growth contracted by -8.6% in 2020 due the combined effect of the delayed budget, COVID-19 and the State of Emergency (this is the latest National Account figure). However, it is expected to return to positive growth of 1.5 % 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, Cyclone Seroja and poor execution of the large state budget, particularly capital and development execution.

The 2022 budget allocation is particularly large due to the increase in the budget ceiling following the rectified budget in May 2022 (\$3.2bn excluding social security fund). However this will not have a significant effect on economic growth which is forecast to grow 2.7%, as \$1bn will be reserved for the Veteran's Fund which will not be spent in the economy this year. Growth has been adjusted down slightly to reflect higher imports in the first half of the year (consumption and investment) which reduce GDP. A main driver of growth for 2022 is the strong execution on Tibar Port which is a significant PPP project for the economy.

2023 GDP is due to grow 3.2% due to an expected stable increase in the budget ceiling as laid out in the Grand Options document, political stability and a return to pre-COVID private investment levels. 2024-2027 economic growth is expected to be stable and steady.

Inflation is forecast to increase to 7.4% for 2022. This has increased from earlier forecasts following Q2 CPI figures. Inflation has increased significantly over the last few months due to an increase in world oil and food prices as a result in the war in Ukraine.

Domestic revenues reached \$83.9 million by the end of June 2022, an increase of \$20.4 million on collections at the same time the year before. This is indicative of an economy that is showing signs of recovery from the economic disruption brought on from the COVID-19 pandemic and the knock-on effects of cyclone Seroja to business activity.

Preliminary forecasts see domestic revenue (excluding ZEESM) set to reach \$150.4 million by the end of 2022. Following the implementation of new consumption taxes, domestic revenue is projected to reach to \$169.4 million by the end of 2023 (or \$174.9 with the inclusion of taxes and fees and charges from RAEOA/ZEESMS). This means that following a fall in 2021, non-oil receipts are set to be on a consistent growth trend for the next 5 years; and are projected to exceed \$200m by 2027 provided that positive macro-economic conditions hold. Further revenue increases can be expected if further fiscal reforms, including the approval of the VAT law, are implemented in the coming years.

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 not only on this year's choice of budget, but also the choices made for the subsequent years.

The analysis shows that under the current expenditure forecast, the Petroleum Fund will run out in just 13 years. If IMF recommendations to reduce and limit expenditure to \$1.2 billion a year are

followed, the Petroleum Fund can last until 2045. If total withdrawals are capped at \$1bn a year the fund will fully deplete by 2047. Finally a combination of gradual spending cuts and fiscal reforms can sustain the fund until 2051 whilst at the same time building up domestic revenues to the point at which the fund is no longer needed.

Historical Expenditure Analysis

A budget rectification was passed in April 2021, following community transmission of Covid-19, the subsequent lockdown and in the wake of Cyclone Seroja. The amendment focused on six key areas; employment support, moratorium on credit, exemption from tuition fees, food acquisition, support to frontline professionals and COVID-19 prevention and mitigation measures. The amendment amounted to a total of \$198.4 million of which \$135.3 million was needed additionally to finance the budget (the remained \$198.4 million came from reallocation of the then current spending plans). The final execution of the rectified budget for 2021 was 75.3%.

Government Priorities and Budget Transparency Proposal

The Budget 2023 will continue to put people at the centre of all and prioritize citizen's well-being to ensure a fair and equitable distribution of the state budget to improve service delivery and economic recovery and resilience to promote sustainable and inclusive economic growth in the medium term and ascend to an upper-middle income country by 2030.

The 2023 Budget proposal is formulated based on the following VIII Government three Strategic Objectives aimed at providing to all citizens as a whole:

1. Opportunity to have a healthy, secure, and long life
2. Access to knowledge, technology, and innovation
3. Access to sufficient resources to guarantee life with dignity.

The Government continues to institutionalize and mainstream the gender equality and social inclusion agenda in the overall planning and budgeting process. The 2023 budget call circular underlines the importance to look more closely at the impact of budgetary measures and policies on gender equality and inclusion and ensure that the needs and interests, priorities, and challenges of women, girls, boys, and men in different age-conditioned social situations, class, location, etc. are adequately addressed in the annual plan. For the 2023 budget proposal must include the following markers to hold the Government to account on various crosscutting issues such as gender equality and social inclusion, nutrition, climate, and supply chain.

Loans and Public Private Partnerships (PPPs)

Loans – At present, external loans are provided by international multilateral banks such as the Asian Development Bank (ADB) and the World Bank (WB) and one bilateral loan is provided by 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 2021, debt stock increased to \$234.65m. Due to the declining impact of Covid-19 pandemic and flood disaster in April 2021 on project implementation, disbursements in 2022 are expected to increase by approximately 32% compared to the previous year.

There are currently 15 ongoing road projects funded by concessional loans of which 12 projects have already been completed. One further project is likely to be completed by the end of the year and this would bring the total numbers of projects completed to 87% 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 \$490m for new concessional foreign loans to be negotiated in 2023.

PPPs – Several PPP projects are currently ongoing: the Tibar Bay Port PPP which is in the Implementation and Operation Stage, the Medical Diagnostic PPP which is in the procurement and negotiation stage, the Affordable Housing PPP, Cristo Rei PPP, President Nicolau Lobato International Airport and Dili Port Redevelopment and Commercialization PPP which is in the feasibility stage.

3 Macro-Fiscal Overview

3.1 Summary

Table 2: Economic Indicators, 2020-2027, %

Summary	Forecast							
	2020	2021	2022	2023	2024	2025	2026	2027
Real GDP (non-oil)	-8.6%	1.5%	2.7%	3.2%	3.4%	3.5%	3.4%	3.5%
Inflation CPI	0.5%	3.8%	7.4%	5.5%	3.5%	2.6%	2.5%	2.3%

Source: GDP 2020= DG Statistics, National Account, GDP Forecast 2021 -2027= National Directorate of Economic Policy, Ministry of Finance, 2022.

- Real non-oil GDP growth fell by 8.6% 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 1.5% although this has been revised down due to Covid-19 confinement, cyclone Seroja and a poor execution of the large state budget by the end of the year (Capital and Development execution was only 39%).
- The 2022 budget allocation is particularly large due to the increase in the budget ceiling following the rectified budget in May 2022 (\$3.2bn excluding social security fund). However this will not have a significant effect on economic growth which is forecast to grow 2.7%, as \$1bn will be reserved for the Veteran’s Fund which will not be spent in the economy this year. Growth has been adjusted down slightly to reflect higher imports in the first half of the year (consumption and investment) which reduce GDP. A main driver of growth for 2022 is the strong execution on Tibar Port which is a significant PPP project for the economy.
- 2023 GDP is due to grow 3.2% due to an expected stable increase in the budget ceiling as laid out in the Grand Options document, political stability and a return to pre-COVID private investment levels. 2024-2027 economic growth is expected to be stable and steady.
- Inflation is forecast to increase to 7.4% for 2022. This has increased from earlier forecasts following Q2 CPI figures. Inflation has increased significantly over the last few months due to an increase in world oil and food prices as a result in the war in Ukraine.
- Inflation 2023-2027 is forecast to reduce as world prices stabilize.
- Between June 2021 and June 2022 the US dollar appreciated 4.0% against a weighted basket of currencies of Timor-Leste’s trading partners (the nominal effective exchange rate, NEER). A strong US dollar can have a downward pressure on domestic inflation. However, this appreciation may also make Timorese non-oil exports more expensive in international markets constraining the development of the country’s exports.

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 2020, non-oil real GDP in Timor-Leste declined to -8.6% to \$1,481m. National Accounts data exist up to 2020, after that DNPE forecast GDP into the future.

Timor-Leste experienced GDP growth, averaging 2.1% per year over 2010-2020. These growth rates were higher in the early 2010s and were 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. 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. However, negative economic growth rates in 2017, 2018 and 2020 have undermined the progress made.

Non-oil GDP growth was negative in 2020. The contraction was a consequence of declines in government expenditure, private sector investment and lower exports and imports. Political uncertainty also led to lower development partner spending and reduced business activity. Export of goods and services fell by 51.1% driven by the COVID 19 restrictions on international borders and lockdowns in the each of the trade partners.

Forecasts for 2021 indicate a return to positive growth of 1.5%.

International

Global growth outlook is projected to slow from 6.1% in 2021 to grow at 3.2% in 2022. In Advanced economies and emerging and developing economies are forecast to grow at 2.5% and 1.4% respectively in 2022 and 2023. The War in Ukraine and the ongoing pandemic are the main factors that contributed to the significant slowdown in growth in 2022 and added to inflation. China is projected to grow at 3.3% in 2022 compared to last year which was 8.1%.

Table 3: Growth Indicators, 2020-2023, %

Country	Actual		Forecast	
	2020	2021	2022	2023
World	-3.1%	6.1%	3.2%	2.9%
Advanced Economies	-4.5%	5.2%	2.5%	1.4%
Emerging and Developing Economies	-2.0%	6.8%	3.6%	3.9%
Emerging and Developing Asia	-0.8%	7.3%	4.6%	5.0%
China	2.2%	8.1%	3.3%	4.6%

Source: IMF World Economic Outlook, July 2022.

Global growth is projected at 2.9% in 2023. Growth in advanced economies is expected to decline from 2.5% in 2022 to 1.4% in 2023, while growth for the emerging market and developing economy group is forecast at 3.6% in 2022 and 3.9% in 2023. The factors contributing to the predicted slowdown in growth in 2023 are the ongoing war in Ukraine and sanctions on Russia, and the COVID-19 pandemic. Slower vaccines rollout and less policy support in some low income countries has contributed to the lower growth in emerging and developing economies. These factors also have contributed to the lower manufacturing activity in several countries leading to an increase in consumer price inflation. Moreover, the war in Ukraine increased higher food and energy prices, which further weighs on the outlook.

3.1.2 Prices and Inflation

Table 4: Global and Regional Inflation Rates (%)

Country	Actual		Forecast	
	2020	2021	2022	2023
World	3.2%	4.7%	8.3%	5.7%
Advanced Economies	0.7%	3.1%	6.6%	3.3%
Emerging and Developing Economies	5.2%	5.9%	9.5%	7.3%
Timor-Leste*	0.5%	3.8%	7.4%	5.5%

Source: IMF World Economic Outlook July 2022. *Ministry of Finance forecast.

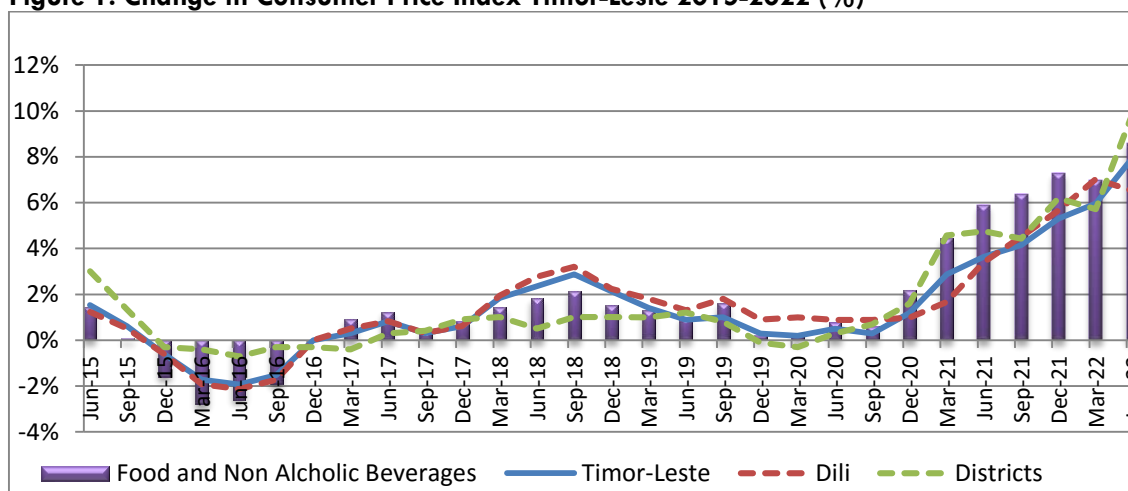
International

Consumer Price Inflation is expected to increase, with global inflation forecast at 8.3% by the IMF in 2022. Rising inflation reflects the impact of higher demand and lower supply due to the war in Ukraine and sanction on Russia. The increase in oil prices, have contributed to the rise in Consumer Price Inflation in advanced economies, however this is projected to recover in the coming years. For emerging market economies, inflation has risen, reflecting the impact of currency depreciation and higher commodity prices which increases the prices of imported goods, but it is projected to moderate due to tighter monetary policy. Global inflation is expected to moderate in 2023.

Timor-Leste

Timor-Leste's level of inflation has seen a strong increase. In June 2022 YoY inflation in Timor-Leste was 8.0%; this means that a basket of goods and services that cost \$100.00 in June 2021 cost \$108.0 in June 2022— on average, prices are up compared to one year ago. YoY food and non-alcoholic beverage inflation in June 2022 was 8.6%, higher than the increase of 5.9% witnessed last June. 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. Inflation in Districts was 9.9% (YoY) which is more than inflation in Dili which rose by 6.5% over the same period. Inflation in Timor-Leste in 2022 is expected to rise to 7.4%. This is mainly due to the strong increase in world oil prices, as a result of the war in Ukraine, pushing up import and food prices. Rising inflation in Timor-Leste can reduce the purchasing power of citizens, Timor-Leste's international competitiveness and investment.

Figure 1: Change in Consumer Price Index Timor-Leste 2015-2022 (%)



Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2022.

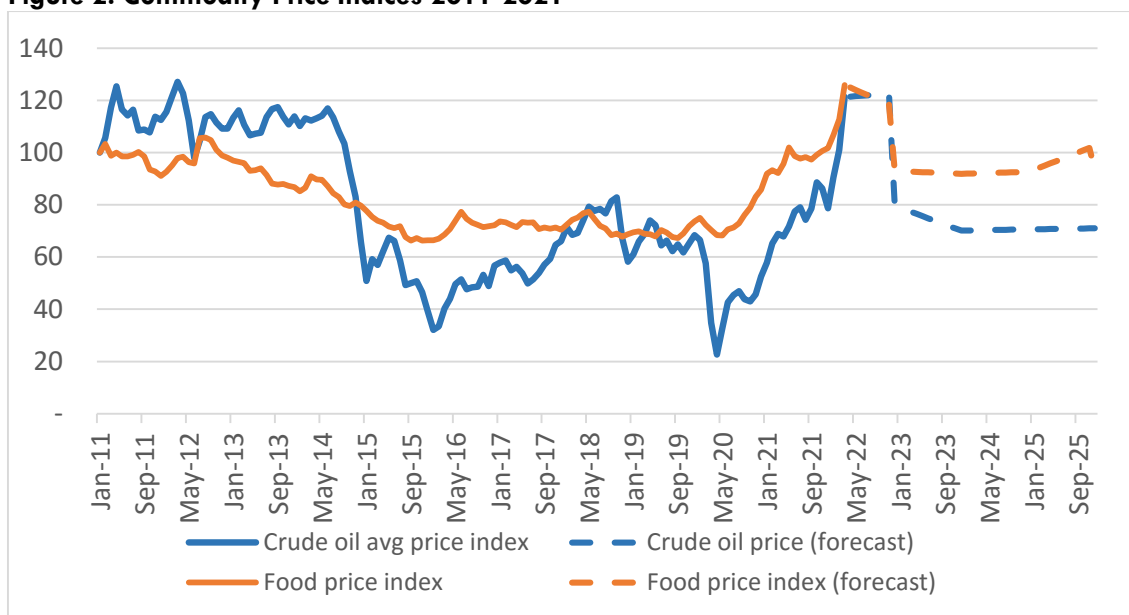
Oil prices

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 \$116.9 per barrel to lows of \$32.1 per barrel in January 2016. The decline in oil prices was driven by the increased global supply during a period of low global demand. Following this, prices started to recover to \$81.3 per barrel in Oct 2018. However, global demand for oil has drastically declined since the onset of the Coronavirus pandemic down to \$22.7/barrel in April 2020. Oil prices then started to rise sharply and reached \$125.8 per barrel in April due to the war in Ukraine. Prices are expected to slowdown 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 Commodity Price Index (2011=100), international food prices have continued to decline from a high of 105.8 in August 2012 to 68.3 in May 2020. However, the World Bank is forecasting that the food prices index increased significantly in April 2022 at 125.8 but is set to decline to 92.9 by December 2022. The increase in commodity prices is in line with supply disruption, the war in Ukraine and sanctions on Russia. Rice specifically is a staple part of the Timorese diet. The benchmark “Thai 5%” (an international measure of rice prices) experienced a decline of 26% in January 2022 from January 2021, but is expected to remain stable through the rest of 2022 and 2023. This will have a positive effect on poorer households where basic foods make up the majority of their spending. Coffee prices (Arabica) are expected to decrease 26% in March 2023, this will negatively affect those families who rely on coffee production in Timor-Leste.

Figure 2: Commodity Price Indices 2011-2021



Source: World Bank Commodity Markets Outlook April 2022

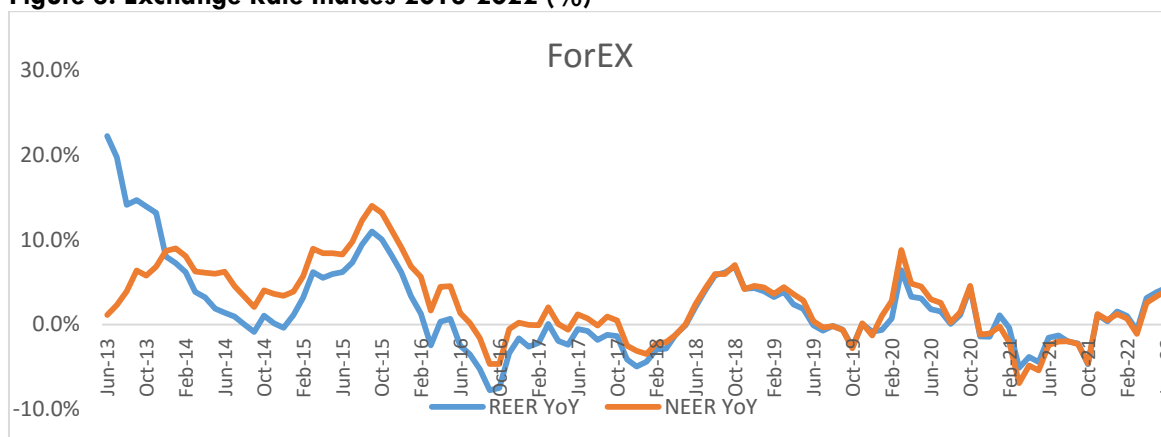
3.1.3 Exchange Rates and Competitiveness

The effective exchange rate is the exchange rate of a country’s currency, measured as the weighted sum of the exchange rates with its commercial partners. The nominal effective exchange rate (NEER) is an unadjusted weighted average rate at which one country’s currency exchanges for a basket of multiple foreign currencies. The real effective exchange rate (REER) is adjusted for the effects of inflation and is a better measure of competitiveness. Between June 2021 and June 2022 Timor-Leste’s NEER appreciated by 4.0% while the REER appreciated 4.4%.

Over this period the NEER also appreciated 4.6% against a weighted Thai Baht and Vietnamese Dong basket and, the REER appreciated by 1.7% against the same basket. This real appreciation places downward pressure on rice prices and inflation in Timor-Leste (as Thailand and Vietnam export large quantities of rice to Timor-Leste).

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 2013-2022 (%)



Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2022.

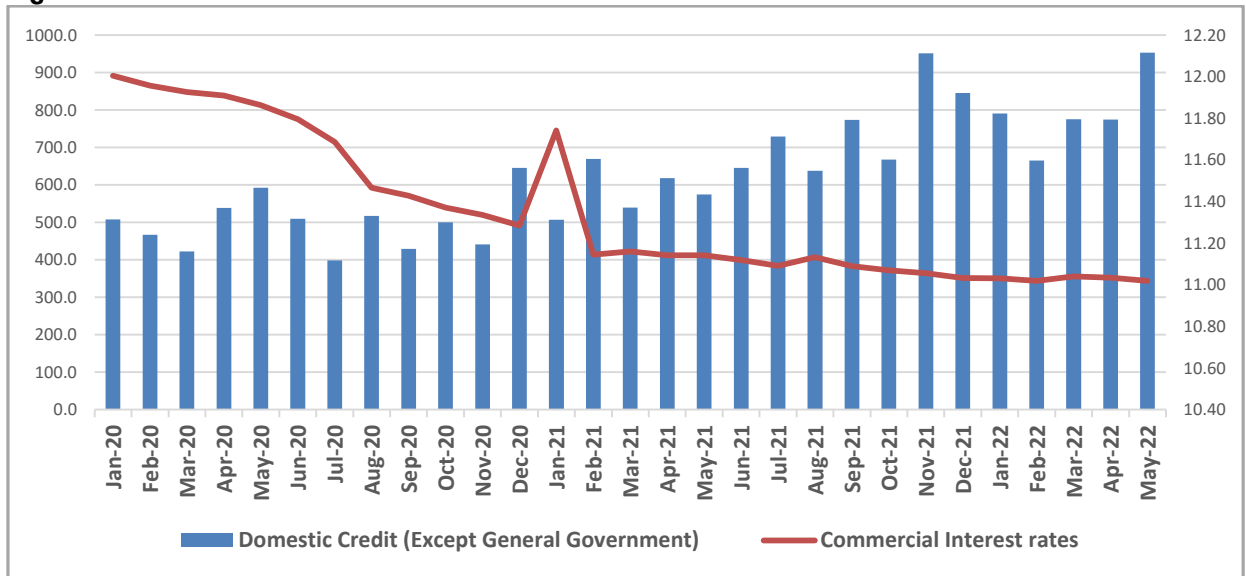
3.1.4 Financial Sector Trends

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 11.02% in May 2022, a decrease of 0.06 percentage points from May 2021 meaning interest rates have stayed similar over the past 12 months. Declines in interest rates will be good for businesses who will be able to borrow money to expand their business at a cheaper cost of financing.

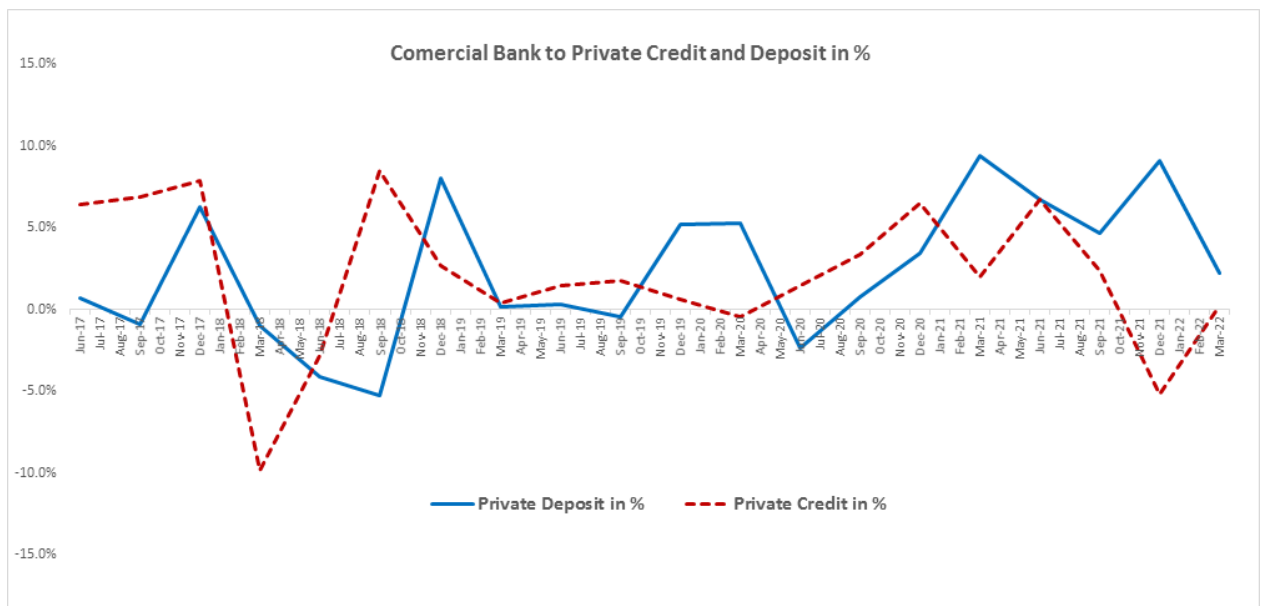
Total domestic credit, excluding general government, was \$954 million in May 2022 and it is increased by 66% from May 2021 with an average of \$680 million over the prior 12 months. However, information from the Central Bank indicates that loans are increasingly being given to individuals rather than businesses.

Figure 4: Commercial Interest Rates and Credit



Source: Banco Central Timor-Leste, 2022. Interest Rate (RHS, %), Credit (LHS, \$m).

Figure 5: Commercial Bank Private Credit and Deposit Growth



Source: Banco Central Timor-Leste, 2022.

Commercial bank private deposit growth was volatile between June 2017 and May 2022 (blue line). The average growth of private deposit between June 2017 and March 2022 grew by 2.4%. Commercial bank private credit was volatile between June 2017 and March 2022 (red line). The average growth of private credit between June 2017 and March 2022 was 2.1%. The growth rates of both private deposit and credit have fallen in the last 12 months.

3.2 Economic Outlook

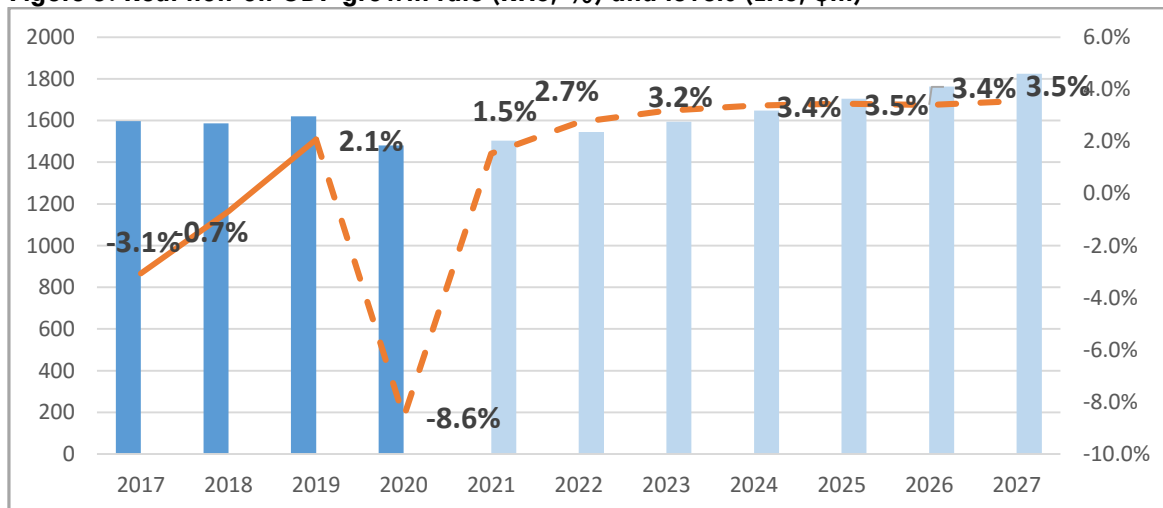
The Ministry of Finance is forecasting non-oil GDP growth to be 1.5% for 2021. Public sector investment in 2020 was constrained by the duo-decimal system, political uncertainty and Covid-19. However, the new coalition should provide the political stability for the Budget to be approved

for 2021 providing greater momentum for public infrastructure projects, especially in education, health, and water and sanitation. Despite the large budget for 2021, this has been revised down from earlier forecasts due to the impact of Covid-19 community transmission and the associated lockdown, Cyclone Seroja and a poor execution of government spending, particularly capital and development execution.

The 2022 budget allocation is particularly large due to the increase in the budget ceiling following the rectified budget in May 2022 (\$3.2bn excluding social security fund). However this will not have a significant effect on economic growth which is forecast to grow 2.7%, as \$1bn will be reserved for the Veteran’s Fund which will not be spent in the economy this year. Growth has been adjusted down slightly to reflect higher imports in the first half of the year (consumption and investment) which reduce GDP. A main driver of growth for 2022 is the strong execution on Tibar Port which is a significant PPP project for the economy.

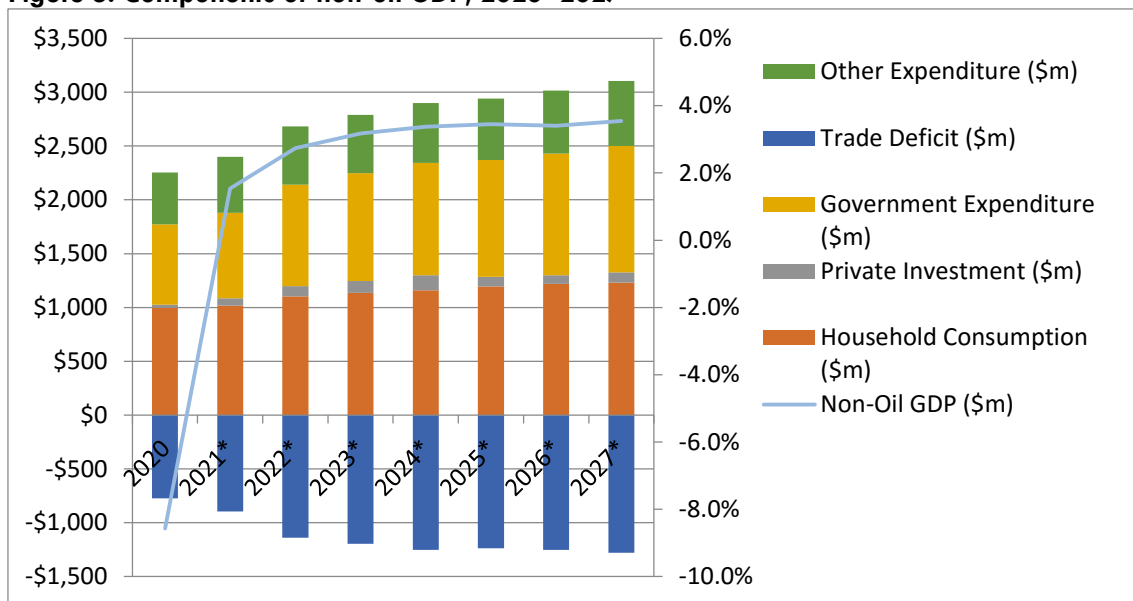
In 2023 GDP is due to grow 3.2% due to an expected stable increase in the budget ceiling as laid out in the Grand Options document, a return to pre-COVID private investment levels and political stability. 2024-2027 economic growth is expected to be stable and steady.

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



Source: Timor-Leste National Accounts 2000-2020, General Directorate of Statistics; 2021-2027 Economic Forecasts, National Directorate of Economic Policy, Ministry of Finance, July 2022.

Figure 6: Components of non-oil GDP, 2020- 2027



Source: *Timor-Leste National Accounts 2000-2020, General Directorate of Statistics; 2021-2027 Economic Forecasts, National Directorate of Economic Policy, Ministry of Finance, 2022.*

Risks and Uncertainty

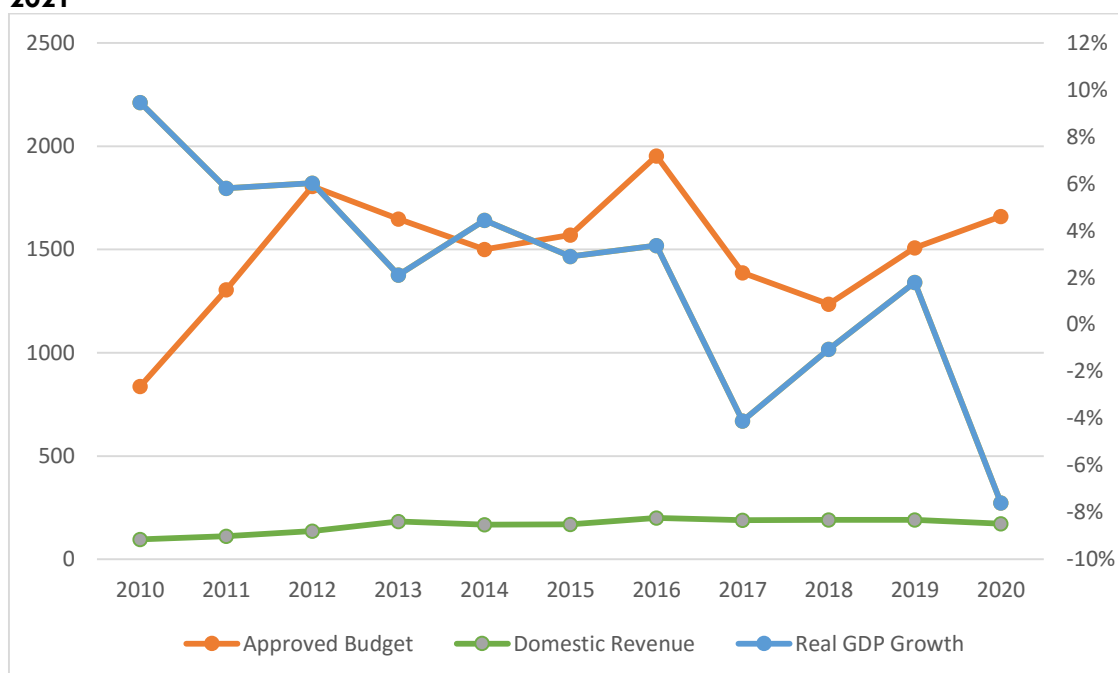
Economic forecasts or projections aim to predict annual GDP growth rates and high level macroeconomic figures. Making forecasts about what macroeconomic variables may be in the future is important to help governments and businesses make decisions with regard to policies, planning and investment. However, 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 2023 there will be parliamentary elections. The above forecasts assume smooth transition from the VIII to IX Constitutional Government, however disruptions could cause delays to implementation of planned government projects and could lead to lower than expected execution.

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 by 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.

For Budget 2023, in line with the new PFM and Budget Law and in the spirit of program based budgeting, entities can allocate their own budget to the different appropriation categories (e.g. goods and services, minor capital etc.) more or less freely in order to deliver the outcomes to which they have committed (however this does not apply to salaries and wages which is more restricted). This does add increased uncertainty to GDP forecasting as the specific final spending on different categories of public spending can vary largely.

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, July 2022.

Between 2010-2020 years there was 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 to 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.

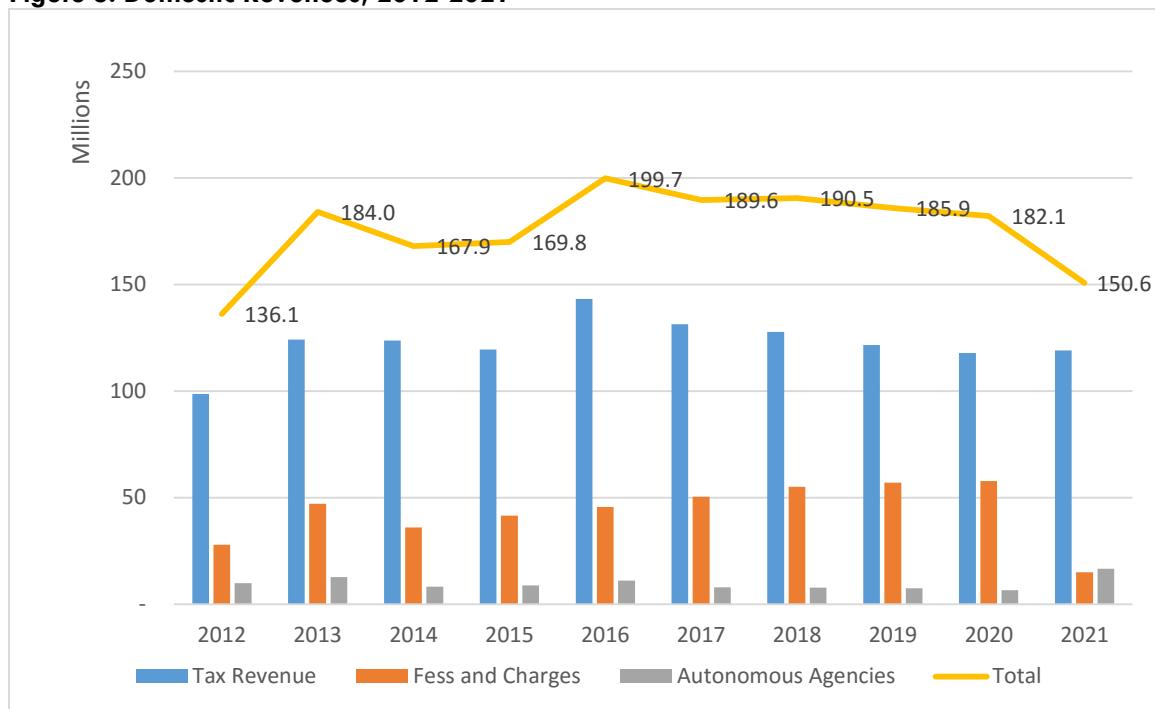
- **Composition and allocation of budget;** Fiscal policy is crucial to boost economic growth. The type of government spending influences economic growth when the share of budget allocation is higher in productive sectors. Investment in crucial infrastructure such as roads, machinery, research and development 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.
- **Quality of public spending;** tradition budgeting ie line item budgeting focuses on inputs and execution ie how much money was spent rather than the impact. For on for this reason there has been a move to Programme Budgeting that focuses on the outcomes at programme and activity level in an aim to establish state budgets that have economic impact in the short and long run, ie improving the quality of public spending.

3.4 Domestic Revenue

3.4.1 Historical Trends

Over the past decade, domestic revenues have not followed a consistent growth pattern. From 2012 to 2013 was the period where revenue growth saw the highest growth rate seen from 2012 to 2022 at 35%. They then saw a decline in 2014, followed by another rise to a peak in 2016 of \$199.7 million. From 2017 to 2021 domestic revenue consistently declined (at an average of 5% a year). Political instability and the COVID-19 pandemic contributed to falls in domestic revenue between 2017 and 2020. In 2021 the economy began to recover from the aforementioned factors, however domestic revenues declined by 17% to their lowest total since 2012. This was due to Electricity of Timor-Leste (EDTL-in Tetum) and Bee Timor-Leste becoming public entities which resulted in a 74% decline in Fees and Charges.

Figure 8: Domestic Revenues, 2012-2021

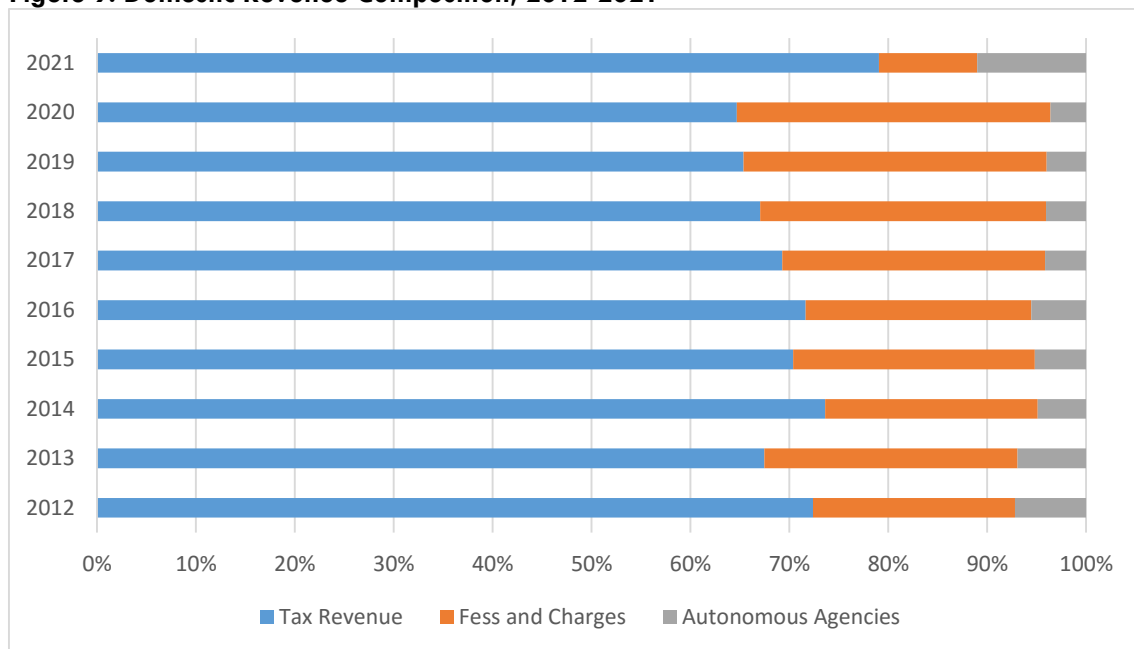


Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Tax revenue has been consistently the largest contributor to domestic revenue, averaging around 70% of total domestic revenue collection across the last 10 years. This is in comparison to around 24% for Fees and Charges and around 6% 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. Yet tax revenue had fallen consistently from 2016 to 2020 (from \$143m in 2016 to \$118m in 2020), alongside a decline in overall collections. Tax revenue in 2021 started to increase again (rising to \$119m), making up 79% of the total revenue in that year. While interest receipts have been increasing over recent years, they still make up less than 1% of overall collections (in figure 8 interest receipts are included within fees and charges).

ZEESM revenue collections as those figures have not yet been made available for 2019-2021. Therefore to allow a fair comparison.

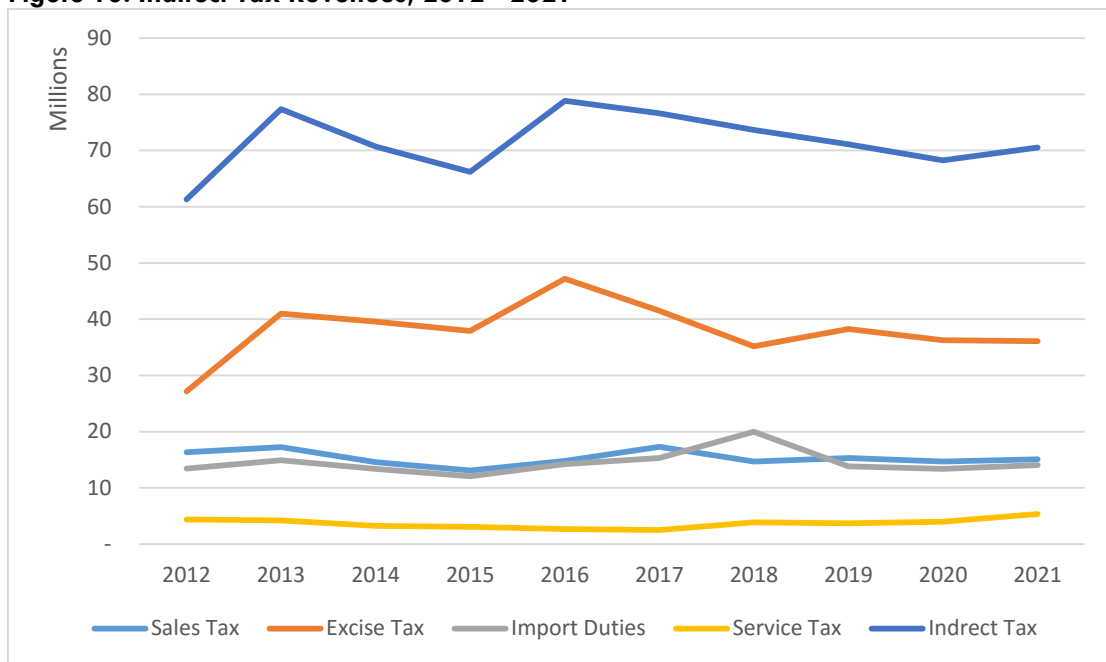
Figure 9: Domestic Revenue Composition, 2012-2021



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

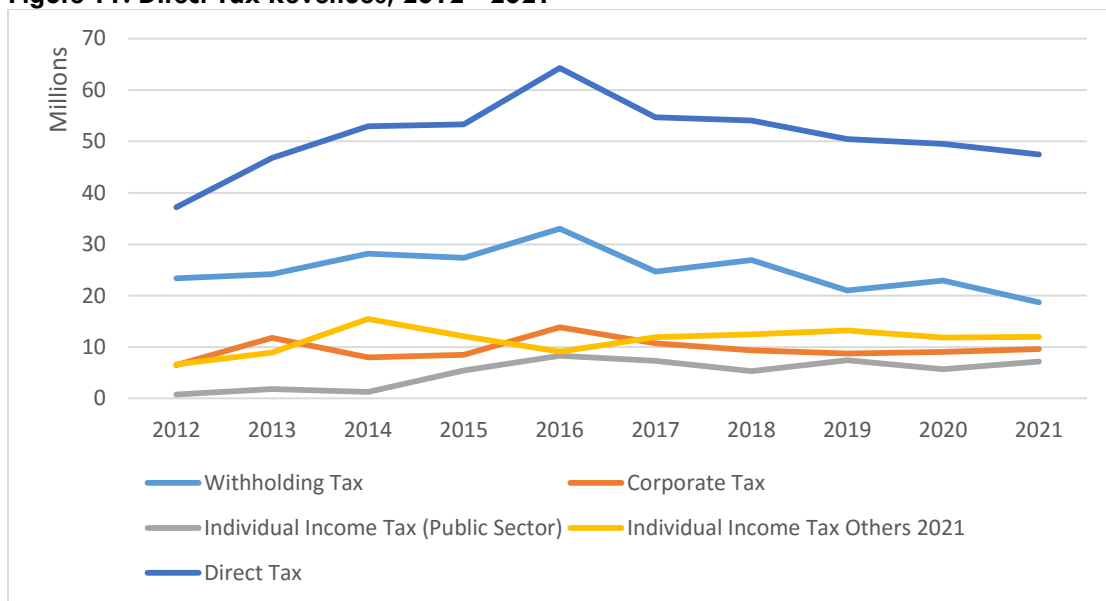
Taxes in 2021 were higher than those in 2020 but started lower in Q1 (\$24.4m) and increased significantly in Q2 (to \$31.8m) before reaching a peak in Q4 (\$35.8m). The biggest year on year increase was seen by service tax which increased by 35% followed by income tax for public sector employees which increased by 27%. The third biggest increase was in corporate taxes which increased by 6%. Excise Tax, corporate taxes on Import duties, sales tax and Individual income tax others were also all higher than the previous year. Withholding taxes in fact declined 18% suggesting a decline in infrastructure spending. Excise taxes continued to be the largest individual contributor to tax revenues, making up 30% of the total. Withholding taxes, making up 16%, and sales tax, making up 13%, remained the second and third highest taxes. Indirect taxes continue to exceed direct taxes in 2021, as they have for the past 10 years.

Figure 10: Indirect Tax Revenues, 2012 - 2021



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

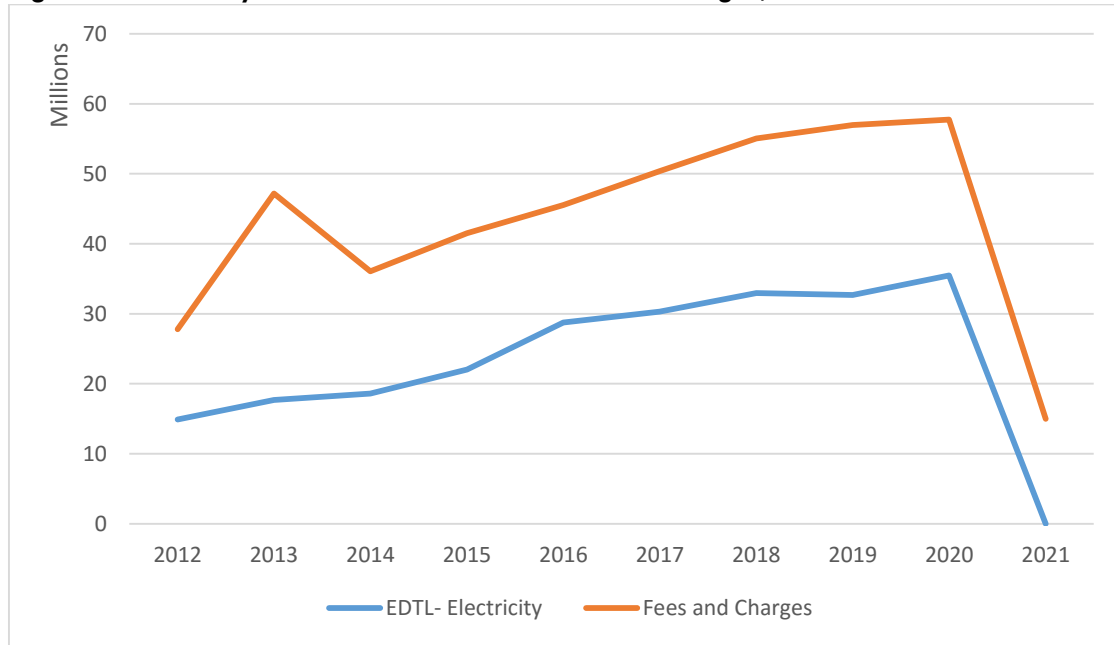
Figure 11: Direct Tax Revenues, 2012 - 2021



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Looking at Fees and Charges, they have seen consistent growth since 2015 and reached a peak in 2020. 2013 was a significantly high year due to an exceptionally large contribution of other non-tax revenues which grew from \$967k in 2012 to \$15.3 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 2012. In 2020, fees and charges reached its maximum point but then saw a large fall of 74% in 2021 due to Bee TL and EDTL becoming public entities

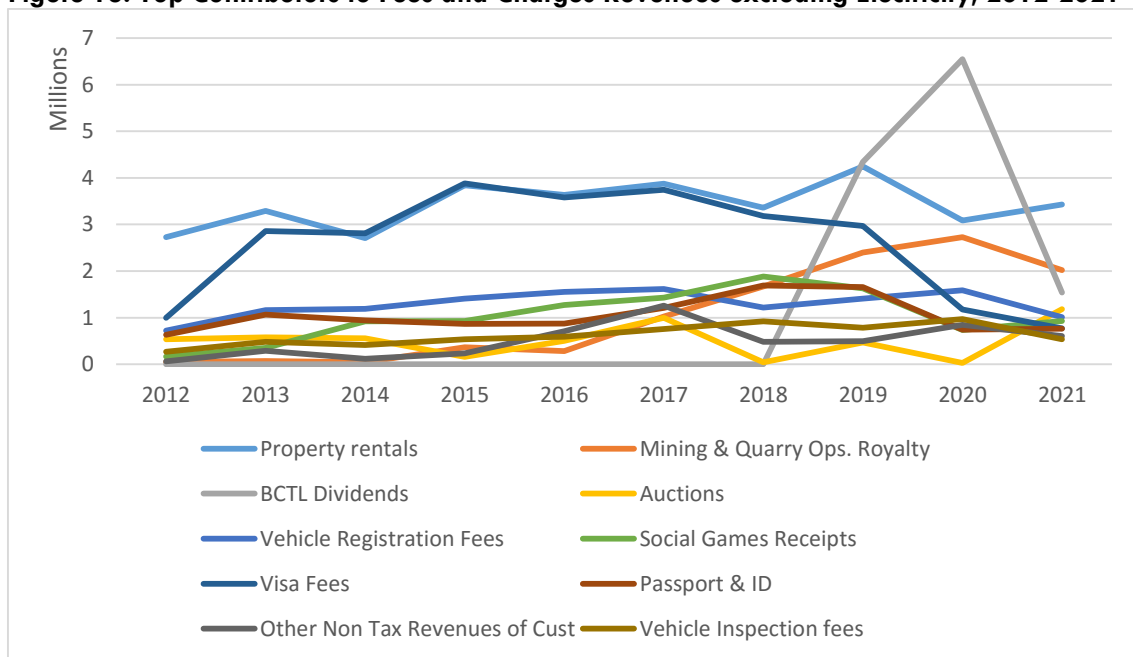
Figure 12: Electricity contributions and total Fees and Charges, 2012-2021



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

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. Dividends from BCTL declined last year to \$1.5 million from \$6.5 million in 2020, making it the third largest fees and charges collection, behind Mining and Quarries and Property Rental fees and charges. Visa fees, usually one of the largest contributors, fell by almost \$2million in 2020 and have continued to fall a further \$400k in 2021. This is largely due to the rapid decline in new arrivals to the country given the COVID-19 pandemic and State of Emergency restrictions. Property rentals became the largest contributor in 2021 making up 23% of the fees and charges.

Figure 13: Top Contributors to Fees and Charges Revenues excluding Electricity, 2012-2021



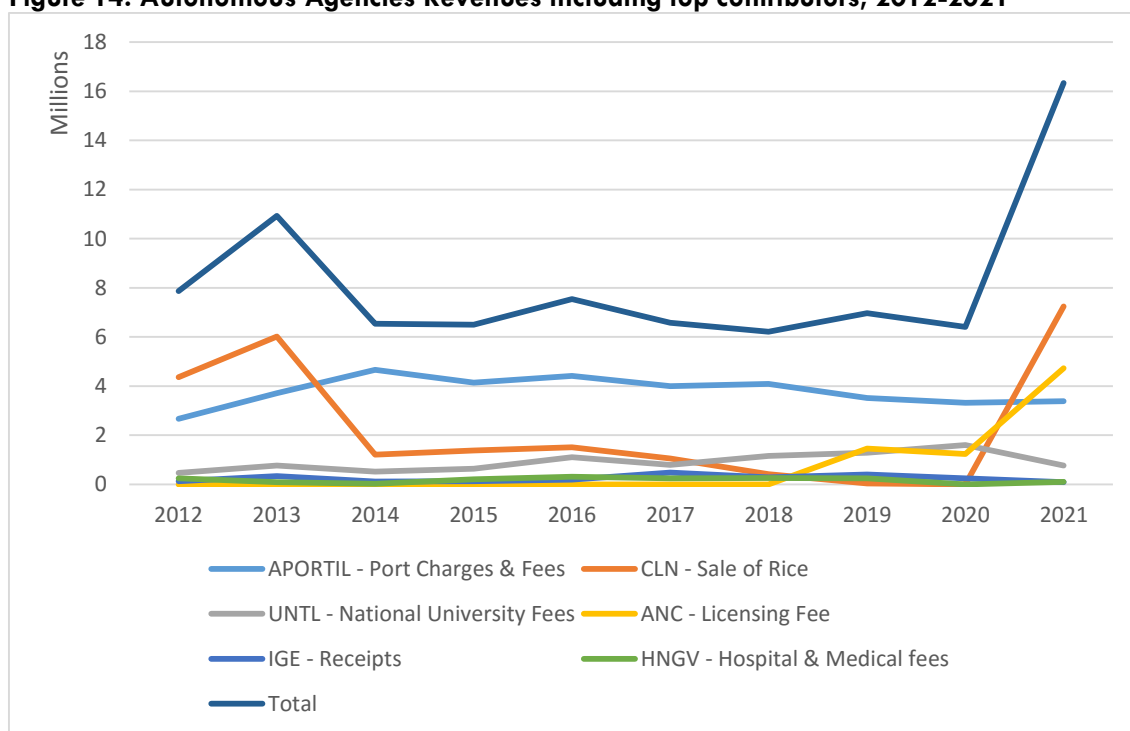
Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Autonomous Agencies do not seem to follow any historical trend. However the large spikes in 2013 and 2016 do coincide with rises in the overall revenue collection. The Autonomous Agencies total for 2021 was 152% higher than in 2020 due an economic recovery from COVID-19. CLN Sale of Rice became the largest contributor of Autonomous Agencies' fees in 2021, and making up 44% despite no revenues coming from this category in the previous year. ANC - Licensing Fee saw a significant increase from \$1.2 million to \$4.7 million, and therefore making it the second largest contributor to Autonomous Agencies Fees in 2021 (contributing 29% of the total) after CLN-Sale of Rice at 44%.

APORTIL has consistently been the largest contributor to the total before 2021, contributing 51% in 2020 and averaging around 40% in the decade before.

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, 2012-2021



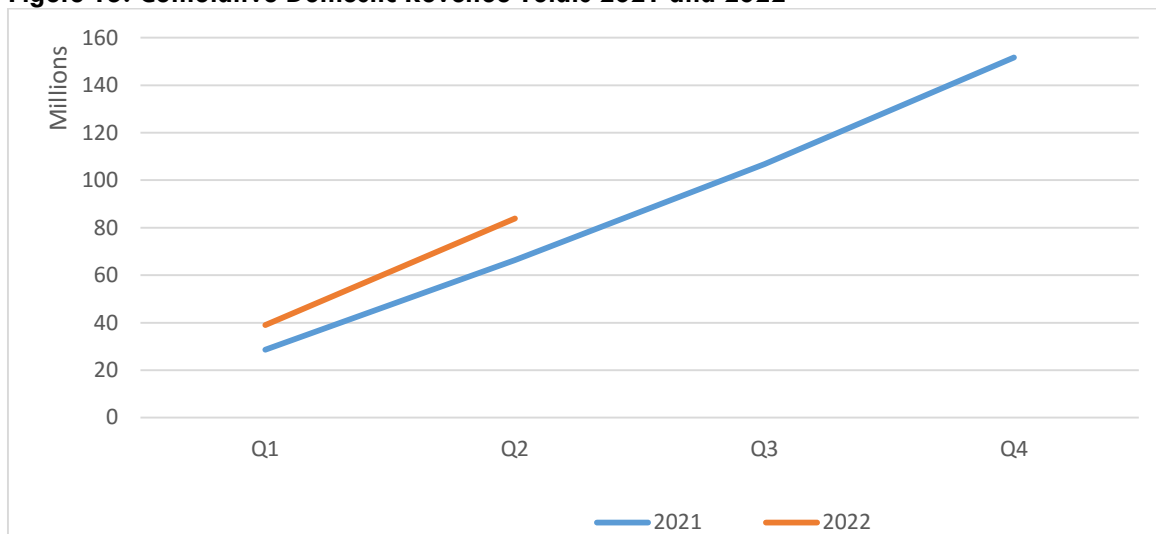
Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

3.4.2 Mid-Year Analysis

Domestic revenues saw a rapid start to collections in 2022, with collections in the first quarter \$10.4m higher than in the first quarter of 2021 (this is a 36% increase). Domestic revenues in Q1 2022 were particularly higher, due to an increase in some important taxes including individual income tax for private sector workers (which more than doubled), corporate tax (which increased by 244%) and sales tax (which increased by 41%). The large increase in receipts, particularly for corporate taxes, is likely due to the economic recovery following the COVID-19 pandemic, especially from the periods of mandatory confinement and sanitary restrictions. The increases are not as dramatic if compared with pre-COVID levels.

Collections continued to increase in the second quarter which saw a 19% increase in revenue collections compared to quarter 2 last year.

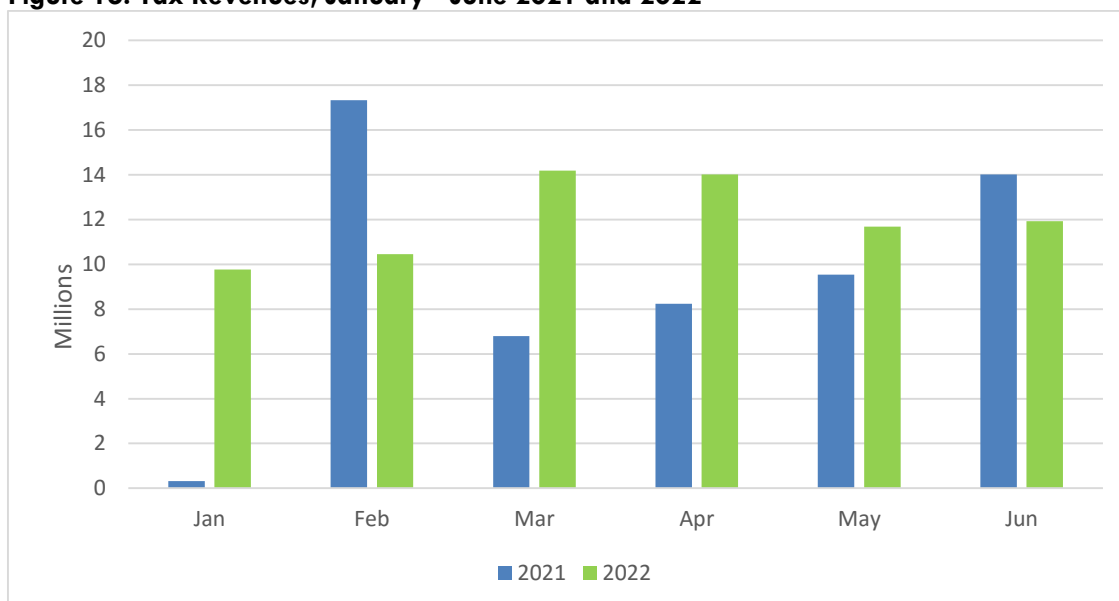
Figure 15: Cumulative Domestic Revenue Totals 2021 and 2022



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Figure 15 shows Cumulative Domestic Revenue of 2021 and 2022 by Quarter. Total cumulative domestic revenue in 2022 up to Q2 is 26% higher than cumulative domestic revenue collected in the same period in the previous year.

Figure 16: Tax Revenues, January - June 2021 and 2022



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Focusing on direct taxes only, Corporate Tax receipts in 2022 saw an increase of 244% in Q1 compared to Q1 in 2021. As mentioned in the previous paragraph this is likely due to the economic recovery from the COVID-19 pandemic as the numbers are in line with pre-COVID years. However the collection of corporate tax in Q2 2022 saw a decline in comparison to Q2 of the previous year by 15%. On the other hand, withholding Tax which is commonly linked to the level of capital spending in 2022, is down in Q1 (by 8%) but increased slightly in Q2 compared to 2021 (by 10%).

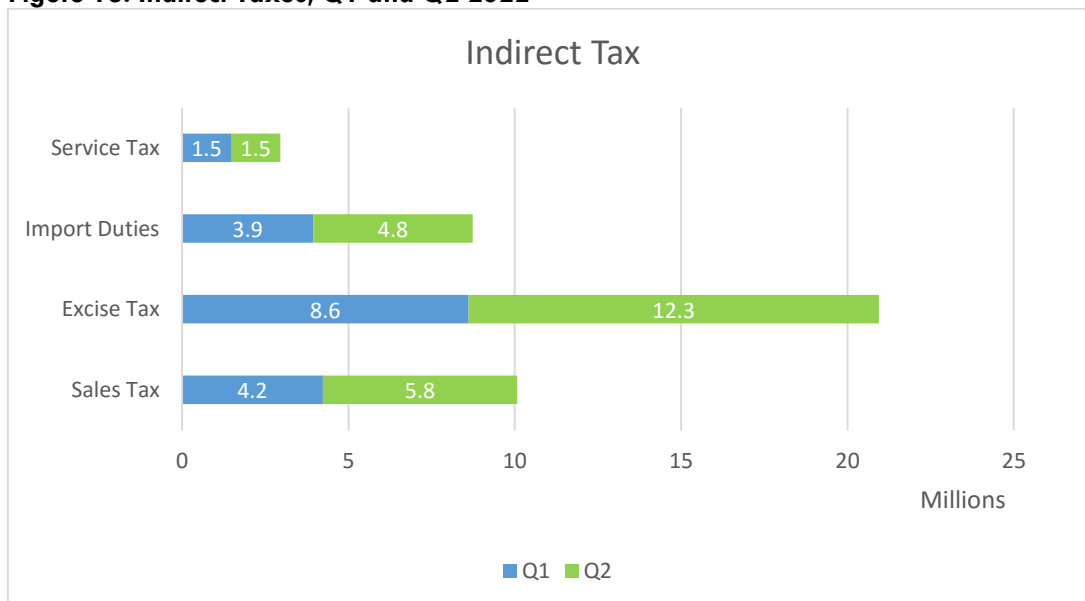
Figure 17: Direct Taxes, Q1 and Q2 2022



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Indirect taxes in 2022 also saw an increase in Q1 by 29% compared with same period the previous year, with most taxes seeing increases of collections by the end of the quarter. In Q2 2022 indirect taxes saw a 36% increases compared to Q2 of the previous year. Indirect taxes are often used as proxy for household consumption, therefore this increase shows promising signs for the overall condition of the Timorese economy. All (Q1 and Q2) indirect taxes are exceeding their collections at the same point last year.

Figure 18: Indirect Taxes, Q1 and Q2 2022



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Revenues from fees and charges saw a reduction of 14% in Quarter 1 of 2022 compared to Q1 of the previous year. However they increased 55% in Q2 2022 in comparison to Q2 of the previous year. As a result, overall collections in the first 6 months of 2022 were 19% higher than in the first 6 months of 2021.

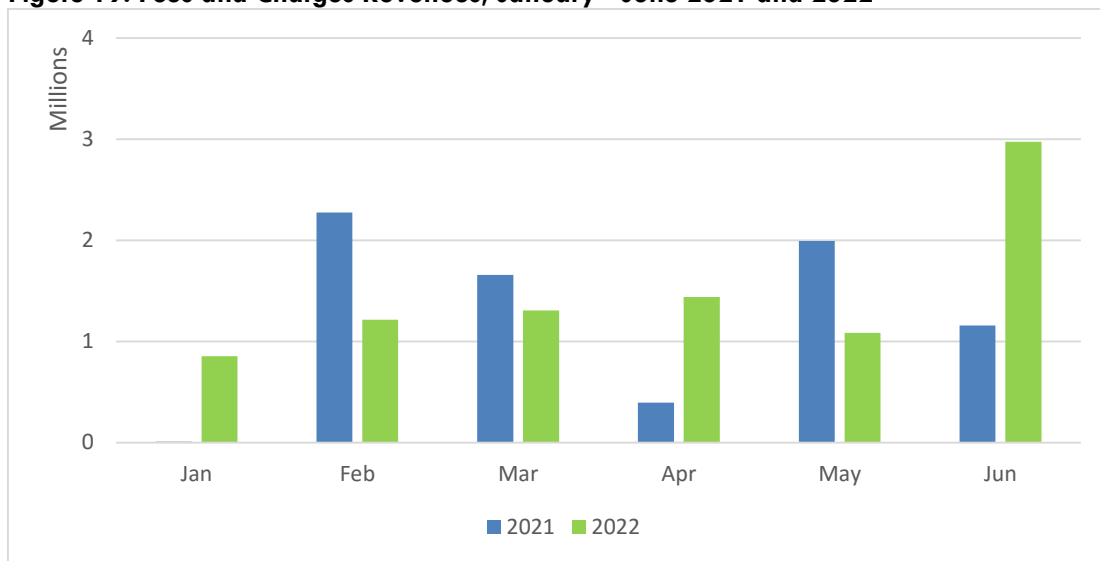
The highest revenue collection of fees and charges came from property rentals which saw a 64% increase between Q1 2021 and Q1 2022 and a 16% increase between Q2 2021 and Q2 2022. Among the top fees and charges (shown in figure 20) all items saw increases in Q2 of 2022 from 12 months before hand.

Passport and ID fees saw a dramatic increase of 1056% between Q2 2021 and Q2 2022 indicating a greater demand among Timorese people to work and study abroad. This is likely a result of the backlog of people who weren't able to travel in 2021 due to international travel restrictions. Similarly increases in Visa fees between Q1 2021 and Q1 2022 (85%) as well as between Q2 2021 and Q2 2022 (194%) was reflective of an increase in visitors as international travel started to recover from its previous decline during the COVID-19 pandemic.

Social games receipts saw increases of 92% and 378% respectively in Q1 and Q2 compared to 12 months ago. Collections for Social games receipts are on track to recover to pre-COVID levels this year. 2019 and 2020 saw significant falls in these collections due to a combination of COVID-19 related movement restrictions and a lack of human resource to control activities related to the games.

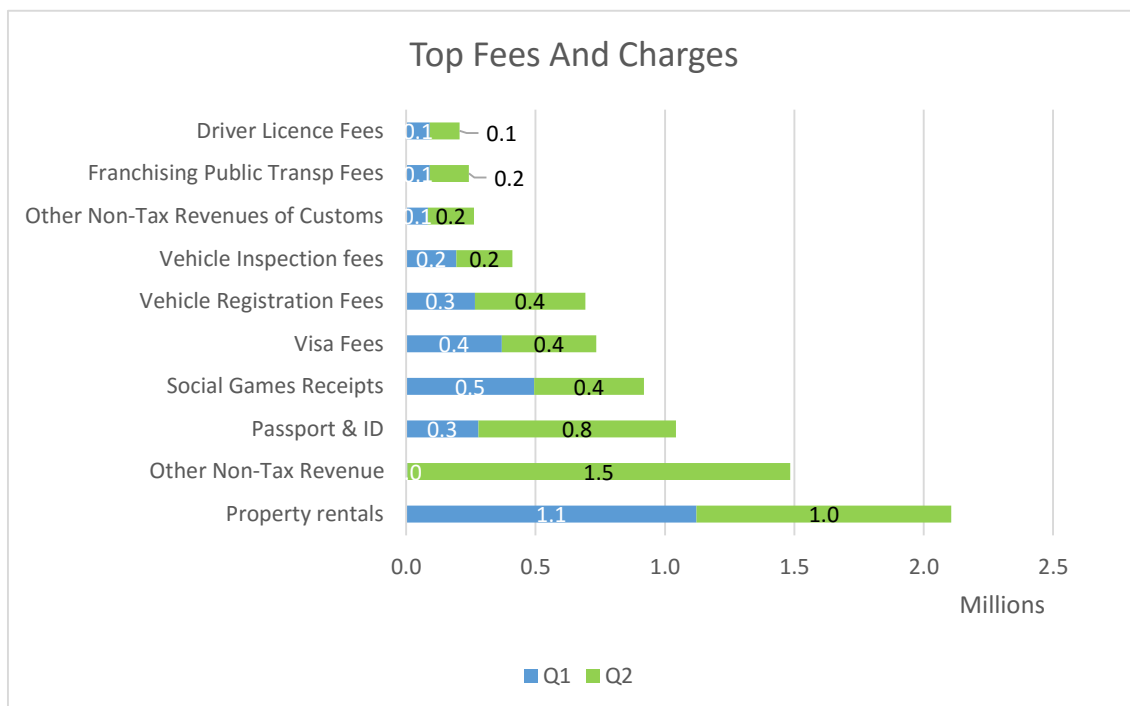
"Other non-tax revenue" saw significant collections during the first 6 months of the year. Whilst collections declined in Q1 (from 12 months ago), the collection in Q2 2022 was 916% higher than 12 months previously. This meant overall collections are \$1.2m higher in the first 6 months of 2022 than the entire collection for 2021. The large increase is not unusual as "Other non-tax revenues" tends to be a fairly volatile revenue category. Vehicle Registration and Inspection fees saw a similar pattern. Whilst they witnessed a modest decline in Q1 2022 (compared to the previous year) they were significantly higher in Q2 meaning that the collections for the year are on track to overtake the revenues collected in 2021.

Figure 19: Fees and Charges Revenues, January - June 2021 and 2022



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

Figure 20: Top Fees and Charges, Q1 and Q2 2022



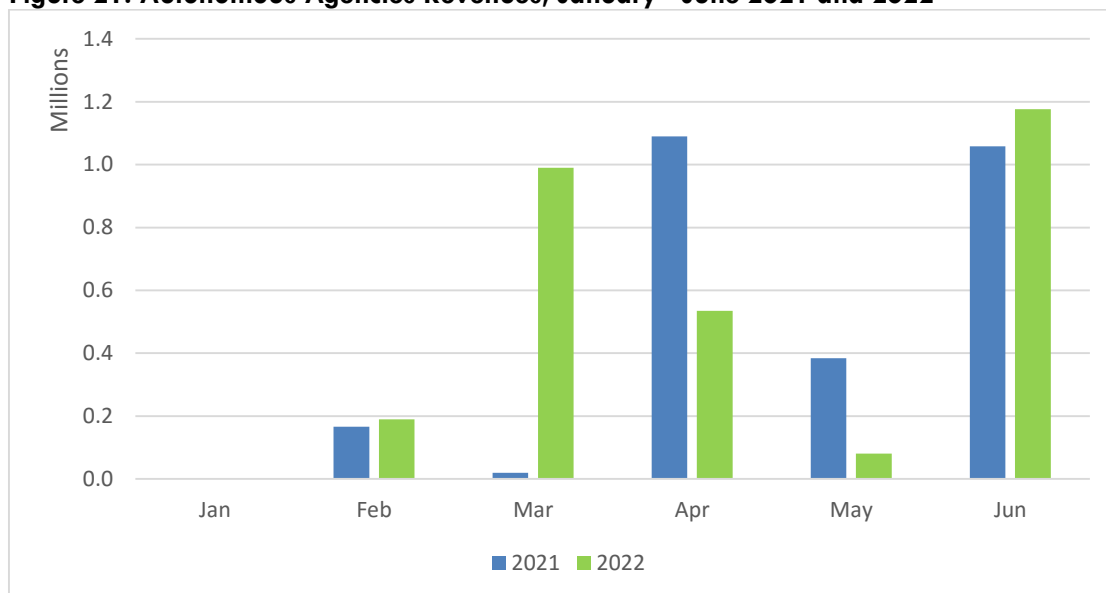
Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Autonomous Agencies collected \$16.6 Million of collections in 2021. So far in 2022, only 3 Autonomous Agencies have reported any revenues. By the end of Q1, only two Autonomous Agencies: (Autoridade Nacional de Comunicações (ANC) and APORTIL reported revenues. During the first six months of this year ANC has seen a 212% increase in revenues from the first 6 months of the previous year. APORTIL however has seen a 12% decline but is the autonomous agency with the highest collections so far in 2022, with revenues of \$1.4 million.

Universidade Nasional Timor-Lororsae did not report any revenues in Q1 but reported revenues of \$780,000 in Q2 which means in the first 6 months of this year their revenues are 7% higher

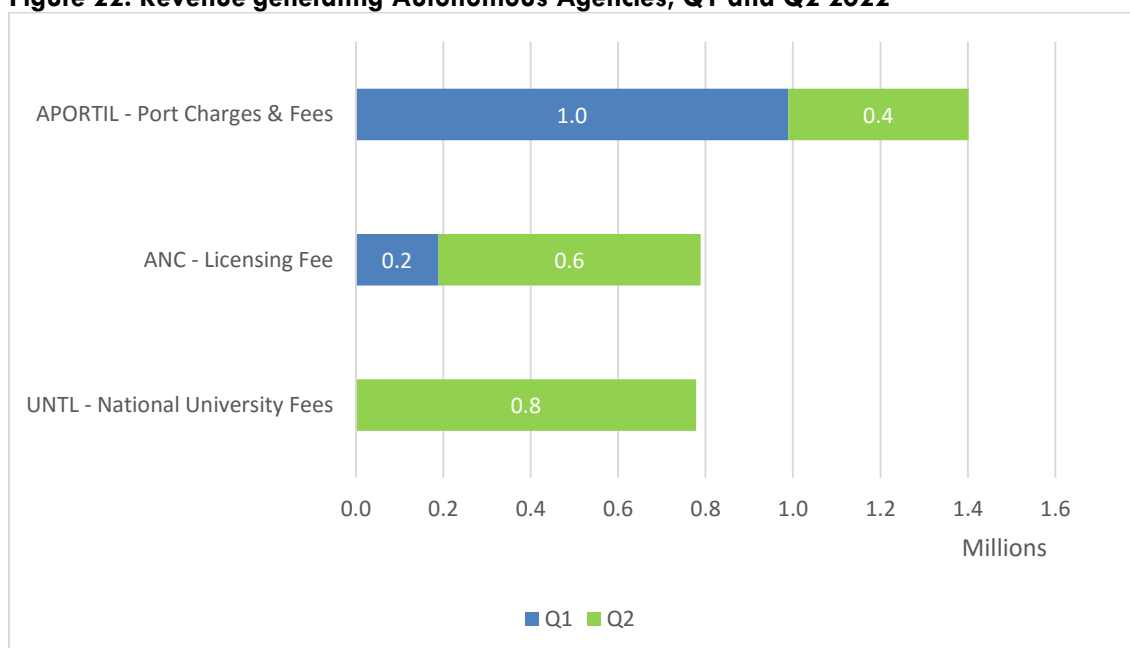
than in the first 6 months of the previous year. There are a further 8 Autonomous Agencies that reported revenues last year but have yet to do so in 2022. These include the National Logistic Centre (CLN) and the national hospital.

Figure 21: Autonomous Agencies Revenues, January - June 2021 and 2022



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

Figure 22: Revenue generating Autonomous Agencies, Q1 and Q2 2022



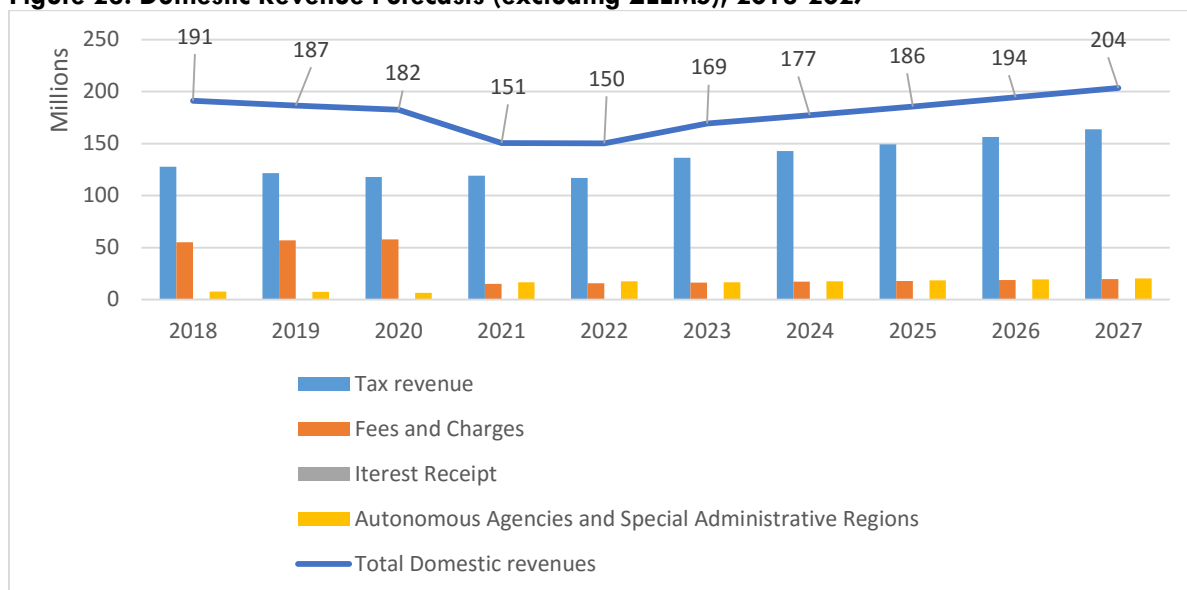
Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

3.4.3 Revenue Projections

In 2022, domestic revenues are predicted to reach similar levels to the collection in 2021. This is because the country is still recovering from the economic downturn associated with the COVID-19 global pandemic. 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 2022. New consumption taxes, introduced in 2022 are also projected to increase tax revenues by up to \$15m a year from 2023 onwards.

Figure 23: Domestic Revenue Forecasts (excluding ZEEMS), 2018-2027



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022.

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), which aims to increase the Tax Authority’s capacity to enforce greater tax compliance. Tax Revenues could also be boosted by 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 has plans to seek the opinion, comments and feedback from a third party on the draft law prior to submission and presentation to Council of Ministers and to parliament.

Furthermore, VAT is a complex tax, which comprises of settlement and deduction operations carried out by the economic agents in every step of the consumption chain. This requires adequate administrative scrutiny and cross-check mechanisms that are not yet in place in the context of a significantly informal economy. Thus, in order to enable the operationalization of VAT, there is also some need to set up legal infrastructure beforehand, namely the introduction of a universal and mandatory issuance of a tax identification number for every citizen, the introduction of accounting standards and account certification requirements for certain businesses, as well as the reinforcement of the inspection powers of the Tax Authority.

Given the need to ensure that the aforementioned preconditions are met before the operationalization of VAT, the collection of substantial revenues from this tax might not be achieved before the end of the current forecasting period (i.e. around 2027).

The move towards 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

The Petroleum Fund projections are updated once a year as part of the final budget process. However, since there have been a number of significant events that will affect the Fund going forward, projections in this Pre-Budget Statement are adjusted to reflect the actual information available for 2020, 2021 and the first half of 2022, as well as the Grand Options Plan approved in May 2022. Projections for 2023 are subject to revision in the final 2023 Budget to be submitted to Parliament in October.

The balance of the Fund is determined by inflows from petroleum revenues, investment returns and outflows from Government withdrawals. 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 the end of 2022. 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.

Petroleum revenues are mainly driven by three major factors: the oil and gas price, production and costs. The projections in the State Budget 2022 were based on the EIA's projected Brent price in September 2021. The production and costs information were provided by the Operator in July 2021. New information will be available in August 2022 which will be incorporated into calculating the ESI for Budget 2023 and projecting future revenues.

The Brent oil price has been averaging about \$68/barrel since it reached its lowest in 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 and 71/barrel in 2021. For 2022, the average price from January to June was \$107 per barrel, much higher compared to \$44.1/b used in Budget 2022. According to EIA's Short-term energy outlook released in July, the Brent price is forecasted to average at \$104/b in 2022 and \$94/b in 2023. The price will continue to fluctuate due to: uncertainty around the Russian-Ukraine crisis with the EU agreeing to ban seaborne Russian oil deliveries, the risk of global recession driven by monetary tightening policy, inflation, and continued supply constraints.

Actual oil and gas production increased slightly from 35.6 million barrels of oil equivalent (BOE) in 2020 to 37.2 million BOE in 2021. For 2022 the forecasted production is 11.7 million BOE, while the actual production from January to May was 9.3 million BOE. At this stage, there is no new production beyond 2022.

The Fund's balance in 2020 has been revised up by \$615.7 million from \$18,289.3 million estimated in Budget 2022. This follows the completion of the valuation of the Petroleum Fund's loans to the Timor Gap. As discussed at length in the Petroleum Fund Annual Report for FY 2020 published in April 2022, the loan instrument is now measured at fair value rather than at amortized costs. In Budget book 2022, the loan, valued at \$701.35 million on 31 December 2020, was excluded from the estimated balance in 2020 due to the ongoing valuation of the value of the loan by an independent third party which was completed in February 2022. The finding was that the instruments were performing loans in that there were expected to be sufficient cash flows from the underlying assets for Timor Gap to meet its obligations. An agreed discount rate of 5.62% was used to estimate its value at December 2020 at \$615.7 million, resulting in a fair value loss of \$85.65 million, compared to 'nil' that previously used to estimate the Fund's closing balance and ESI 2022 calculation. During the 2020, the Fund received \$326.2 million of payments of petroleum taxes, royalties and profit oil and \$886.3 million out of \$963.9 million approved by the Parliament, was transferred to the state budget. Thus, the Fund's closing balance at 31 December 2020 was \$18,905.0 million.

During the 2021, the Fund's balance increased by \$660.1 million to end the year at \$19,565.0 million. Petroleum revenues contributed \$719.6 million to the Fund, while the investment return was \$1,088.5 million over the year. A total of \$1,147.9 million out of \$1,337.6 million approved by the Parliament, was withdrawn to finance the Government's expenditure. Note that the Fund's investment return and balance are subject to change to account for the ongoing valuation of the value of the loans at 31 December 2021.

For 2022, petroleum revenue was estimated at \$45.6 million. As of May 2022, receipts from the sale of oil and gas amounted to \$568.3 million, this is 8 times higher than the projection used in the Budget 2022 as the prices of the oil and gas were nearly two times higher than estimated. The revenues also include a transfer of profit oil for Q4 2021 totalled \$358 million made in February 2022. The Fund's investment return is negative 6.5%, which translates to a loss of \$1,431.2 million.

Table 5: Petroleum Fund Revenues 2020-2022 (\$m)

	2020 Provision	2020 Actual	2021 Provision	2021 Actual	2022 Budget	2022 As of May
Total Petroleum Fund Revenue	1,483.8	2,099.4	1,412.2	1,807.9	491.3	-862.9
PF Investment return, net	1,157.6	1773.3	1,184.0	1088.3	445.6	-1,431.2
Petroleum Revenue	326.2	326.2	228.2	719.6	45.7	568.3
Petroleum Taxes *	131.9	145.5	122.5	400.5	14.7	168.8
Royalties and Profit oil	164.5	164.6	88.1	309.8	20.9	399.6
Other Taxes payment **	29.8	16.1	17.6	9.2	10.1	0

Source: Petroleum Fund Policy and Management Office, Ministry of Finance, July 2022

* 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.

Revenues for 2022 are estimated to reach over \$600 million by the end of the year, while other projections for future revenues will be made in September 2022 when the new information from the operator is incorporated into the ESI 2023 calculation. However, based on the recent information available, the future petroleum revenue will be a lot lower 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.

As mentioned above, the Fund registered a mark-to-market loss of \$1.4 billion as May 2022, or about -6.5%. This is well within the range of expected returns during an adverse event. Global uncertainty, rising interest rates and lower growth are all negatives for equities. The MSCI World's return is -13% for the year until May and has fallen further in June. An overweight to value and quality stocks has allowed the Petroleum Fund's equity portfolio to perform a little better than the benchmark and post a return of -11.9% for the year until May. The return on the growth portfolio is -8.04% until May. The value of the liquidity portfolio has been relatively stable and ended at \$2,975 million. The portfolio has recorded a small year to date loss of 0.8% because shorter-term interest rates have risen sharply with the sudden shift in Fed policy. Future cash returns will benefit if rates continue to rise as expected.

The Fund is a relatively long-term investor that can ride through adverse periods. We do not seek to time markets and have benefitted from a long-term approach in the past. For example, in the first quarter of 2020, equities lost well more than \$1 billion as a result of the COVID outbreak and lockdowns. The PF maintained its equity allocation and the strong subsequent recovery contributed to the \$1.8 billion net profit at the end of 2020. The Fund's significant allocation to cash and short maturity bonds in the liquidity portfolio provides some protection in absolute return terms. In addition, the Fund is currently seeking to implement a new mandate by having an allocation to US Treasury Inflation Protected Securities, which will outperform in a high inflation regime.

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 \$544.1m in the 2022 Budget is maintained despite Fund's actual outcome for 2020 and 2021 are much higher than estimated in September 2021 as discussed above. For example, if we are to recalculate the 2022 ESI using the new information, the result will be \$608.4 million. Table 2 shows the estimated Petroleum Wealth and the ESI from 2020, 2021 and 2022 as approved in each respective fiscal years. For 2023, the preliminary ESI calculated based on the current development in the Petroleum Fund until May 2022. The final figure will be determined in September 2023.

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

	2020 Budget	2021 Budget	2022 Budget	Preliminary ESI 2023
Estimated Sustainable Income (PWx3%)	544.4	547.9	554.1	483.6
Total Petroleum Wealth (PW)	18,145.0	18,262.5	18,469.3	16,119.4
Opening PF Balance	17,691.8	18,065.7	18,323.8	16,016.4*
Net Present Value of Future Revenues	453.2	196.8	145.5	103.0

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

The revised Petroleum Fund balances are shown in the table below and take into account the actual result in 2020, 2021 and 2022 discussed above.

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

	2020 Actual	2021 Actual	2022 Initial Budget	2022 Rectification Budget	2023 Pre-Budget
Opening PF Balance	17,691.8	18,905.0	18,323.80	18,323.8	16,016.4
Petroleum Revenue (excluding PF Interest)	326.2	719.6	45.6	45.6	104.2
PF Interest, Net	1,773.30	1,088.3	442.30	442.3	436.4
Total Withdrawals	-886.3	-1,147.9	-1,311.4	-2,552.6	-1,346.1*
Closing PF Balance	18,905.00	19,565.1	17,500.3	16,259.1	15,210.9

Source: Petroleum Fund Policy and Management Office, Ministry of Finance, 2022. * expected withdrawal as approved in the Grand Plan Options.

Where: PF Interest, Net = PF Net Investment Return

The proposed withdrawal for the FY 2022 increased from \$1,377.6m to \$2,552.3 million following the approval the rectified budget for 2022, which includes \$1 billion for the creation of the *Fundo dos Combatentes da Libertação Nacional (FCLN)*. This is four times over the 3 per cent ESI. Since 2009, the withdrawal is averaging at 5% of Petroleum Wealth and the cumulative withdrawals totalled \$14,068.7m (over \$14bn). From January to May 2022, \$450m has been transferred to the State Budget and the Balance of the Petroleum Fund is \$18.3 bn.

Petroleum revenues from Bayu-Undan will end this year and the outlook for financial markets is challenging. The Fund's balance is forecasted to reach \$16.0 billion by the end of 2022 and to

\$15.2 billion in 2023. The Fund is expected to fall in value at least until there are inflows from Greater Sunrise. The balance was able to grow in the last three years 2019-2021 mainly because lower withdrawals, higher than estimated petroleum revenues and investment return which was driven by equity market performance was well above current expectations. A careful fiscal planning is needed now rather than later. This includes more emphasis on projected expenditure and withdrawals over the medium-term to help ensure fiscal policy is sustainable and avoid the prematurely depleting the fund. This will also allow better management of the risk in the investment portfolio.

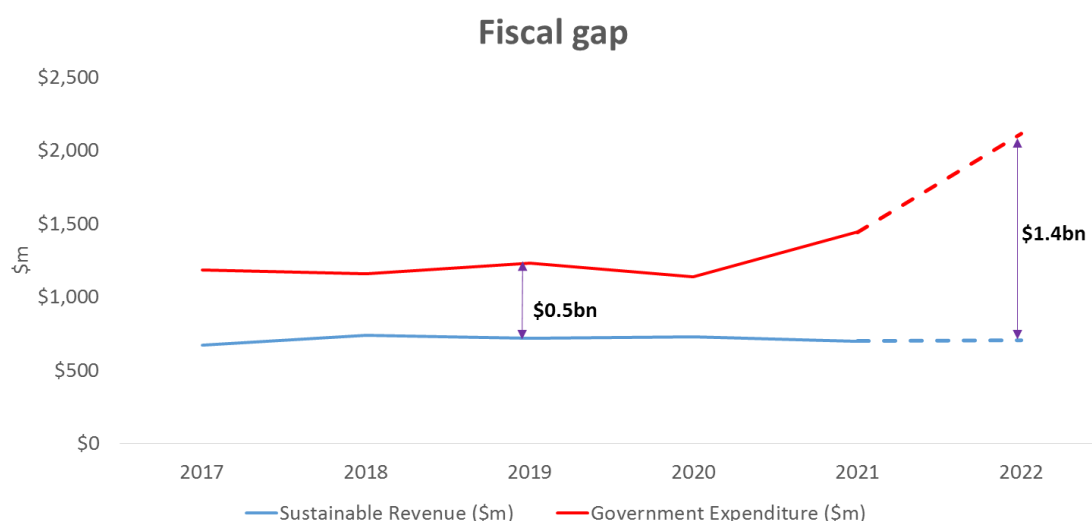
3.7 Fiscal Sustainability Analysis

Over the past decade the bulk of government spending has been financed by withdrawals from the Petroleum Fund. Withdrawals from the fund have averaged more than \$1bn a year, whereas non-oil domestic revenues have been below \$200m annually. This means that fiscal sustainability is closely tied to the longevity of the Petroleum Fund.

Petroleum Fund withdrawals are comprised of two parts: Estimated Sustainable Income or ESI (which is 3% of the total value¹ of the fund in any given year) and Excess Withdrawals (any amount above the ESI. Limiting Petroleum Fund withdrawals to ESI ensures that the Petroleum fund lasts in perpetuity.

Not including funding from development partners, this means that the government can rely upon sustainable revenue sources that sum to the total of domestic revenues and ESI. Over the past 5 years sustainable revenue sources have averaged at \$710m a year. However government spending has exceeded total sustainable revenues. As shown by the Figure below, the fiscal gap (the amount by which government expenditure exceeds sustainable revenues) has increased since COVID. In 2022, the fiscal gap is set to be almost three times higher than pre-COVID levels.

Figure 24: Growth in Fiscal Gap Post COVID, \$millions



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

¹ Total value including the net present value of future revenues.

The fiscal gap is almost entirely financed by excess withdrawals from the Petroleum Fund. As shown in the figure above, this current spending trajectory means that the fund is projected to fully deplete by 2035.

The Ministry of Finance conducts 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. The model predicts that between 2022 and 2027 domestic revenues will rise in line with forecasts from the National Directorate of Economic Policy at the Ministry of Finance. It predicts that in the long run, domestic revenues will increase in line with long run inflation and population growth assumptions². The model also uses up to date assumptions on the estimated rate of return on petroleum fund from the Petroleum Fund Unit in the Ministry of Finance. Changes to any of these assumptions would have significant changes on the forecasted end date of the Petroleum Fund. For example, if the domestic revenue growth or investment returns are lower than 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. 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 negative economic consequences from 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.

Below we present three different expenditure scenarios and how they would impact the potential life-span of the Petroleum Fund.

3.7.1 Petroleum Fund Depletion under Different Expenditure Scenarios

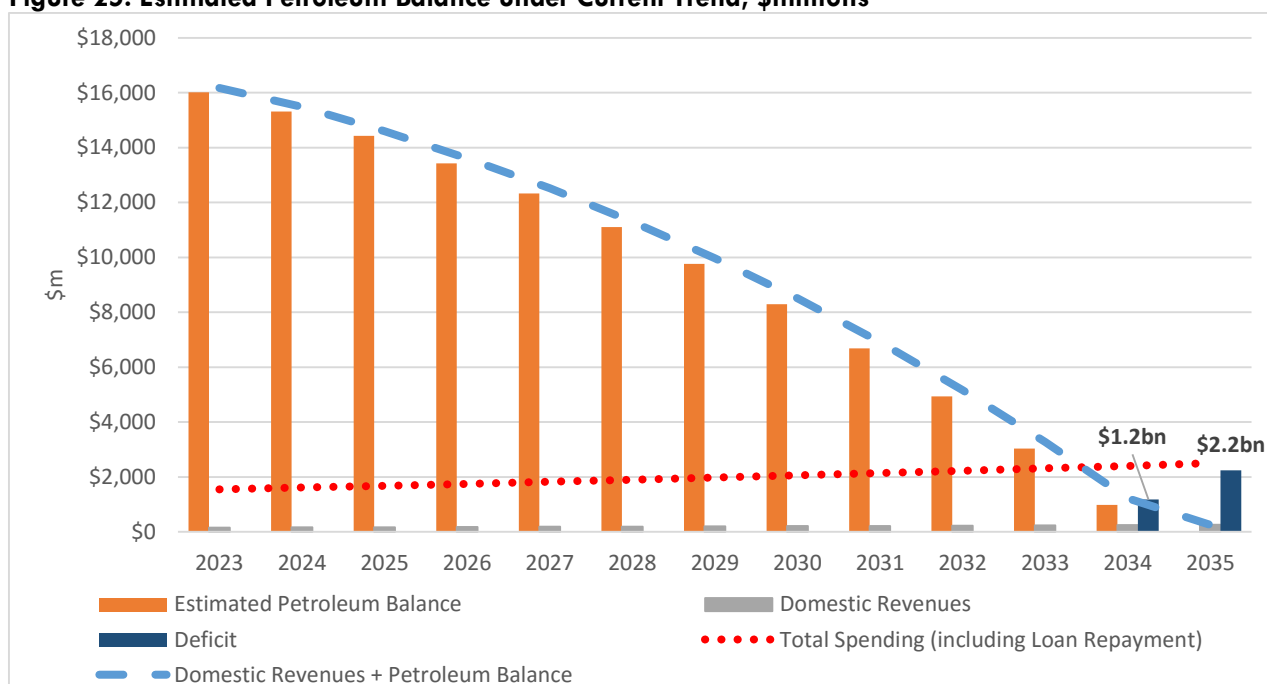
Scenario 1 – Current Expenditure Trend

The figure below projects the life of the Petroleum Fund under the current expenditure trajectory. The blue dotted line shows total available revenues (this is the sum of the petroleum balance and domestic revenues and excludes funds through new loans or from development partners). The red dotted line shows total expenditure. The large orange bars show the depletion of the petroleum fund which is projected to fully deplete by 2035.

This scenario factors in the approved GOP ceiling for 2023 and assumes that beyond that expenditure will continue to increase in line with long run inflation and population growth (i.e. at 4% nominal growth a year). Under this scenario by 2024, projected expenditure is likely to exceed total available revenues by \$1.2bn. This means that under current spending plans in 2034, the government would to cut spending by 50% and by a further 80% the following year. It should be noted that the petroleum fund will deplete earlier than projected by this scenario if expenditure is increased beyond 4% a year.

² Long run population growth is assumed to be 2% Long run inflation is assumed to be 2% as well

Figure 25: Estimated Petroleum Balance under Current Trend, \$millions

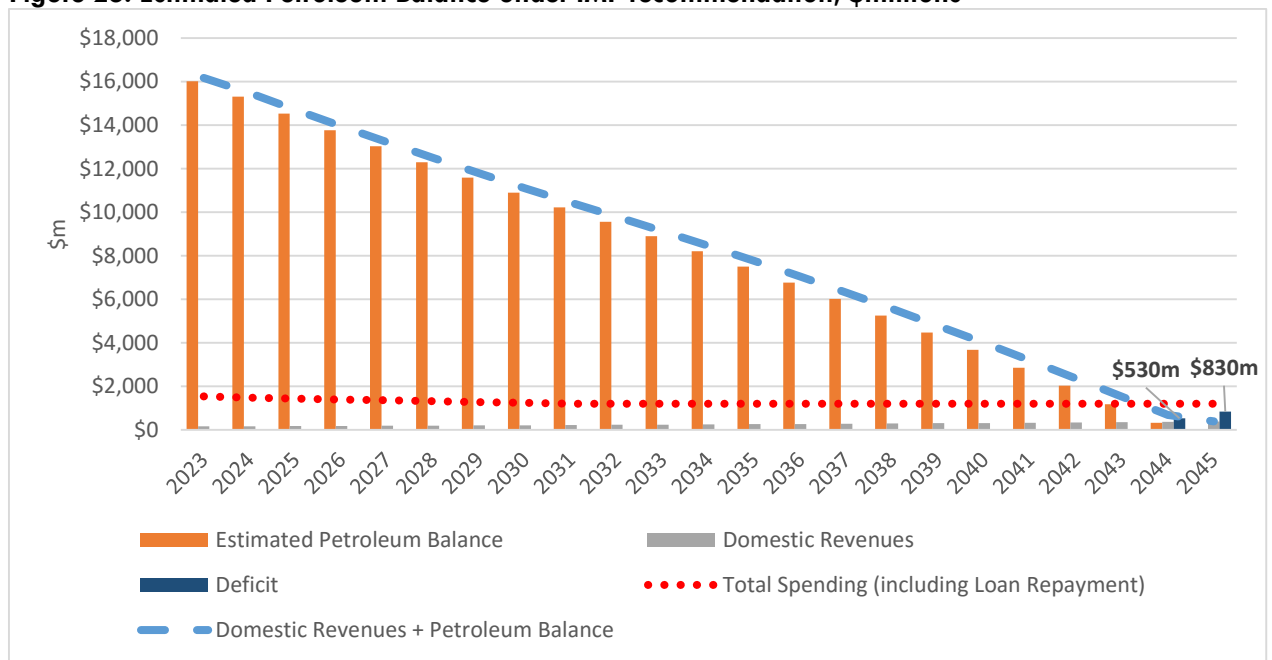


Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

Scenario 2 – Follow IMF recommendations for expenditure

In June 2022, the IMF recommended the government of Timor-Leste to reduce the fiscal gap to pre-COVID levels by limiting government expenditure to \$1.2bn. In Figure 26, we model the impact of a gradual reduction in spending to \$1.2bn followed by a spending freeze at that level. In this scenario the government reduces nominal expenditure (excluding expenditure financed by loans or by development partners) by 3% a year up until it reaches \$1.2bn by around 2031. Fixing expenditure at \$1.2bn at that point would mean that the Petroleum Fund would not deplete until 2045. This would allow for another decade to build up domestic revenues and to diversify the economy so that it is no longer dependent on Petroleum Fund Revenues.

Figure 26: Estimated Petroleum Balance under IMF recommendation, \$millions



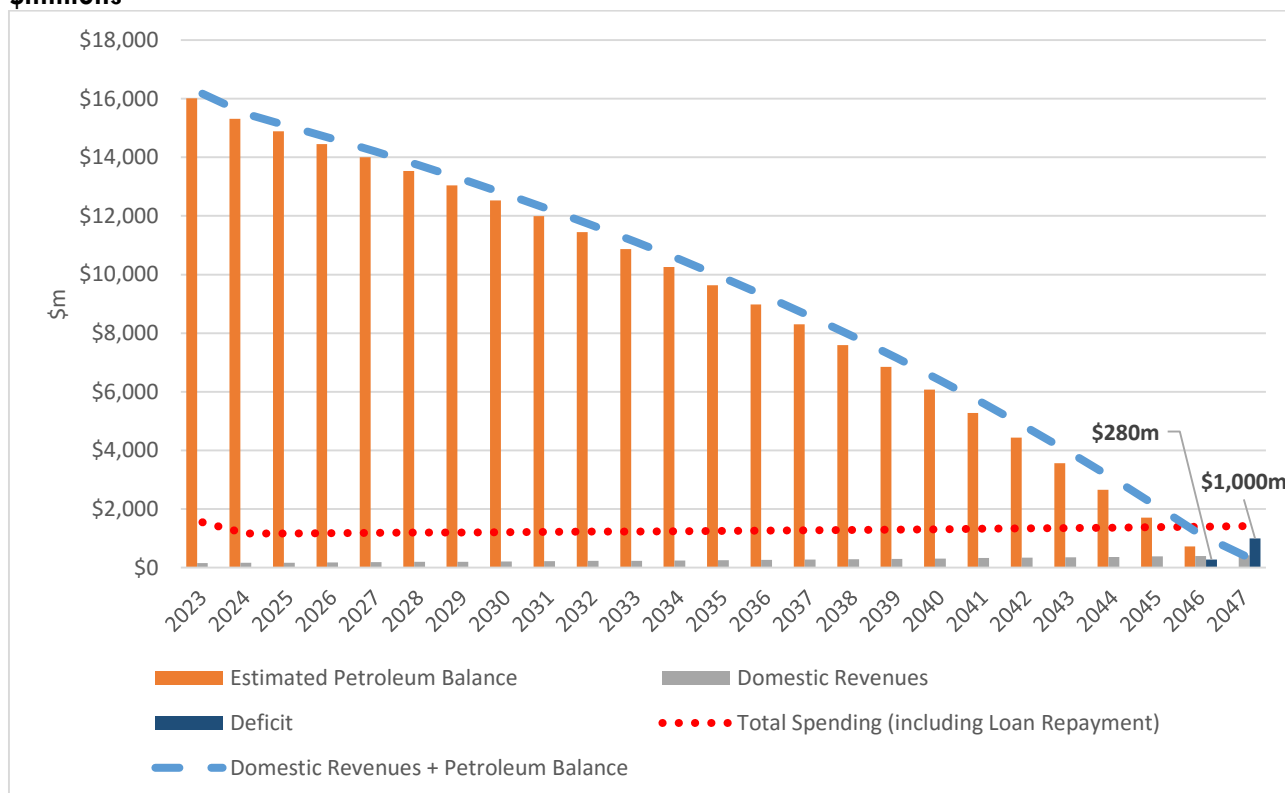
Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

Scenario 3 – Petroleum Fund Withdrawals Capped at \$1.2bn a year

The final scenario modelled, in the figure below, is one where Petroleum Fund withdrawals are capped at \$1bn a year until the point that the fund fully depletes. Under this scenario the Petroleum Fund would fully deplete in 2047, giving the government an additional 12 years to prepare for this eventuality as compared with the current trajectory.

The modelling results demonstrate that delaying the point at which the Petroleum Fund depletes will reduce the scale of the spending cuts required. In the section below, we point out that a second key advantage is that it allows more time for the government to implement strategies to mitigate the economic consequences from depleting the Petroleum Fund.

Figure 27: Estimated Petroleum Balance if petroleum withdrawals are capped at \$1bn, \$millions



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

3.7.2 Mitigation Strategies

Depleting the Petroleum Fund sooner will force the government to carry out large cuts in government spending. Under the current spending trajectory over \$3bn worth of spending cuts would need to be implemented in 2034 (see scenario 1). This would result in a large shock to GDP, likely resulting in large rises in unemployment and large falls in incomes, the provision of public services and ultimately living standards.

This eventuality also has implications for the country's ability to continue importing to the same scale and circulate currency internally. The country is currently able to sustain a dollarized economy due to the fact that Petroleum Fund revenues guarantee a regular supply of US dollars. A large non-oil trade deficit (projected to be greater than \$900m in 2022) is only possible with a dollarized economy because inflows of dollars from the Petroleum Fund are able to replace the large outflow of dollars that is spent on imports.

If a currency alternative is not in place well in advance of the point that the Petroleum Fund depletes, persistent trade deficits could spark a liquidity crisis. Without the use of Petroleum Fund inflows to finance the outflow of US Dollars from expenditure on imports, individuals and businesses could find themselves without the currency needed to finance day to day transactions.

Above we presented results from our economic model where we showed how gradual cuts to expenditure can improve fiscal sustainability.

A complementary strategy is to seek alternative revenue sources. This includes introducing fiscal reforms to supplement domestic revenues such as introducing new taxes and widening the tax base. Prioritising measures to diversify the economy can also boost GDP growth and therefore lead to further increases in domestic revenue (by boosting individual and business income). Economic

diversification can also broaden opportunities for private sector investment and therefore reduce the need for government investments.

Finally, the government can also reduce the amount of excess withdrawals through sustainable debt financing for long term investments. The Debt to GDP ratio in 2021 was around 13% which is one of the lowest levels at the world. This means that there is some (albeit limited) scope to increase financing from loans and continue to borrow at sustainable levels provided that loans are used for long term investments.

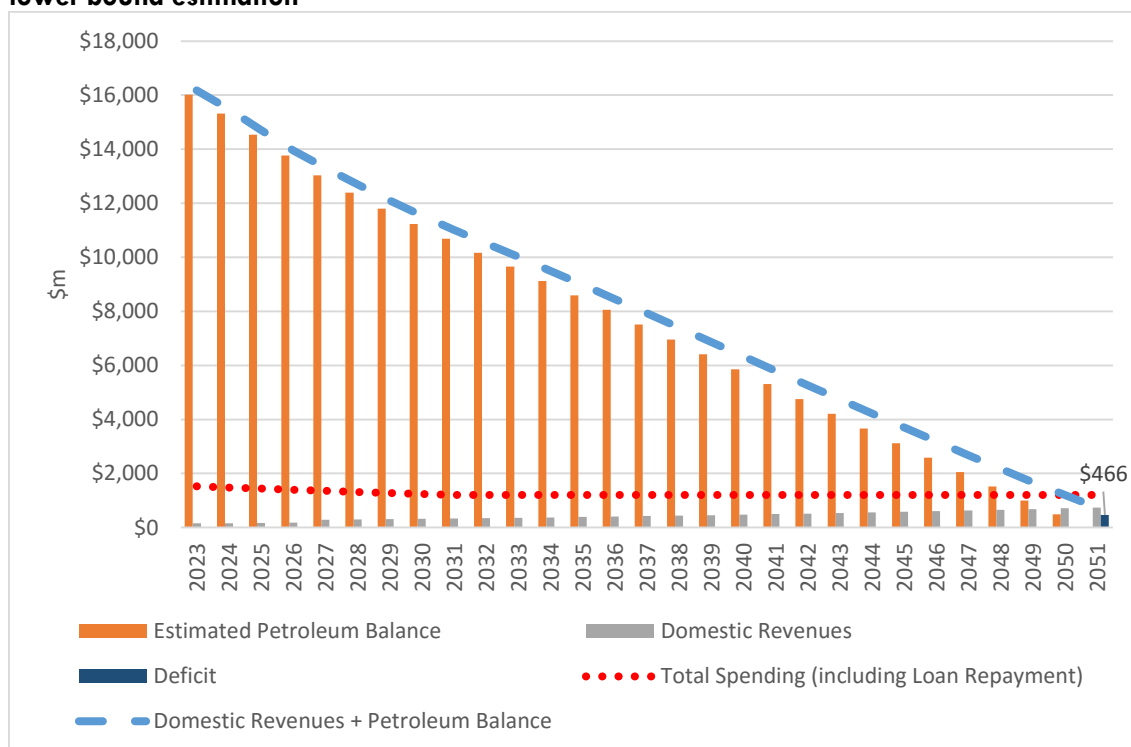
3.7.3 Example pathway for Fiscal Sustainability

In this section we present an example of how a combination of gradual spending cuts and moderate fiscal reforms can put Timor-Leste on a more fiscally sustainable pathway. Using the Fiscal Sustainability Model we demonstrate that if gradual spending cuts are implemented (as shown in expenditure scenario 2 above) alongside the implementation of VAT and property taxes by 2027 the Petroleum Fund can last till 2051. Furthermore under this scenario at the point that the fund depletes, the gap between spending and available revenues would be reduced to less than \$500m.

The scenario is presented in the figure below. As with expenditure scenario 2 presented earlier, here we assume that the government reduces spending (excluding new loans and development partner funded spending) by 3% a year until spending reaches \$1.2 billion at which point spending is frozen. Here we also assume that the government implements VAT and property taxes by 2027. Preliminary estimates from the National Directorate for Economic Policy at the Ministry of Finance suggest that these taxes could raise a lower bound figure of around \$100m a year.

Under this scenario, by the time the Petroleum Fund depletes, domestic revenues would be able to finance \$740 million of spending. However this figure could be greater if extra years of petroleum revenues are used to successfully diversify the economy and achieve further revenue growth.

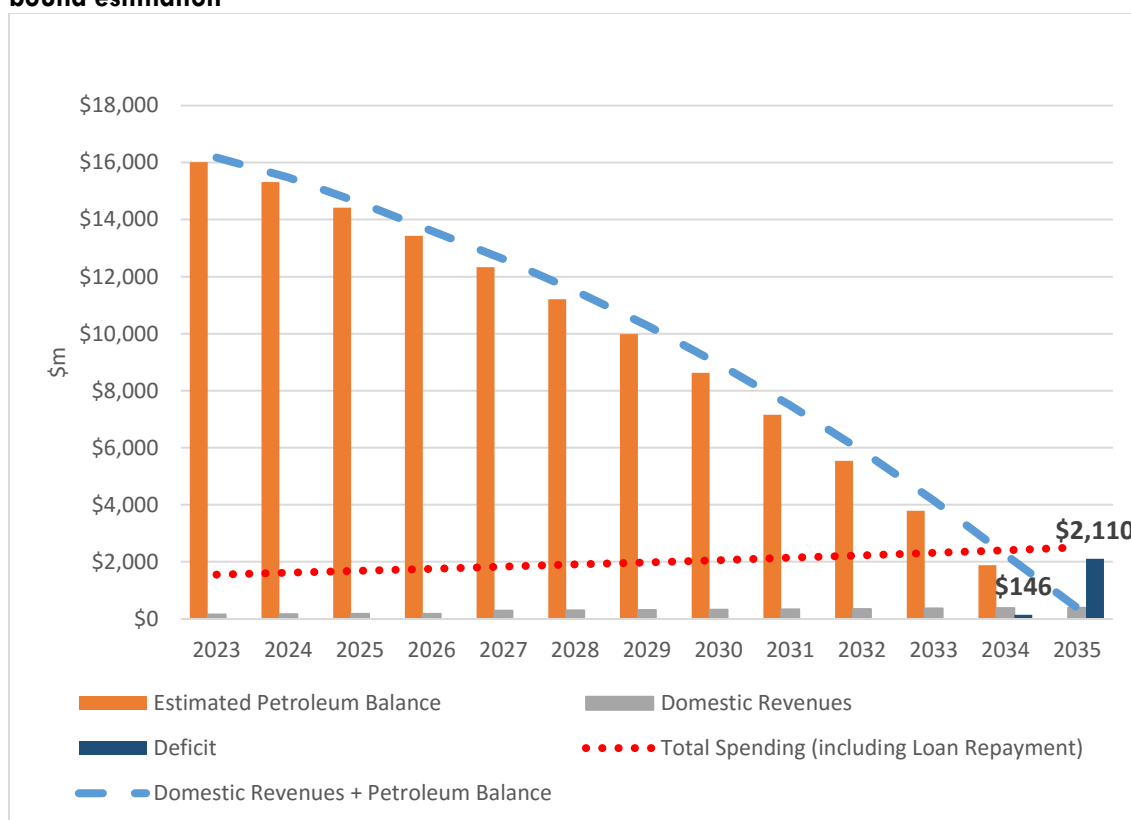
Figure 28: Estimated Petroleum Balance under IMF recommendation + VAT and Property tax lower bound estimation



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

Our modelling also shows that fiscal reforms alone will not be sufficient to achieve a path to fiscal sustainability. Below we model a scenario where additional tax revenues from preliminary estimates of VAT and property tax collection are introduced in 2027 but where the current trend of spending continues. Under this scenario the Petroleum Fund is expected to fully deplete by 2035 at which point there would be a \$2bn gap between spending and revenues.

Figure 29: Estimated Petroleum Balance under Current Trend + VAT and Property tax lower bound estimation



Source: National Directorate of Economic Policy, Ministry of Finance, July 2022

3.8 Fiscal Risks and Contingent Liabilities

Timor-Leste, like any other nation has a number of contingent liabilities, i.e. 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’s responsibility to identify, manage and mitigate risks to reduce to possibility of unexpected pay outs. The

government will aim to provide comprehensive disclosure and publish a Fiscal Risks Statement in the coming years.

4 Social Economic Indicators

It is important to not only use GDP when evaluating the state of an economy. Broader social indicators are also key to develop a full understanding of the position of a country and the impact of government’s policy choices on people’s everyday lives.

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

1. Human Development Index

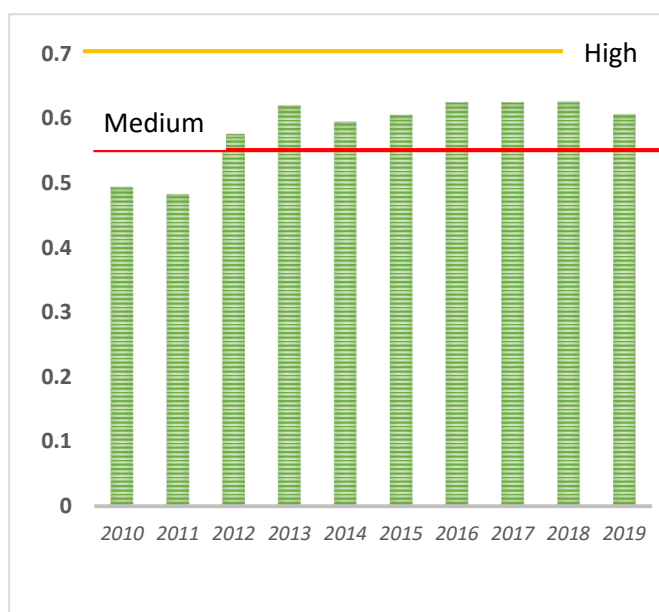
The Human Development Index (HDI) is a summary measure of average achievement in three key dimensions of human development: a long and healthy life, being knowledgeable and have a decent standard of living. The health dimension is assessed using indicators such as life expectancy at birth while the education 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.

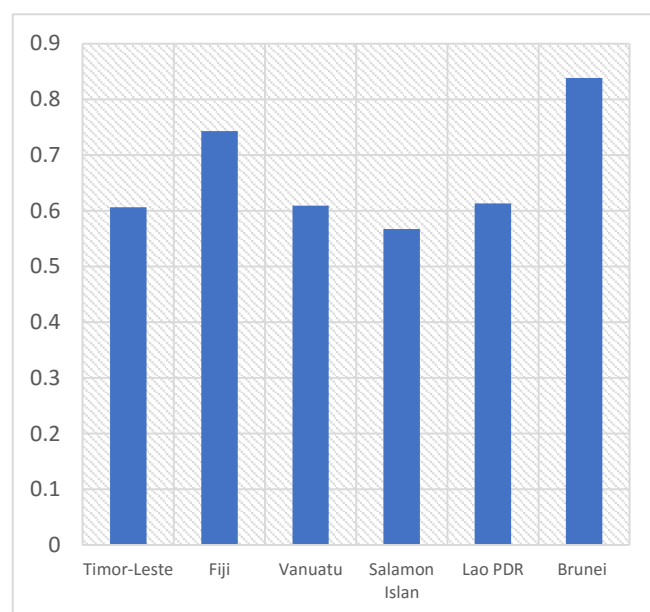
Timor-Leste’s mean years of schooling score was lower than Fiji, Vanuatu, Solomon Island, Lao PDR and Brunei Darussalam in last five years. On the other hand, Timor-Leste has seen progress on the life expectancy score which is now above Myanmar, Lao PDR and Fiji compare to 2018.

Figure 30: Timor-Leste HDI score, 2010 - 2019



Source: UNDP, Human Development Report 2020

Figure 31: Comparison of Timor-Leste HDI with other countries in Asia Pacific, 2019

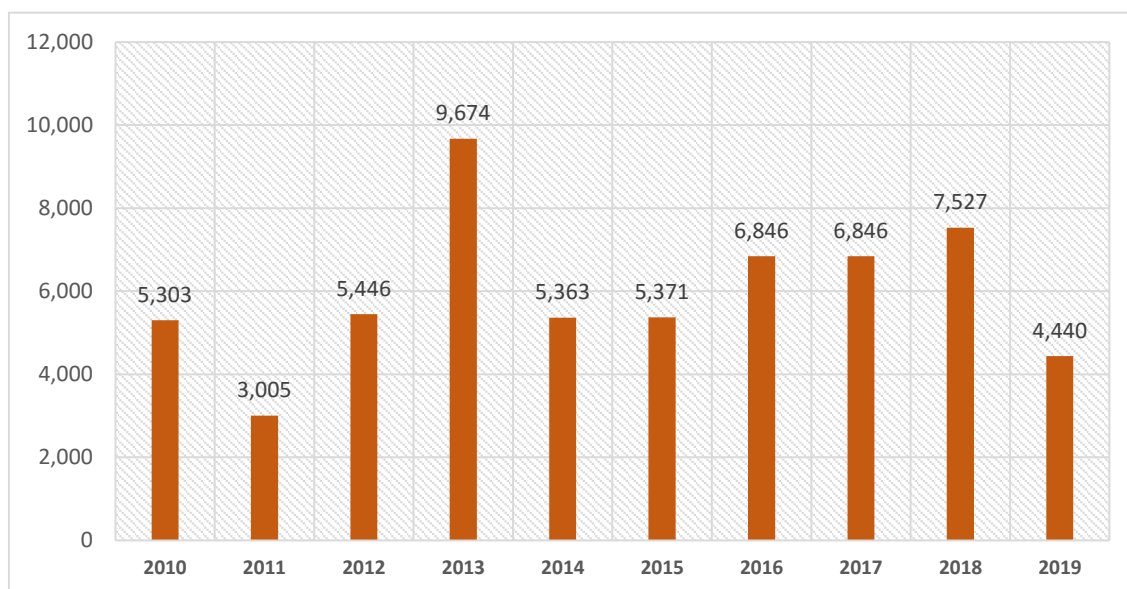


2. Inequality

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 below.

Figure 32: 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 2019 Timor-Leste's female labour force participation rate was 62%, the rate was high compared to the East Asia Pacific region average (57%). In 2016, 64% of Timor-Leste's working-age population was employed. This was lower than the average for its region (65%) but higher than the average for its income group (54%).

7. Adult Survival Rate

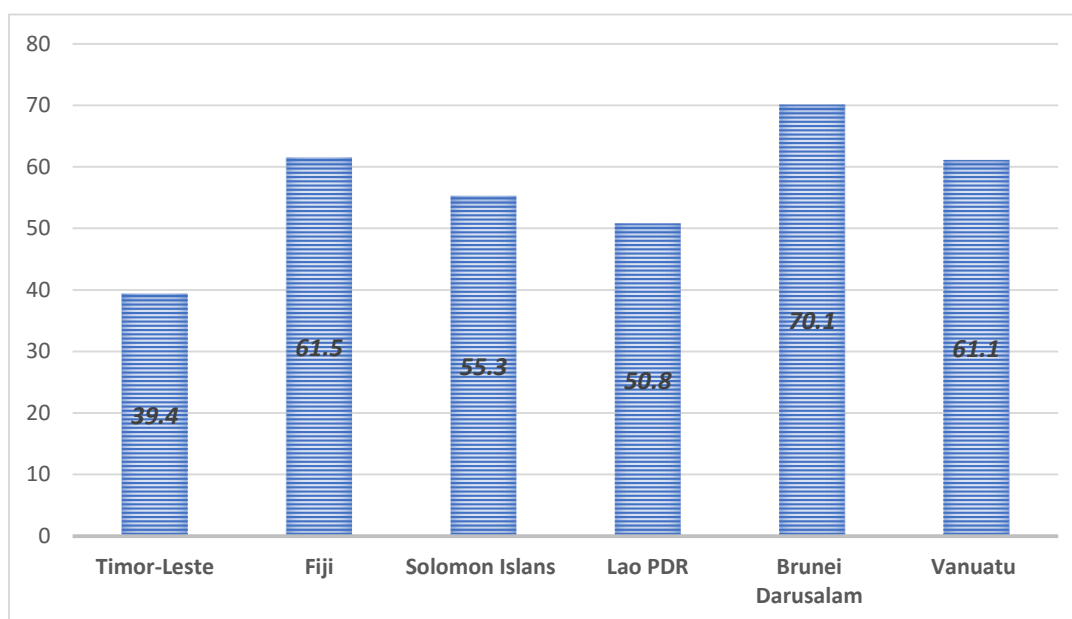
Across Timor-Leste, 86 percent of 15-years old will survive until age 60. This statistic is a proxy for the range of health risks that a child born today would experience as an adult under current conditions.

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 33: 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

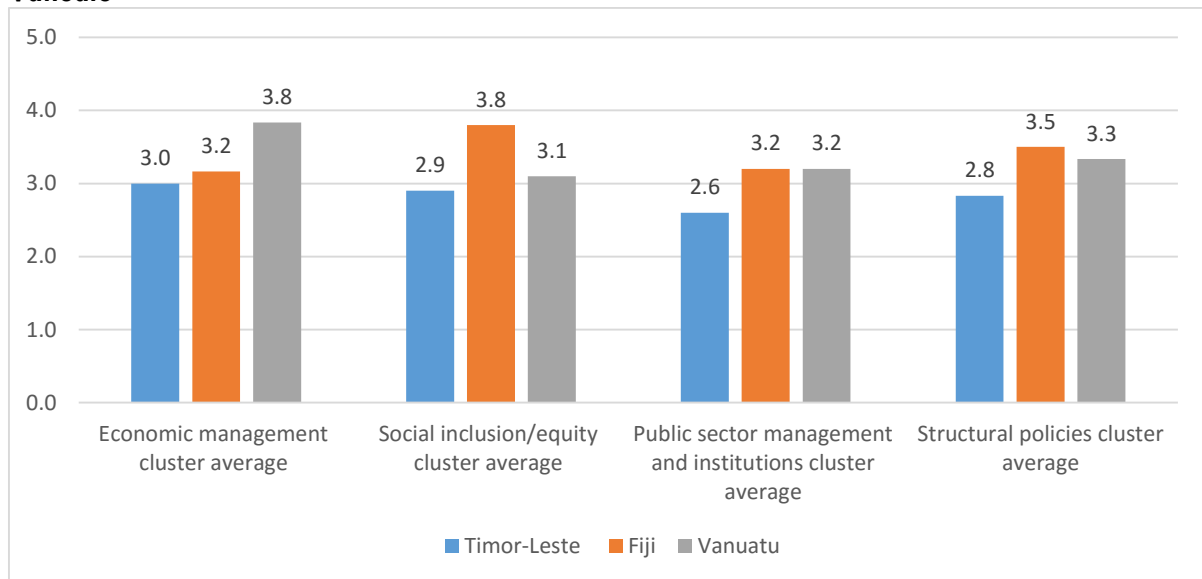
Source: The World Bank, Ease Doing Business Report 2020

9. Country Policy and Institutional Assessment (CPIA)

The Country Policy and Institutional Assessment (CPIA) by the World Bank is a framework to measure and compare countries’ ability to effectively utilise aid. It consists of 16 criteria, each marked out of a possible 6 points, over 4 categories; economic management, structural policy, social inclusion/equality measures and public sector management and institutions.

In 2020, Timor-Leste's highest categories were economic management and social inclusion/equality measures with an average score over the related indicators of 3.0. Public sector management and institutions had the lowest average with 2.6 and structural policy averaged at 2.8. The highest individual score was for Trade at 4 out of 6. The lowest score was 2 out of 6 which was assigned to business regulatory environment, environmental sustainability, property rights and rule-based governance and quality of public administration. In fact Timor-Leste has seen very little change in its scores since they were first collected in 2006. In 2006, the average score across all indicators was 2.7 out of 6. In 2020, it has only risen to 2.8.

Figure 34: Comparison of Timor-Leste's 2020 CPIA cluster average scores with Fiji and Vanuatu



Source: The World Bank, Country Policy and Institutional Assessment 2020.

When comparing with Fiji and Vanuatu, Timor-Leste still has some way to go to improving scores in line with peers. However, scores on the trade rating and transparency accountability and corruption in public sector were more closely aligned with these other small island states.

5 Expenditure Analysis

5.1 Historical Trends

5.1.1 Total level of expenditure

This section will analyse the trends of the last 5 fully executed budgets, i.e. 2017-2021 given that we are mid-way through 2022.

The General State Budget (GSB) for 2021 was originally \$1.895 billion including loans. This was later rectified to include a number of additional support measures in the wake of community transmission of Covid-19 and Cyclone Seroja, amounting to a rectified budget of \$2.03 billion. The total amendment was budgeted as \$198.4 million (of which, \$63.1 million was from a reallocation of current spending) and was financed with an addition of \$135.3 million. Out of this, 76.74% was allocated to recurrent categories.

The materiality directive³ of Timor-Leste states that the government must spend 100% of the budget by the fourth quarter (Q4). The total government execution by Q4, 2021 (by current budget which includes transfers, virements and contingency transfer) was 75.3%. The Infrastructure Fund including loans (IF), Human Capital Development Fund (HCDF) and COVID-19 Fund execution for Q4 2021 stood at 35.3%, 79.4% and 76% respectively.

The highest government expenditure in the last five year period was in 2021 at \$2.03bn with a rectification budget, despite this, Capital and Development execution was particularly low in 2021 (39%) due to lockdowns interrupting infrastructure projects. Larger budgets tend to have lower execution.

Table 9: Government execution of the final budget (2017-2021)

AppCat	2017 Execution	2018 Execution	2019 Execution	2020 Execution	2021 Execution
Capital & Development	71.20%	85.40%	71.50%	73.49%	39%
Goods & Services	86.00%	90.30%	82.70%	66.85%	73%
Minor Capital	66.30%	42.70%	74.00%	58.65%	73%
Salary & Wages	91.80%	96.00%	93.50%	96.85%	92%
Transfers	95.70%	95.60%	93.30%	78.40%	93%

Sources: IFMISU, Ministry of Finance, July 2022

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 2017 and 2021, executed an average of 75.3% over the same period. In 2020 and 2021, its execution was 75% and 35% respectively. Its execution is often driven down by a low execution of loan projects and furthermore, in 2021 due to number of scheduled projects being delayed due to the lockdown, resources from the IF were reallocated - additional funds were also released due to savings on maintenance costs. This amount also includes \$54.0 million being reallocated internally with the Infrastructure Fund from

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

other programmes to support the maintenance and rehabilitation of damaged infrastructure affected by calamity (Cyclone Seroja) programme.

HCDF received an average budget of \$21.6 million across the past 5 years (2017-2021). Its executions over that time was an average of 86.5%. In 2020 and 2021, the overall execution was 82.5% and 79% respectively. All of its budget is allocated to trainings, workshops and scholarships.

5.1.3 Expenditure by economic classification

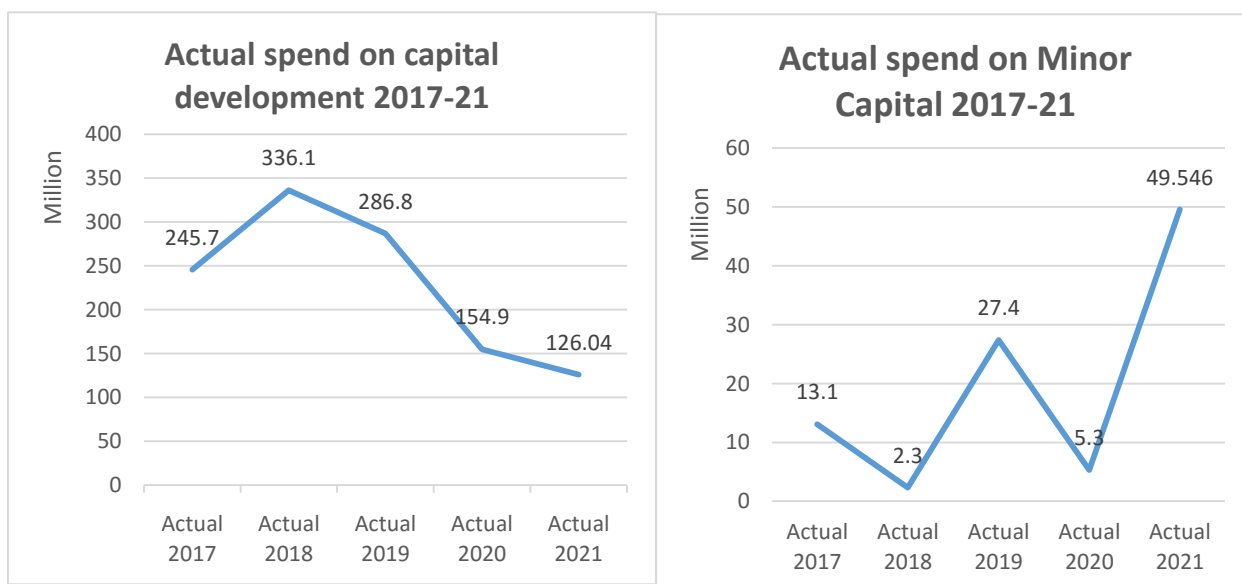
Capital

Capital development (CD) has been a stated policy objective of many consecutive governments in Timor-Leste. When looking at budget allocations between 2017 and 2021, CD has had the highest allocation out of the 5 years as well as the highest average amount with 29.1% of the total budget allocation of the government. In State Budget 2021, it received \$3.6 million in allocations. The total expenditure on CD usually follows the trend of IF which is the main implementer of all big infrastructure projects, with an average execution between 2017-2021 of 67%, correlating with an execution of 73.5% and 35% in 2020 and 2021 respectively.

Minor capital includes expenditure on capital equipment such as furniture, vehicles and other moveable assets. It has had the most fluctuating budget of all the appropriation categories, largely due to the limitations on its spending during times of duo-decimal budgets. In 2021, minor capital was allocated (pre-budget rectification \$61.1 million) \$ 57.4 million, reflecting a 5 fold increase from the previous year's budget which was very small owing to the duo-decimal budget of 2020.

Its average execution rate for the past 5 years is 65.7%, with range from a low of 42.7% in 2018 to a high of 84.1% in 2016. Execution in 2021 was 73%.

Figure 35: Capital expenditure, 2017-2021



Source: ProClarity, Ministry of Finance, July 2022

Recurrent

Recurrent budget (salary and wages, goods and services, and transfers) final allocation has remained between 68.7-85.3% from 2017-2021. In 2021, recurrent budget allocation prior to

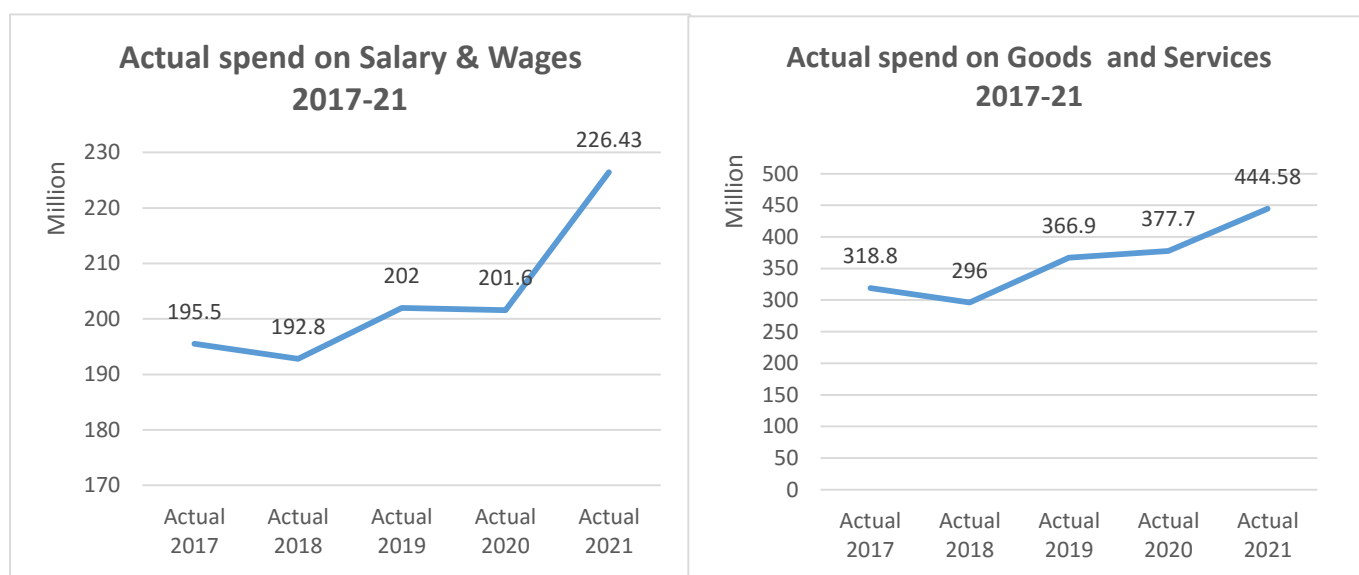
budget rectification was \$1359.8 million. Post budget rectification, the total budget allocation for this category was increased to \$1558.2 million and the final execution was 85.4%.

Salaries and wages have been given between 9.4-15.7% of the approved budget allocation between 2017 and 2021, averaged 13.8%. The 2021 state budget allocation for SW allocation was 16.5% higher than 2020's budget allocation. The increase has been budgeted to finance key measures that include RAEOA –ZEESM payment of civil servants, new recruitment for the Timor-Leste Defence Force and towards internal promotion of civil servants within government institutions.

There was an increase in the 2017 salaries and wages expenditure due to retroactive payments of teachers from 2011-2016 and recruitment of health professionals. The additional rise in 2019 was due to 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, consigned payments, budget transfers to RAEOA-ZEESM and some public enterprises. In general, transfers are driven by the contributory regime, prevention and mitigation package for COVID-19, veteran payments, the Bolsa da Mae scheme, disaster management and social investments. Transfers have composed 27.4% of the approved government budget for the past 5 years, with a high in 2021 of 34.7% and a low of 24.4% in 2016. Its decline in 2018 was driven by a reduced allocation for RAEOA-ZEESM, as they were able to finance infrastructure projects using unspent funds rather than requiring additional financing from the state budget. 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. Further in 2021, \$29.2 million made up for transfers to RAEOA-ZEESM for Capital Development.

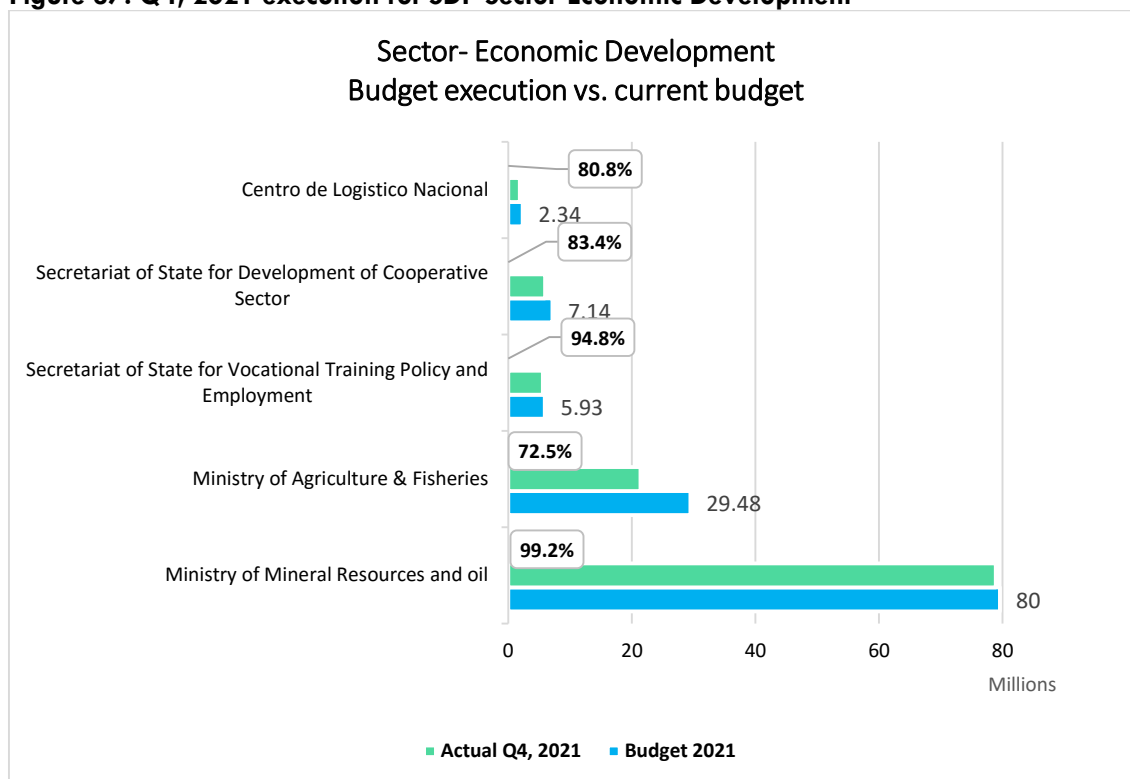
Figure 36: Recurrent expenditure, 2017-2021



Sources: ProClarity, Ministry of Finance, July 2022

5.1.4 Expenditure by functional classification in 2021

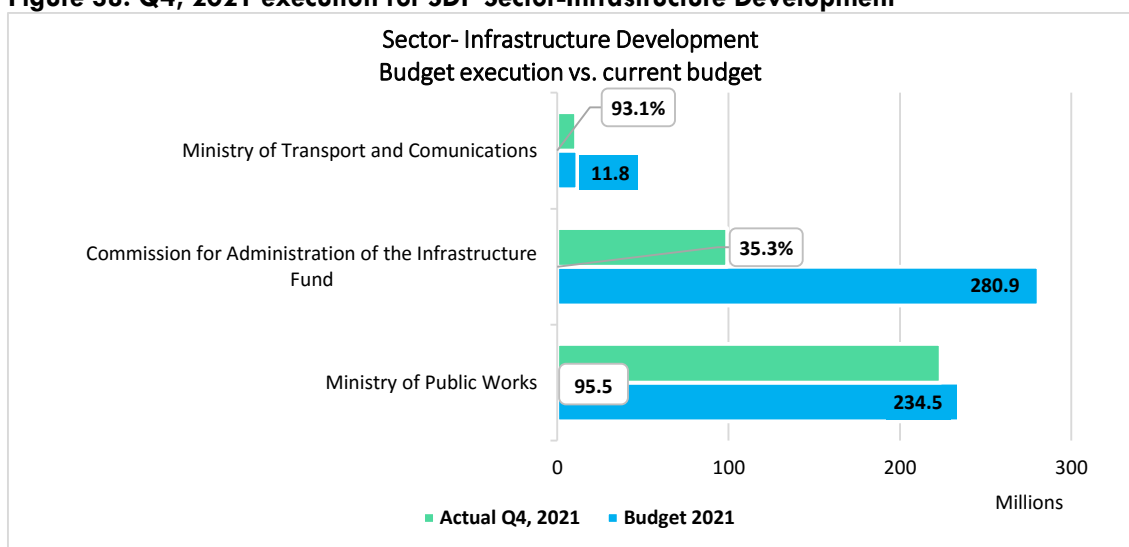
Figure 37: Q4, 2021 execution for SDP Sector-Economic Development



Sources: IFMISU, Ministry of Finance, July 2022

The Ministry of Mineral Resources and Oil had the highest budget in the Economic Development SDP sector in 2021 and has also the highest execution at 99.2%. This was followed by the Secretariat of State for Vocational Training Policy and Employment with the second highest execution rate of 94.8% which had the fourth highest budget allocation with an execution on good and services of 92.1%. The Ministry of Agriculture and Fisheries (MAP) had an overall execution of 72.5%, with an execution of just 31.3% on minor capital and 89% on capital development. Public transfer (88.9% - 100%) and salary and wages (60% - 93.1%) saw higher execution rates.

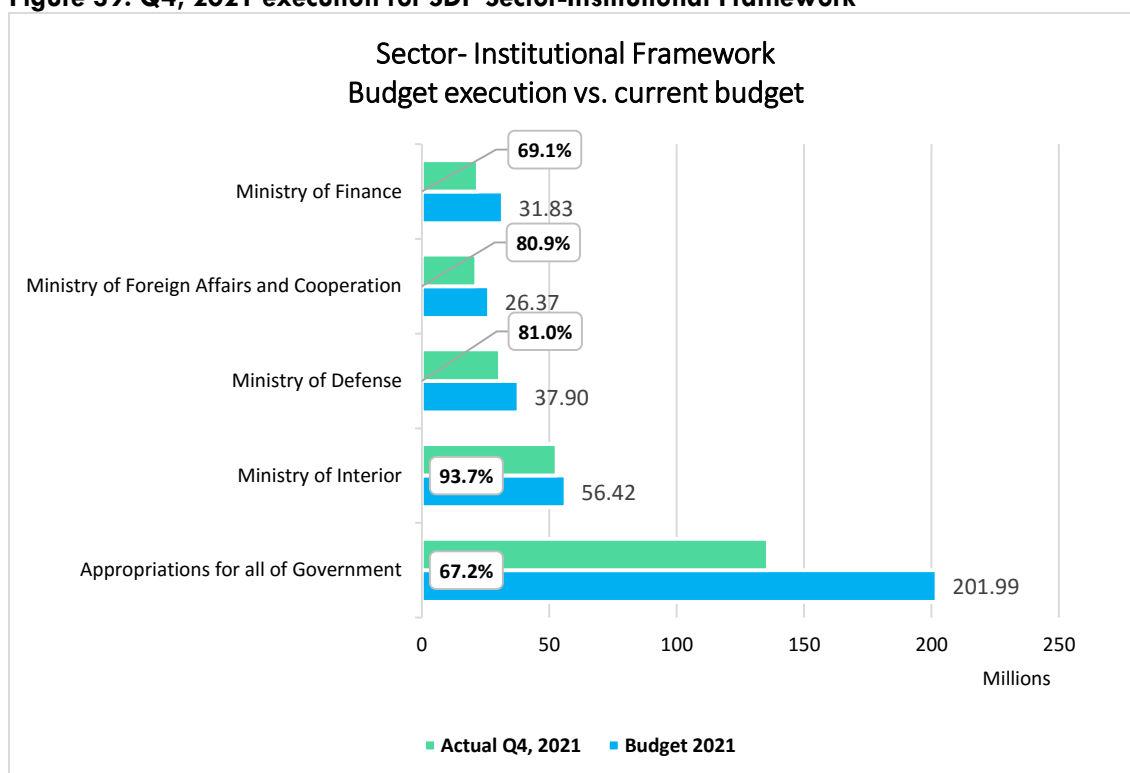
Figure 38: Q4, 2021 execution for SDP Sector-Infrastructure Development



Sources: ProClarity, Ministry of Finance, July 2022

Ministry of Public Works (MOP) had the highest execution rate and had the second highest budget allocation in the Infrastructure Development sector. It received a total budget allocation of \$234.5 million. Execution of goods and services was 76.1%, the execution of capital and development was 68.4% and execution progress of the categories on minor capital (75.2%) and salary and wages (97.1%), contributed to the average execution for the MOP in Q4 at 95.5%. The Infrastructure Fund received the highest budget allocation in 2021. However, \$116 million from the Infrastructure Fund was reallocated as a number of projects scheduled for 2021 were delayed due to the lockdown. Additional funds were also released due to savings on maintenance costs. The amount also includes \$54.0 million being reallocated internally with the Infrastructure Fund from other programmes to support the rehabilitation of damaged infrastructure affected by Cyclone Seroja. As for Ministry of Transport and Communication, cumulative execution was 93.1%, based on executions from salary and wages of 91.9%, goods and services of 96% and capital development of 75.5% and minor capital of 96.3%.

Figure 39: Q4, 2021 execution for SDP Sector-Institutional Framework



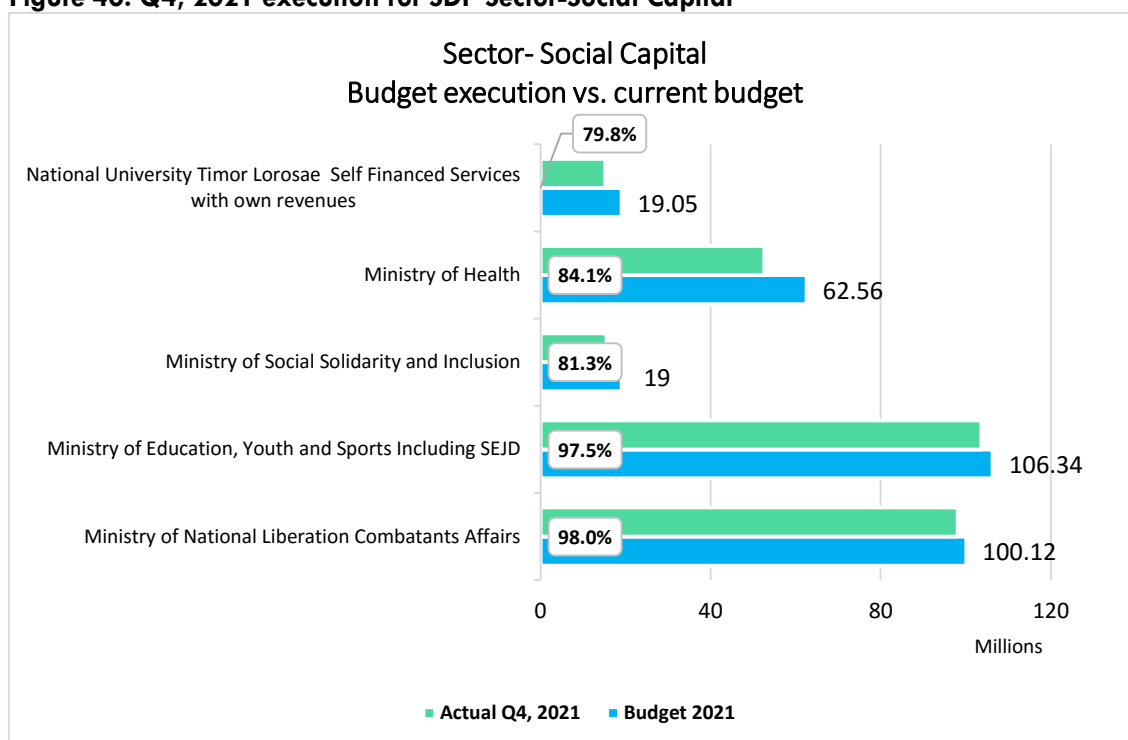
Sources: IFMISU, Ministry of Finance, July 2022

Institutional framework received a total of \$470 million in all appropriation categories in the 2021 budget, which was equivalent to a quarter of the budget. Appropriations for all of Government received the highest budget allocation in 2021 in the Institutional Framework but has one of the lowest execution rate of 67.2%: low execution for Goods and Services at just 24.1% and minor capital at 37.3% but public transfers were 93.8%

The Ministry of Interior has the second highest budget allocation but had the highest execution at 93.7%. There was an execution of just 26% for Capital Development, execution rates in the other categories were much higher with salary and wage at 93.8%, goods and services at 95.8%, minor capital at 98.9%, and contingency budget at 100%.

The Ministry of Foreign Affairs and Cooperation received the fourth highest budget allocation in this sector, however, had the third highest annual execution, and was preceded by Ministry of Defence at an execution of 81%. The execution in different appropriation category was; salary and wages at only 89%, good and service 70.1%), minor capital 94.4%, with a cumulative execution of 80.9%.

Figure 40: Q4, 2021 execution for SDP Sector-Social Capital



Sources: IFMISU, Ministry of Finance, July 2022

The Ministry of Education, Youth and Sports including SEJD received the highest budget allocation in 2021 (\$106.3m) within the social capital sector, with execution of 99.9% for salary and wages, 96.6% for goods and services, 86.6% for minor capital, 39% for capital development, 99.8% for public transfers, giving a cumulative execution of 97.5%.

The Ministry of National Liberation Combatant Affairs (MACLAN) received the second highest budget allocation in 2021, with final execution of 95.4% for salary and wages, 85.9% for goods and services, 96.9% for minor capital, 44.6% for capital development, 99.8% for public transfers, giving a cumulative execution of 98%.

The Ministry of Health had the third highest budget allocation with minor capital execution at 44.4% and good and services execution at 56.5% by end of 2021. However the other categories with much higher execution were, with salary and wages (93.5%), goods and services (80.5%), and public transfers (98.5%), giving a cumulative execution of 84.1%.

The National University Timor Lorosa'e execution was 79.8% due to the execution on category capital development of just 49.8% but other categories such as minor capital, goods and services and salary and wages executed in the range 84.9% - 94%. Other ministries executions were relatively near target as shown in the graphs.

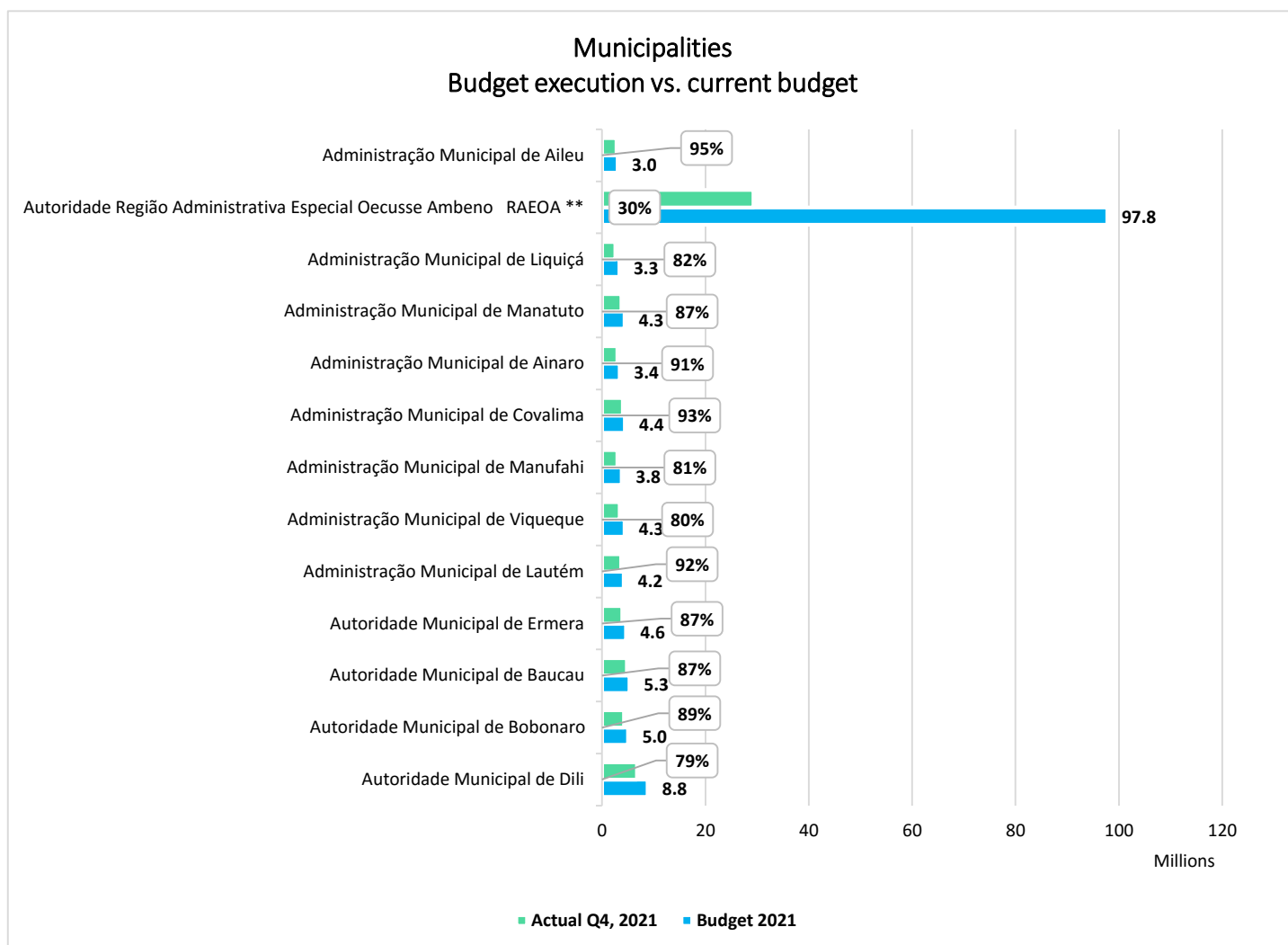
5.1.5 Municipalities in 2021

Municipality budget total execution ranged between 79% - 95%. Please note Atauro was not yet a separate municipality in 2021. Dili (including Atauro) had the highest budget allocation in 2021 (\$8.8m), with a cumulative execution of 79% which comes from salary and wages, good and service, and public transfer ranging from 33.4% - 99.6%. Municipality Aileu, received the lowest budget allocation in 2021 (\$3.0m) but had the highest in the budget execution as shown in the graph below (95%). This is due to execution from each appropriation category in the range of 96% - 100%.

** Autoridade Região Administrativa Especial Oecusse Ambeno RAEOA has been included in the expenditure analysis, although it is given a special status, to enable comparisons across the regions. It had the highest budget allocation in 2021, however, the lowest budget execution.

Figure 41: Q4, 2021 execution for Municipalities

Source: IFMISU, Ministry of Finance, July 2022



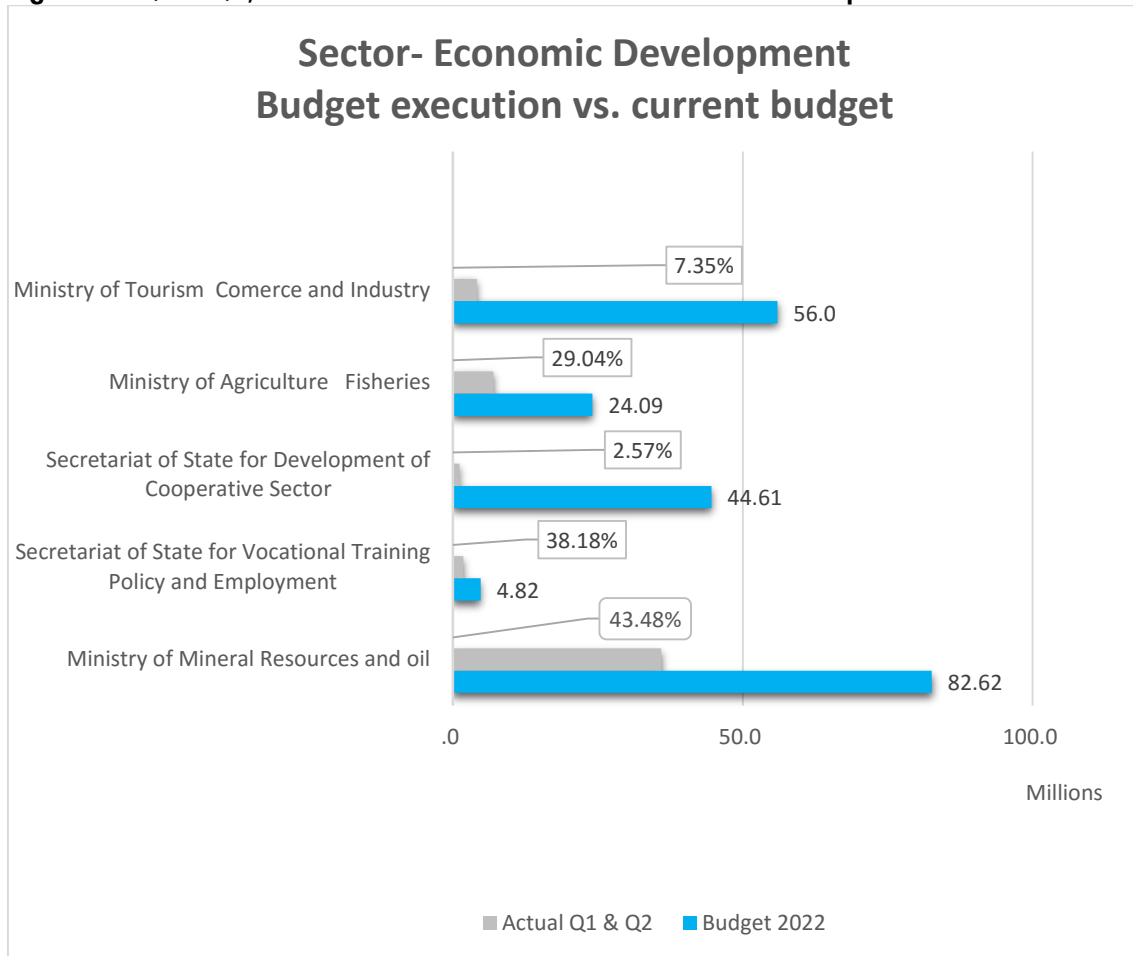
5.2 Mid-year analysis for 2022

This section describes budget execution until the end of June 2022 using Timor-Leste’s own Strategic Development Plan (SDP) classification. Five ministries for each sector, those with the highest budget allocation, are displayed in the following graphs.

Execution for 2022 is calculated on the basis of the rectified final budget that has been passed by parliament in May 2022 (\$3.2 billion excluding social security fund), making the 2022 state budget the largest in the history of the country. The rectified Budget included new measures such as subsidy for households at Christmas, Uma Kabit Lae Plus the newly established Veteran’s Fund. The Fund will mostly be spent on financial investment to generate revenue to pay for veterans’ expenses. Therefore, the money invested in financial instruments has to be reallocated every year, as happens with the Social Security Fund.

5.2.1 Line Ministry Execution by SDP Sector

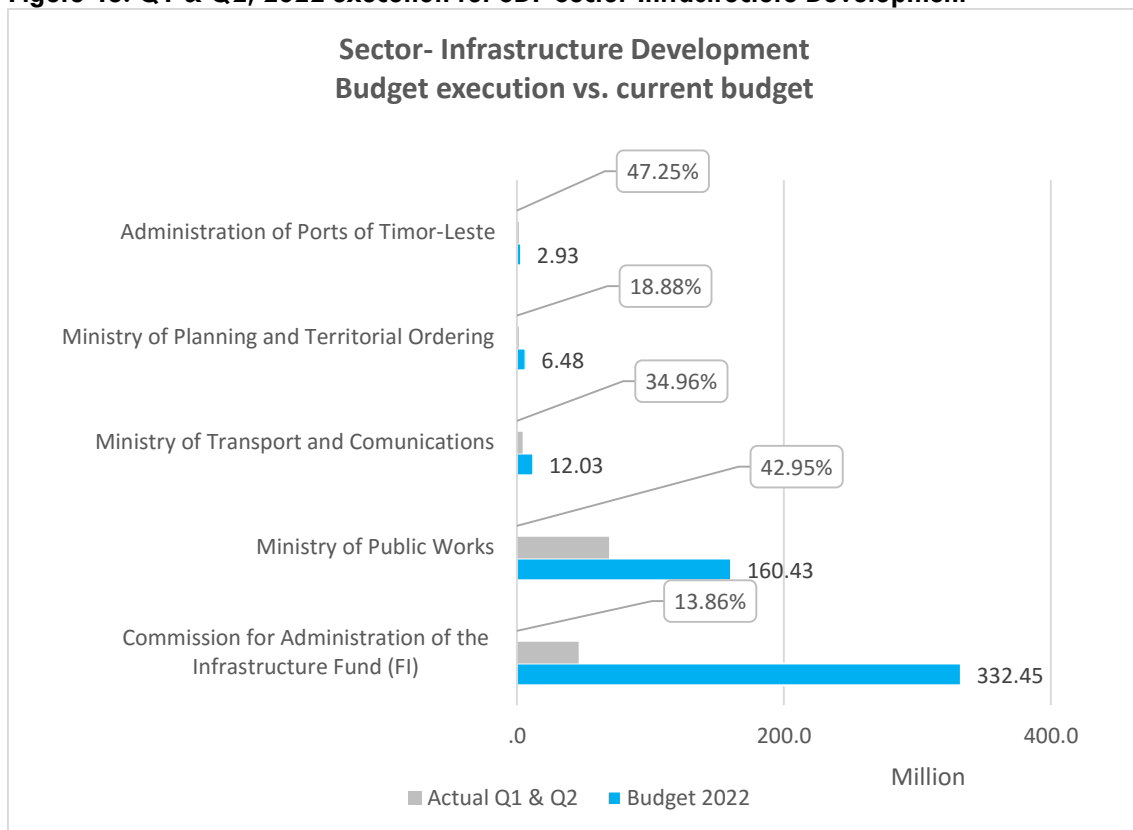
Figure 42: Q1 & Q2, 2022 execution for SDP Sector-Economic Development



Source: IFMISU, Ministry of Finance, July 2022

The Ministry of Mineral Resources and Oil has the highest budget allocation along with the highest budget execution in the mid-year analysis (43.48%). Ministry of Tourism and Commerce is the second institution with the highest budget followed by one of the lowest execution rate of 7.35% in the first half of the year. The Secretariat of State for Vocational Training Policy and Employment has the second highest budget execution rate reaching nearly 38.18% though its budget allocation is at 5th place.

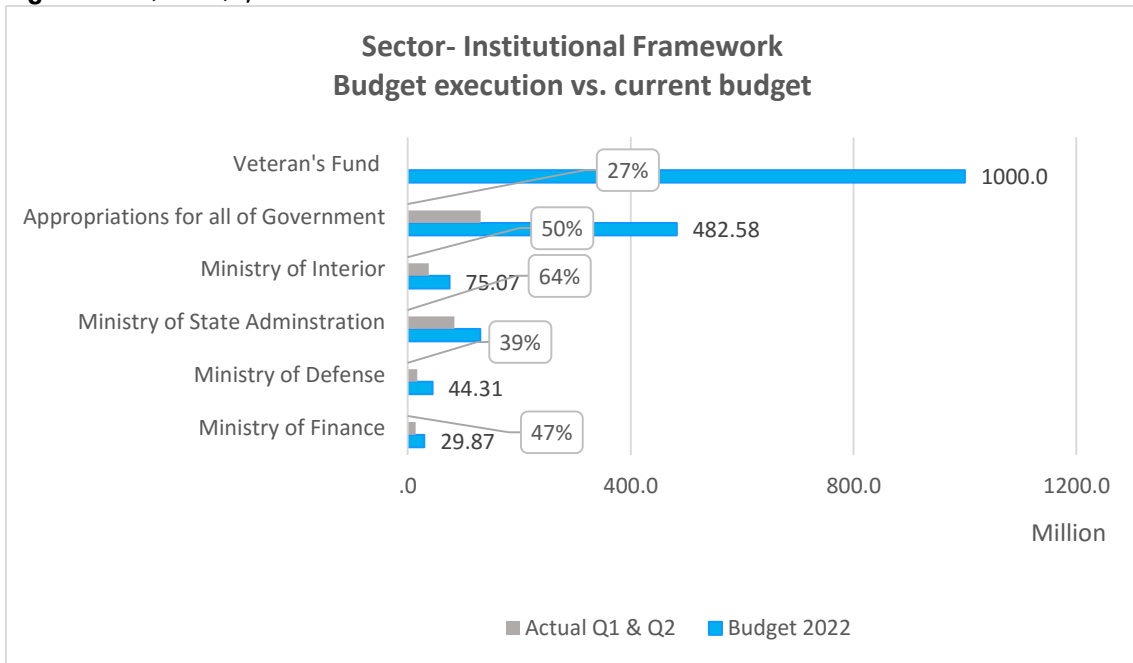
Figure 43: Q1 & Q2, 2022 execution for SDP Sector-Infrastructure Development



Source: IFMISU, Ministry of Finance, July 2022

This year the Commission for Administration of the Infrastructure Fund (FI) has the highest budget allocation in the infrastructure development category equivalent to \$332.45million. Nevertheless, it is the institution with the lowest execution rate at only 13.86% by the end of June. Following the FI, the Ministry of Public Works is the second institution with the second highest budget (\$160.43m) also displaying execution of 42.95% which is closer to 50%. The Ministry of Planning and Territorial Ordering achieved an execution of 18.88%. Administration of Ports of Timor-Leste has the highest execution rate but of a small budget of \$2.93m.

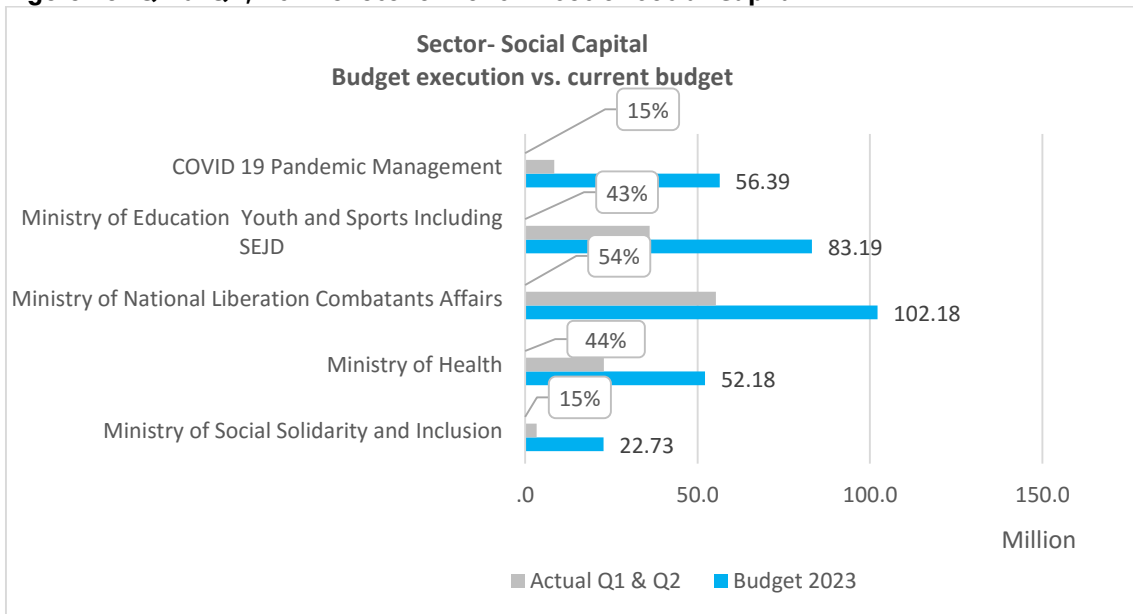
Figure 44: Q1 & Q2, 2022 execution for SDP Sector-Institutional Framework



Source: IFMISU, Ministry of Finance, July 2022

Excluding the Veteran’s Fund, which will be set up as an independent entity has a total allocation of \$1bn. There is currently no execution of this fund. The Fund will mostly be spent on financial investment to generate revenue to pay for veteran’s expenses. Therefore, the money invested in financial instruments has to be reallocated every year, as happens with the SS Fund. The Appropriations for all Government category still has the second highest allocation, with 27% execution. The Ministry of State Administration is the institution with the highest execution rate reaching 64% and with the second highest budget allocation (\$130m). The Ministry of Interior is the second institution with the highest execution rate of 50% halfway through the year.

Figure 45: Q1 & Q2, 2022 execution for SDP Sector-Social Capital



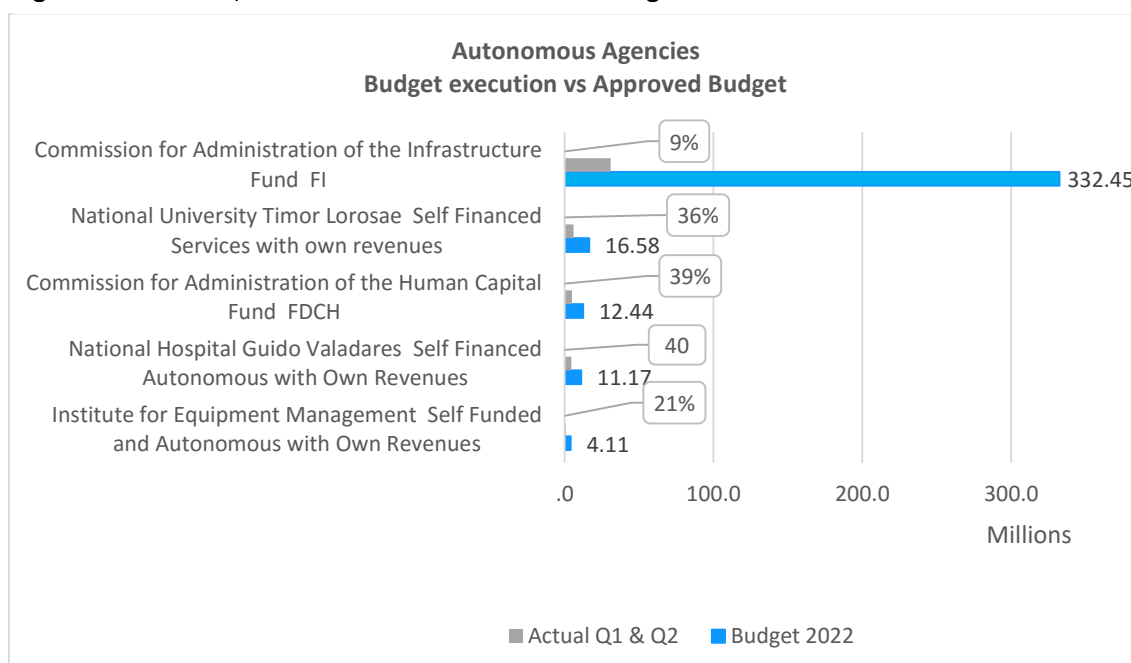
Sources: IFMISU, Ministry of Finance, July 2022

The COVID-19 Fund became a new category in the social capital sector since 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 together with the Ministry of Social Solidarity and Inclusion at the lowest 15%. The Ministry of National Liberation Combatants Affairs has the highest budget allocation with the highest execution rate of 54%.

5.2.2 Autonomous Agency Execution

For autonomous agencies, the Commission for Administration of the Infrastructure (FI) has the highest budget allocation reaching \$332.45 million, however the execution rate only reach 9% in semester 1. The agency with the highest execution rate is the National Hospital Guido Valadares with execution rate of 40%. Three other institution including the National University of Timor-Leste, FDCH and the Institute for equipment management have executed their budget over 20%.

Figure 46: Q1 & Q2, 2022 execution for Autonomous Agencies



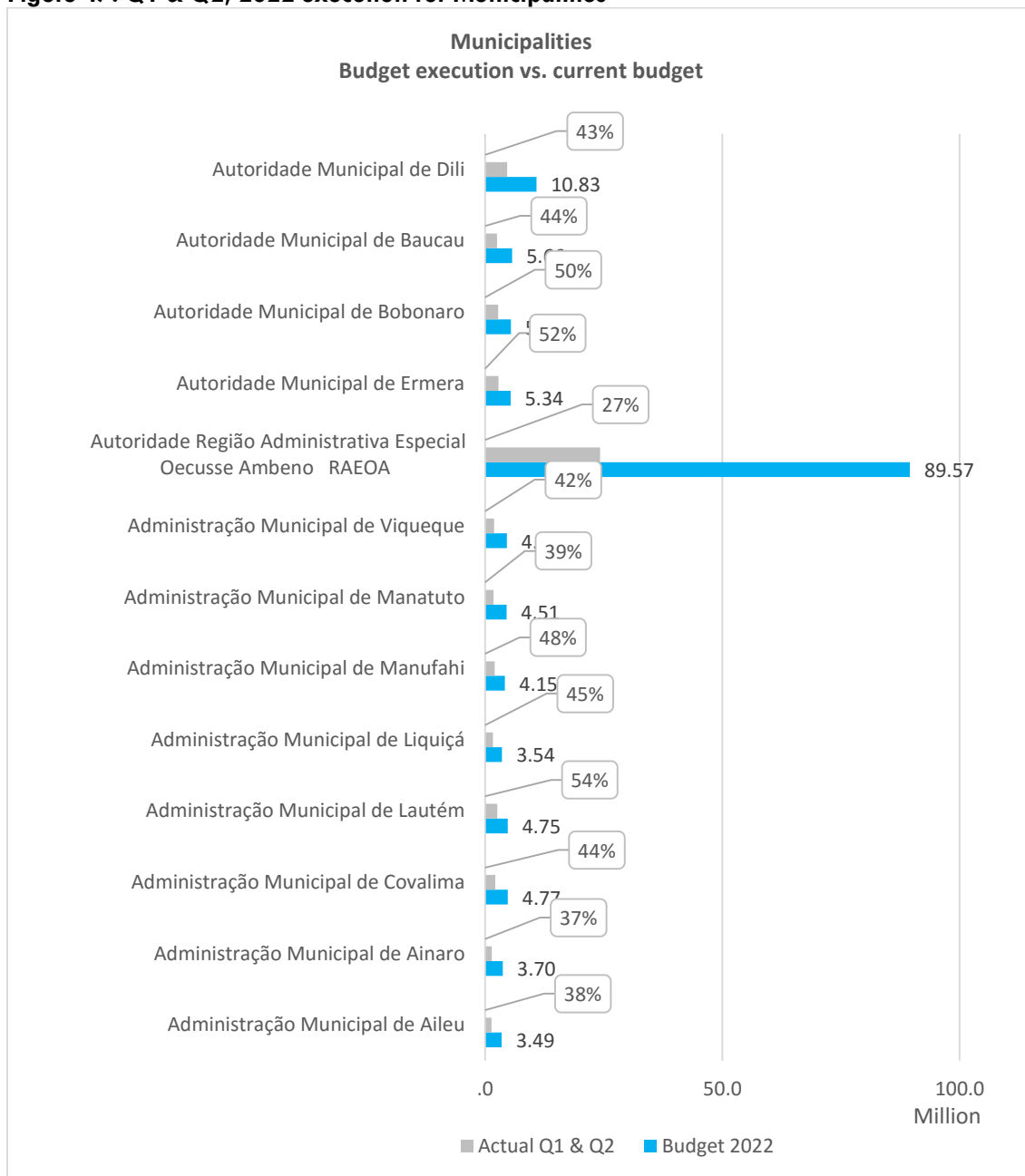
Sources: ProClarity, Ministry of Finance, July 2022

5.2.3 Municipalities Execution

RAEOA-ZEESM has the highest budget allocation (\$89.57m) with the lowest execution (27%). Dili is the municipality with the second highest budget allocation. This year's budget allocation to Dili is \$10.83 million with an execution rate of 43% at the end of June. Other municipalities' budget allocation are ranged from \$3 to 5.5 million where Baucau got allocated budget of \$5.66 million following Aileu with the lowest budget allocation among municipalities at U\$3.49 million. Lautem is the municipality with the highest execution rate reaching 54% followed by Ermera with 52%.

**Autoridade Região Administrativa Especial Oecusse Ambeno RAEOA has been included in the expenditure analysis, although it is given a special status, to enable comparisons across municipalities. Including RAEOA, this becomes the municipality with the highest budget allocation, equivalent to \$89.57 million but the one with the lowest execution rate of 27% amongst the others.

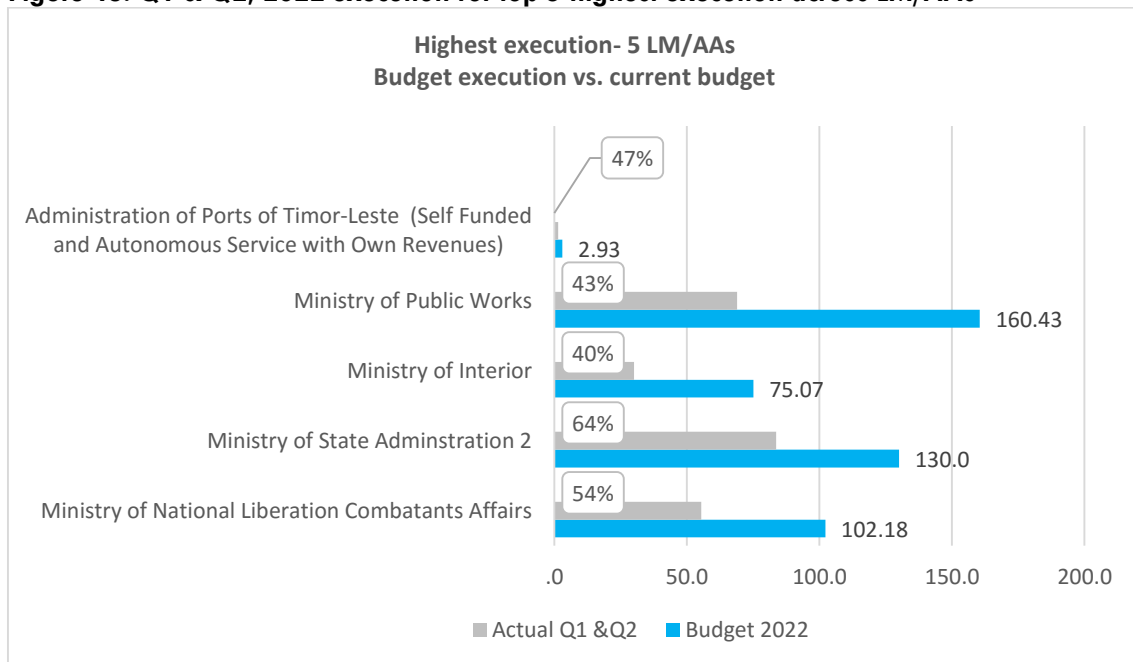
Figure 47: Q1 & Q2, 2022 execution for Municipalities



Sources: IFMISU, Ministry of Finance, July 2022

5.2.4 Top 5 highest execution across LM/AAs

Figure 48: Q1 & Q2, 2022 execution for top 5 highest execution across LM/AAs



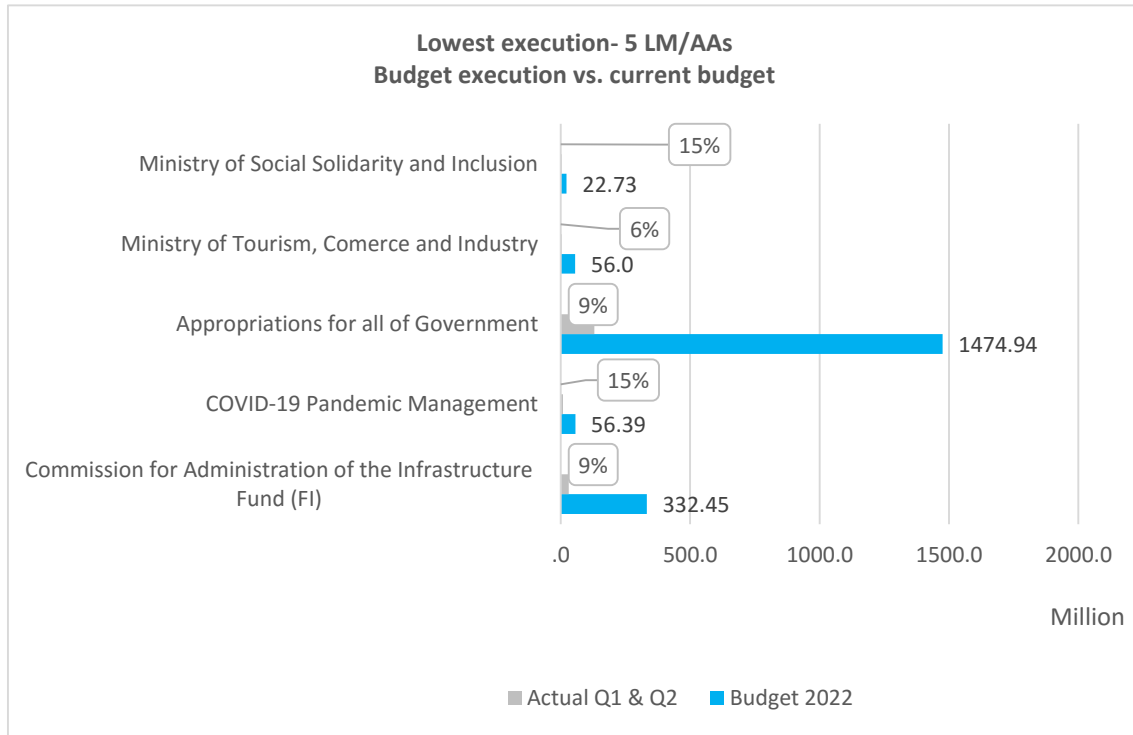
Sources: IFMISU, Ministry of Finance, July 2022

The top 5 institutions with the highest execution rate include the Ministry of National Liberation Combatants Affairs, the Ministry of State Administration, the Ministry of Interior, the Ministry of Public Works and Administration of Ports of Timor-Leste at 54%, 64%, 40%, 43% and 47% respectively. The Ministry of Public Works is the institution with the highest budget allocation in this category (\$160.43m).

5.2.5 Bottom 5 lowest execution across LM/AAs

Figure 49: Q1 & Q2, 2022 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 executions rates ranging from 6% to 15%. These institutions include: the Ministry of Social Solidarity and Inclusion, the Ministry of Tourism, Commerce and Industry, Appropriation for all Government, COVID-19 Pandemic Management and the Commission for Administration of the Infrastructure Fund at 15%, 6%, and 9%, 15% and 9% respectively.

6 Government Priorities and Budget Transparency Proposal

The Budget 2023 will continue to put people at the centre of all and prioritize citizen's well-being to ensure a fair and equitable distribution of the state budget to improve service delivery and economic recovery and resilience to promote sustainable and inclusive economic growth in the medium term and ascend to an upper-middle income country by 2030.

6.1 Government Priorities and Measures for 2023

The 2023 Budget proposal is formulated based on the following VIII Government three Strategic Objectives aimed at providing to all citizens as a whole:

4. Opportunity to have a healthy, secure, and long life
5. Access to knowledge, technology, and innovation
6. Access to sufficient resources to guarantee life with dignity.

With these three strategic objectives and goals in mind, the Government's agenda for inclusive development aspires to promote holistic well-being for the people and foster an environment for its people to live, contribute and participate in the economic development of the country. Such an ambition requires the development of liveable communities, which includes providing access to quality education, healthcare, water and sanitation, social protection, basic infrastructures, and major investments in the productive sector to recover and diversify the economy. Essentially, the 2023 Budget will continue to recover the economic growth and resilience to achieve sustainable and inclusive development.

In 2023, the health, education, and inclusion sector will receive the largest expenditure reflecting the importance given to universal access to quality education and healthcare and social protection, especially for vulnerable segments of society. A gender-responsive budgeting approach will also be undertaken when developing plans recognizing the differences in outcomes for all citizens, thus requiring potentially tailored approaches in key areas such as gender-based violence, social protection, health, and education programs.

Following the promulgation of the new Framework of the General State Budget and PFM (Law No. 2/2022), the budgetary processes now adopt a "two-step" process namely the Grand Options Plan Law & General State Budget proposal. The Grand Options Plan (GOP) is the document that bridges the gap between planning and budgeting which identified the planned measures (*obtained from the SDP, the medium-term plans, and the annual plans of the Public Administrative Sector services and entities, as well as any other political and strategic documents of the Government*) that will be carried out that year and will have budgetary implications. The GOP constitutes the justification for budgeting the activities that will be included in the General State Budget, presenting both concrete and abstract measures that contribute to achieving the objectives and targets set out in the Annual Plan.

Most of the priorities presented in the GOP constitute investment expenses and should only be presented in the GOP operating expenses for which there is a large difference from the previous year due to their importance, volume, etc. This means that the GOPs, in principle, will prioritize Ministries that have large investment expenses (MOP, MTC, MS, MEJD, etc.) and not those that focus on operating expenses, as they essentially provide services to other departments. Government (GPM, PCM, MF, MAPCOMS, etc.).

While the GOPs are not a Medium Term Plan, they do provide concrete key measures focusing on large multi-year investments in the productive sector to recover and diversify the economy, as well as key measures in key strategic areas such as education, health, protection social security, water,

and sanitation, etc., which will have budgetary implications. The GOP is reviewed and updated annually for each measure in the key strategic areas and submitted to the National Parliament on May 10th for discussion and approval. See Annex of Law No. 8/2022, of June 15, the Grand Options Plan for 2023, for a list of key measures for 2023.

The 2023 budget proposal will be organized into around sixteen (16) strategic areas with 275 key measures that will be implemented across the forty-five (45) national programs and contribute to the 28 national results as stated in the Grand Options Plan Law (Law No. 8/2022). The 16 Strategic areas are aligned with subsectors of the National Strategic Plan (SDP), and budget allocations for strategic areas will be calculated during the elaboration of the annual planning exercise and will inform the Government and public of the overall budget allocated to each area/subsector. The following highlights Government priorities in key strategic areas that will be implemented in the fiscal year 2023:

a) Agriculture, Livestock, Fisheries and Forestry

Agriculture, livestock, fishing, and forestry are strategic areas for the settlement of rural populations and the development country's economy. For the 2023 fiscal year, the Government intends to consolidate measures and increase budget allocation to reinforce investment in this sector. Key interventions area includes improving farming practices, and agricultural productivity and accelerating the transition from subsistence farming to a modern and market-oriented agricultural model that guarantees food security, diversification, and strengthening of domestic consumption. Furthermore, the Government is also investing in the animal husbandry sector due to its great potential to contribute to the improvement of the nutrition of the Timorese people, both through access to and consumption of fresh meat and dairy products. To improve this sector, thus, in 2023 the Government plans to invest in affordable and quality feed and ensure the vaccination and deworming of animals. Similarly, the Government anticipates improving investment in the fisheries sector and expanding the sector to combat food insecurity and malnutrition, and contribute to economic growth, improved livelihoods, and job creation. Lastly, for this sector, the Government continues to invest in the protection of the country's wildlife and biodiversity, promote investment in the forest sector, and carry out the demarcation and measurement of potential areas for the development of commercial sandalwood plantations and Encourage and develop community forest nurseries.

b) Economy and Employment

The creation of new businesses and industries and investment in the private sector is the engine of growth, innovation, and job creation for the Timorese people and will enable the transition to a non-oil economy. The Government is committed to diversifying the economy and creating the fiscal and bureaucratic conditions that allow a greater predisposition for national and international investors to invest in the country. In this regard, for the fiscal year 2023, the Government proposes interventions in five key areas, trade, industry, private sector, employment, and cooperatives, to improve the business and investment environment, create conditions for entrepreneurship, stimulate active participation in the national economic system and increase the export of goods, which ultimately contributes to increasing state revenue through tax collection.

c) Tourism

Tourism is an important driver for the development of the national economy due to its impact on job creation and income, also contributing to the safeguarding of Timor-Leste's natural and cultural heritage. With incomparable natural beauty, a rich history, and a unique cultural heritage, Timor-Leste has all the conditions to develop an original tourist sector, which mainly involves its people, religion, and culture. In this sense, for 2023, the Government has identified key measures including promoting ecotourism, combining accommodation with coffee or rice plantations and suco-level tourist sites and empowering communities to develop and manage the sites, and increasing the

number of tourists by increasing the number of cruise ships that dock at national ports as well as providing support to private companies that implement activities in the tourism sector.

d) Territorial Development and Housing

The Government aims to promote the quality of life of all Timorese, especially those who live in remote and difficult-to-reach areas, through various incentives ranging from the municipal level to the village level, to create local jobs and raise the standard of living and well-being of the population. In this sense, for 2023, some of the major priorities include continuing the implementation of the Integrated Municipal Development Planning (PDIM) program for new projects, PNDS and R4D program, as well as promoting and developing community economic activities through the Post-Administrative Manpower - *Mão-de-Obra* Posto Administrativo Program (PMOPA) and community economic activities through the *Movimento Hafoun Aldeia* Program (PMOHA).

e) Environment

Air pollution has grown substantially, especially in Dili, as a result of emissions from cars and motorbikes, in addition to smoke released by homes and forest fires. The VIII Constitutional Government's Program places special emphasis on the need to promote and implement an environmental policy, ensure the protection and conservation of nature and biodiversity, control pollution, combat climate change, and strengthen licensing services and environmental education, as well as inspecting potentially harmful activities to flora and fauna and guaranteeing national development in an environmentally sustainable manner. In this context, some of the key measures foreseen to be implemented in 2023 include improving the system of environmental licensing services, including the collection of environmental fees, preparing and passing the environmental tax law to increase revenue collection, and promoting the identification of plants to be included in the carbon market as well as promote resilience to climate change through adaptation, mitigation, and substance control actions chemicals that damage the ozone layer.

f) Petroleum and Minerals

The oil sector has been the main source of revenue from the General State Budget to provide public services to the population and to build and maintain our Nation's infrastructure. The Government remains committed to boosting oil and mineral revenues and achieving the balance of the Petroleum Fund, to ensure its sustainability for future generations. The Government has identified key interventions that will be taken in 2023 to maximize investment in the oil and mining sectors including increasing study and research activities through the continuous promotion of onshore and offshore blocks to exploration to maximize investment in the oil and mining sectors and developing feasibility and sustainability studies on the use of natural gas for the production of electricity, making efforts to use energy that is less expensive and takes into account environmental issues.

g) Electricity and Renewable Energies

Access to regular and reliable electricity supply is a fundamental right and the basis of Timor-Leste's economic growth. For the 2023 budget proposal, the Government, therefore, intends to continue investing in updating and improving the transmission and distribution of electricity and rural electrification programs, while investing in the expansion of renewable energies. Investing in renewable energy sources can contribute to a less polluted environment and mitigate the impacts of climate change in accordance with the commitments assumed in international conventions.

h) National Connectivity

The Government is committed to improving national connectivity through the construction, rehabilitation, and maintenance of central and productive infrastructure that are resilient to climate

and weather conditions to connect and create conditions for the movement of people and goods, for economic growth, the creation of jobs and the development of the private sector. For the fiscal year 2023, the Government remains committed to investing in three priority areas in this sector namely a) infrastructure (ports, airports, roads, and bridges); b) logistics (the system of land, sea, and air transport); and c) telecommunications (sea and terrestrial fibre optics).

i) Water and Sanitation

Access to clean, potable water and modern sanitation services is critical to protecting the health of all

Timorese. Improving the quality of water, sanitation and drainage in Timor-Leste will help build the resilience needed for the country to face future health challenges and grow the economy. For 2023, some of the key interventions include initiating the project to modernize the water treatment, sanitation and drainage system in Dili in collaboration with the Millennium Challenge Corporation (MCC), increasing the coverage area of the drinking water supply service, and completing the emergency rehabilitation of damaged clean and potable water facilities.

j) Education and Training

The provision of quality education and training are essential to shape the personality, create conditions for employability and competitiveness of people of working age and ensure the economic development of the country, being a fundamental instrument for the exit from poverty. To ensure that all children and young people have access to learning and essential qualifications for success in society, the Government remains committed to investing significantly in the rehabilitation of basic educational infrastructures, strengthening the quality of the national curriculum of formal education, and improving the opportunities for continuous training and professional development of current teachers and school leaders. For 2023, some of the new initiatives in this sector include introducing reform in the school feeding program, ensuring access to the internet in all schools and universities, awarding a merit scholarship to the best students at the elementary and secondary education levels, continuing with the implementation of the home-schooling program, implementing a recruitment program aimed at the best students from national universities, and initiating the feasibility study for the establishment of the *Escola de raiz*. The Government also plans to initiate a pilot project for the establishment of day care centres (*crèches*) in the municipality of Dili, to support children aged 0-3 years, whose parents work and need this support. Additionally, the Government also plans to conduct a design study to improve education by developing a centre of excellence that will provide pre-service training for future secondary school teachers and school leaders, and provide continuous and professional training for current teachers and school leaders, in collaboration with Millennium Challenge Corporation.

k) Health

Equitable access to essential and quality health services that are well equipped and staffed with competent health professionals is a fundamental objective. Thus, for 2023, the Government's intervention is oriented toward rehabilitating basic health infrastructures at both national and municipal levels, expanding the healthcare services, introducing public-private partnerships in Health Diagnostic Services, and improving the quality of health service provision through innovation of the primary health care system, promoting constant improvement in the development and deployment of human resources, strengthening efforts to combat malnutrition and improving the national response to outbreaks and emergencies of dengue, cholera and other diseases.

l) Social Inclusion and Protection

The Government is continually committed to assisting the poorest and most vulnerable citizens of Timorese society. The 2023 budget proposal will provide a specific focus on consolidating a policy of social cohesion and guarantee of dignity and human rights to all Timorese, either through the improvement of the sustainability of the Social Security System or through the strengthening of

social assistance to the most disadvantaged. In this context, the Government has identified key interventions to ensure that women and children, young people, as well as the elderly and other vulnerable citizens, have access to the satisfaction of their needs fundamentals and well-being, as well as access to opportunities to break out of their fragile state. Some of the key Interventions include a set of reforms of the *Bolsa da Mãe-Nova Geração* program, and the creation of protection in case of illness (temporary incapacity), family protection (family allowance), work accidents and occupational diseases, and unemployment within the scope of the contributory social security system.

m) Culture and Heritage

The Government is committed to the conservation, protection, and preservation of the historical-cultural heritage and the development of arts and culture, as well as the protection of rights relating to artistic and literary creation. Major interventions that will be carried out in 2023 include proceeding with the initial steps towards the implementation of the National Library and the identification of artefacts to constitute the National Museum in the future and the construction of the “Jardim da Chama Eterna”, a memorial of high symbology, which is intended to concentrate the recognition of all those who perished in the struggle for National Liberation. The Government also continues to invest in the development and promotion of cultural activities, actions, and practices, in particular the establishment of creative industries that generate income and employment, and at the same time defend and enhance cultural heritage, which has unique characteristics of great interest.

n) Reform of the State

The State Reform is divided into four major institutional reforms in progress – the Public Administrative Reform, Fiscal, and Public Finance Management Reform, Judicial Reform, and the Administrative Decentralization Process. These four reforms are interconnected and have the common objective of improving the management and functioning of the public sector, as well as ensuring that the State operates within a framework of legality and legal certainty more efficiently and effectively. For 2023, the Government remains committed to ensuring the implementation of initiatives stated in the policy documents of the four institutional reforms.

o) Defence and National Security

The development of transparent, efficient, competent, and professional defence and security institutions is fundamental to the maintenance of democracy and the consolidation of stability and peace at the national and international levels. For the 2023 fiscal year, the Government remains committed to strengthening coordination and close cooperation between the defence forces (F-FDTL) and security forces (PNTL) and ensuring clarity and commitment in accordance with their respective responsibilities and missions, as well as guaranteeing the territorial integrity, the normal functioning of democratic institutions, freedom and the protection of the State's and citizens' patrimony.

p) International Relations and Foreign Policy

Foreign policy actions are crucial to support national development and improve Timor-Leste's participation on the international stage and its insertion in regional and international economies. The Government continues to conduct a foreign policy that promotes bilateral and multilateral cooperation, promoting cultural, economic, and commercial partnerships with other countries, essential for attracting investment. For the fiscal year 2023, the Government will continue to promote efforts for Timor-Leste to become a full member of ASEAN and the World Trade Organization and promote the definitive delimitation of land and sea borders.

6.2 Gender and Social Inclusion (GESI) Responsive Budgeting

Advancing gender equality and social inclusion continues to remain at the heart of the VIII Constitutional Government. Since 2017, the Government has reinforced Gender-Responsive Budgeting (GRB) to be adopted as a strategy when developing programs and subprograms to achieve a positive impact on the promotion of gender equality, empowerment of women and girls, and social inclusion.

The Government continues to institutionalize and mainstream the gender equality and social inclusion agenda in the overall planning and budgeting process. The 2023 budget call circular underlines the importance to look more closely at the impact of budgetary measures and policies on gender equality and inclusion and ensure that the needs and interests, priorities, and challenges of women, girls, boys, and men in different age-conditioned social situations, class, location, etc. are adequately addressed in the annual plan.

For the fiscal year of 2023, the Government continues to invest in social protection to improve the socio-economic status and economically empower vulnerable groups, namely girls, women, youth, elderly, disabled, and marginalized groups. In this context, the Government has earmarked US\$25m to introduce the Bolsa da Mãe-Nova Geração measure (DL. No. 22 /2021) which aims to provide support and improve health and maternal and child nutrition during the first childhood years. Special support is also given to children with chronic illness or disability, by increasing the value of the respective subsidy. The new mother's allowance sets up a subsidy of US\$15 per month for pregnant women, US\$20 per month for each child up to age 6, and a \$10 surcharge for children with disabilities. The Government has also assigned US\$36m for the elderly and disabled as part of the non-contributory scheme.

Furthermore, the Government continues to invest in measures to combat poverty, reduce inequalities and improve well-being by improving budget allocation for nutrition support. For the fiscal year 2023, the Government has improved the quality of meals for the *Merenda Scholar* program to meet the nutritional needs of children by increasing the expenditure per child and per meal from US\$0.25 to US\$0.42. A total of US\$18.6m has been allocated to execute this measure covering 13 municipalities and RAEOA. To complement this, the Government has also set aside US\$10m annually for the next five years to implement the National Health Sector Nutrition Strategic Plan. This hopefully addresses micronutrient deficiency related to poor nutrition in children and has a positive impact on children's lives.

Moreover, the Government continues to invest in facilitating universal access to education through social protection measures by providing scholarships for the children of the National Liberation Combatants and merit scholarships awarded to the best students at the elementary and secondary education levels. In this context, for the 2023 fiscal year, the Government has distributed US\$1.1m to the Scholarships program for the children of the National Liberation Combatants and US\$7.5m to the best students in the elementary (top 3 best students) and secondary education (top 5 best students) levels. The Government also intends to continue the Home Schooling program by allocating US\$2.1m to provide support to students at their respective place of residence in the teaching process and learning, particularly for children of the ages of preschool education and the First Year of Basic Education, in all sucos and villages in Dili, as well as the availability of Mobile Libraries to the entire student community. Through the financing of the aforementioned activities by the State, which is understood to be complementary to each other, it is hoped to achieve an increase in the rate of student participation in the school process, at all levels and modalities of education and teaching, and an increase in the percentage of school success.

6.3 Budget Transparency and Accountability

The 2023 budget proposal must include the following markers to hold the Government to account on various crosscutting issues such as gender equality and social inclusion, nutrition, climate, and supply chain.

a) *Gender Marker*

To monitor the proportion of the State Budget allocated to the promotion of gender equality and the commitments made to eliminate existing inequalities, the Government established a Gender Marker in the budget and planning system.

During the preparation phase of the General State Budget, all government entities are required to conduct gender analysis as part of Gender Responsive Budgeting when developing their programs, subprograms, and activities. To classify a subprogram by Gender Marker, government entities should consider the extent to which the gender aspect is integrated by analysing the context of the subprograms with its activities, the expected results (outputs), and the budget allocation. The gender marker is a mandatory tool that must be used by all LMs/AAs in their Annual Action Plan and applied at the subprogram level. Subprograms cannot be left without a gender marker. The aforementioned Gender Marker contains three (3) markers, namely:

1. **Principal (P):** The principal expected result of the subprogram is to reduce gender inequalities. The subprogram would not have been undertaken without this gender equality and social inclusion objective.
2. **Significant (S):** Gender equality and social inclusion aspect is an important and deliberate expected result, but not the principal reason for undertaking the subprogram. The subprogram, in addition to other expected results, is designed to have a positive impact on inclusivity and advancing gender equality and/or the empowerment of women and girls (gender mainstreaming). For a subprogram to be considered "Significant" by the Gender Marker, there must be at least one of the criteria below:
 - There is at least one activity focused on gender issues in the subprogram;
 - At least one of the outputs is indicated the expected result to achieve equality between men and women;
 - Objectives, baselines, targets, and performance indicators are clearly defined to address gender inequalities, and data are disaggregated by sex.
3. **Not-Targeted (NT):** The subprogram does not intend to reduce gender inequalities nor address the needs and concerns of vulnerable and marginalized groups.

b) *Child Marker*

To effectively identify and monitor activities with budget allocations that support the realization of children's rights, the Democratic Republic of Timor-Leste (RDTL) adopted a Child Marker for planning and budgeting on 27 October 2021. The Child Marker applies to all government entities that receive funds from the General State Budget, showing which activities, and how much budget, are specifically designed to address children's rights (ages 0 to 17), and thus reinforces transparency and accountability.

The Child Marker was integrated into the Government's planning, monitoring, and evaluation system, *Dalan Ba Futuru Timor-Leste (DBFT)*, as an integral part of public financial management. The Child Marker includes three (3) categories that assess the focus on realizing children's rights and apply at the activity level, namely:

1. **Specific (E).** This category applies to activities that specifically aim to address children's rights (survival, development, protection, and participation).

2. **Extended (A).** The 'Extended (A)' category applies to activities that provide goods and services that directly benefit people, including children.
3. **Indirect (I).** This category refers to activities that only have an indirect contribution to children's development and well-being.

c) Nutritional Budget Tagging

The VIII Government is committed to institutionalizing nutritional budget tagging (NBT) through the Government's planning and budgeting system. The NBT aims to identify, classify and mark nutrition-related expenditures in the public finance management system, allowing for the estimation, monitoring, and tracking of critical nutritional expenditures of different government entities, and analysing the extent to which the composition of state budget allocations for interventions aimed at eliminating all forms of malnutrition among the population.

There are two (2) nutritional budget tagging that will be included in the Government's fiscal year 2023 planning and budgeting system and will be applied at the activity level, namely:

1. **Nutrition-Specific interventions (NE).** This category applies to activities that address the immediate causes of malnutrition and deficiencies in the physiological development of the population, such as those that provide for the provision of vitamin A supplements, deworming, or dietary diversification among pregnant mothers.
2. **Nutrition-sensitive interventions (NS).** This category refers to activities that address the underlying causes of malnutrition such as improving agriculture and food security, social protection, early childhood development and education, sanitation and water hygiene, etc.

In 2023, in a pilot phase, the nutritional budget marker will be applied to the budgets of seven (7) Government entities namely: Ministry of Health (MS), Ministry of Education, Youth and Sport (MEJD), Ministry of Social Solidarity and Inclusion (MSSI), Ministry of Agriculture and Fisheries (MAP), Ministry of Tourism, Commerce and Industry (MTCI), Ministry of Public Works (MOP) and Secretary of State for Equality and Inclusion (SEII). For the elaboration of the Annual Action Plan 2023, these entities are required to analyse, plan, and budget for nutrition-related interventions and to identify each activity as nutrition-specific (NE) or nutrition-sensitive (NS).

d) Climate Budget Tagging

The VIII Constitutional Government has decided to introduce Climate Budget Tagging (CBT) in the public finance management system to ensure that Timor-Leste is adequately prepared to adapt and mitigate the impacts of climate change. The CBT is a tool for identifying, classifying, weighing and marking relevant expenditures for combating climate change and nature conservation in a government's budget system, allowing the estimation, monitoring, and tracking of these expenditures. There are two (2) Climate Budget Markers that will be included in the Government's planning and budgeting system for the year 2023 and will be applied at the level of activities, namely:

1. **Highly Relevant (H).** This category applies to activities with a clear primary objective of producing specific results that improve climate resilience or contribute to climate change mitigation and the sustainable use of natural resources. Examples are expenditures aimed at reducing the risk of natural disasters, supporting the energy transition, preventing the over-exploitation of fisheries resources, etc.
2. **Relevant Medium (M).** This category applies to activities with secondary objectives related to building climate resilience or contributing to climate change mitigation and sustainable use of natural resources. An example is the irrigation extension activities that, despite being implemented to improve livelihoods, also result in greater protection against droughts.

In 2023, on a pilot basis, climate budget markers will be applied to the budgets of three (3) Government entities, namely: the Ministry of Public Works (MOP), Secretary of State for the Environment (SEA), and Ministry of Agriculture and Fisheries (MAP). For the elaboration of the Annual Action Plan 2023, the MOP, SEA, and MAP are required to analyse their activities to identify whether they are climate resistant, which means that they correspond or not to the impacts of climate change.

Starting in the fiscal year 2024, the climate budget tagging will cover all Ministries. This phased implementation will provide the opportunity to fine-tune the system, and will also provide the space for focused capacity development at the line ministry level.

e) Value chain Marker

The Ministry of Finance plans to introduce a Value Chain Marker in the Public Finance Management System to ensure the implementation of the "Timoriza Value Chain" policy. GPM and MCAE are responsible for coordinating with relevant entities to identify key measures concerning building value chains and reporting to the Ministry of Finance. To this end, they will use the following five (5) activity-level markers:

1. **Production (P).** The Production category (P) applies to activities that directly or indirectly aim to increase national production, either through increasing the productivity of the national economy and/or substituting imports, such as labour training activities, support for the internationalization of Timorese companies, or the modernization of the fishing fleet.
2. **Industry/Processing (I/P).** The Industry/Processing (I/P) category applies to activities that aim directly or indirectly to favour the development of industry and/or local processing of raw materials and intermediate goods, such as activities to support the development of agro-industry.
3. **Distribution (D).** The Distribution and Marketing (DM) category applies to activities that directly or indirectly aim to improve the circulation of raw materials, intermediate products, and final products inside and outside the national territory, such as the construction or improvement of basic infrastructure for commerce such as airports and ports.
4. **Wholesale/Retail Trade (CGR).** The Wholesale/Retail (CGR) category applies to activities that directly or indirectly aim to boost trade in national production or partially processed products within the national territory, especially through exports, such as programs to support business competitiveness; activities related to the organization of fairs for traditional products, or the integration of Timor-Leste in international trade circuits.
5. **Consumption (C).** This category refers to activities that contribute to increasing consumption inside and outside the national territory of national production or partially processed products within the national territory, such as public purchase programs for locally produced food products, subsidy programs for national exports, or conditional transfer programs for families to purchase local products.

f) Subprogram for the social inclusion of people with disabilities

The VIII Constitutional Government is committed to defending the rights of persons with disabilities to have equal access and opportunities to be active citizens in all spheres of public life and to be involved in decision-making processes in all areas of the country's development to contribute to sustainable development. For the elaboration of the Annual Action Plan for 2023, there will be a new sub-program created under Program 980: Gender Equality and Social Inclusion to reinforce the Government's commitment to the implementation of the National Action Plan for the People with Disabilities (2021-2030) as well as to monitor and track disabilities-related expenditures.

There are eleven (11) Government entities namely the Ministry of Justice (MJ), Ministry of Health (MS), Ministry of Education, Youth and Sports (MEJD), Secretary of State Youth and Sports (SEJD), Ministry of Higher Education, Science and Culture (MESCC), Ministry of Social Solidarity and Inclusion (MSSI), Ministry of Public Works (MOP), Ministry of Transport and Communications (MTC), Secretariat of State for Equality and Inclusion (SEII), State Secretariat for Vocational Training and Employment (SEFOPE) and State Secretariat for Social Communication (SECOMS) that are required to plan and allocate budget for the activities listed in the policy and map it to the new subprogram called: **Implementation of the National Action Plan for the Rights of Persons with Disabilities.**

7 Budget Proposal 2023

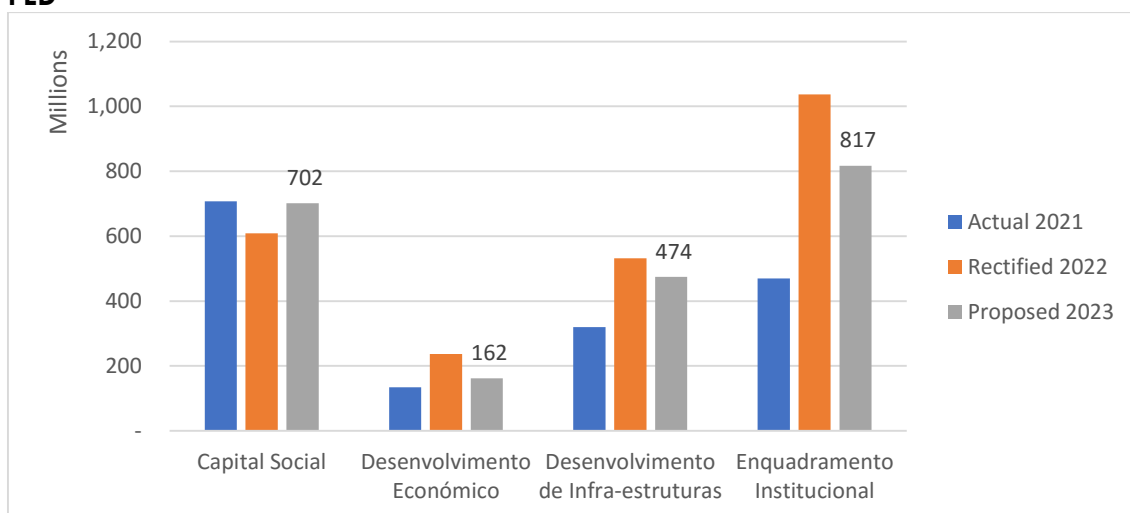
7.1 Analysis of the 2023 Proposed General State Budget

Analysis of the 2023 Proposed General State Budget by Sector

The 2023 GSB proposal included the Social Security sector in the disaggregation of the budget ceiling to increase the transparency of the budget cycle. Therefore, to allow for consistency and comparability with previous year’s expenditure and allocations the analysis that follows in section 2.3 and 2.4, as opposed to the historical analysis and the mid-term review, does include the Social Security sector⁴. Timor-Leste’s 2011-2030 Strategic Development Plan (PED) is organized around four pillars: Institutional Frameworks, 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 2023 Budget allocates the largest share of the budget to the Institutional Framework pillar, followed by Social Capital, Infrastructure Development, and Economic Development. The figures include loan disbursements and transfers to ZEESM-RAEOA.

Figure 50: Comparison of 2021 Expenditure, rectified 2022 GSB and proposed 2023 GSB by PED

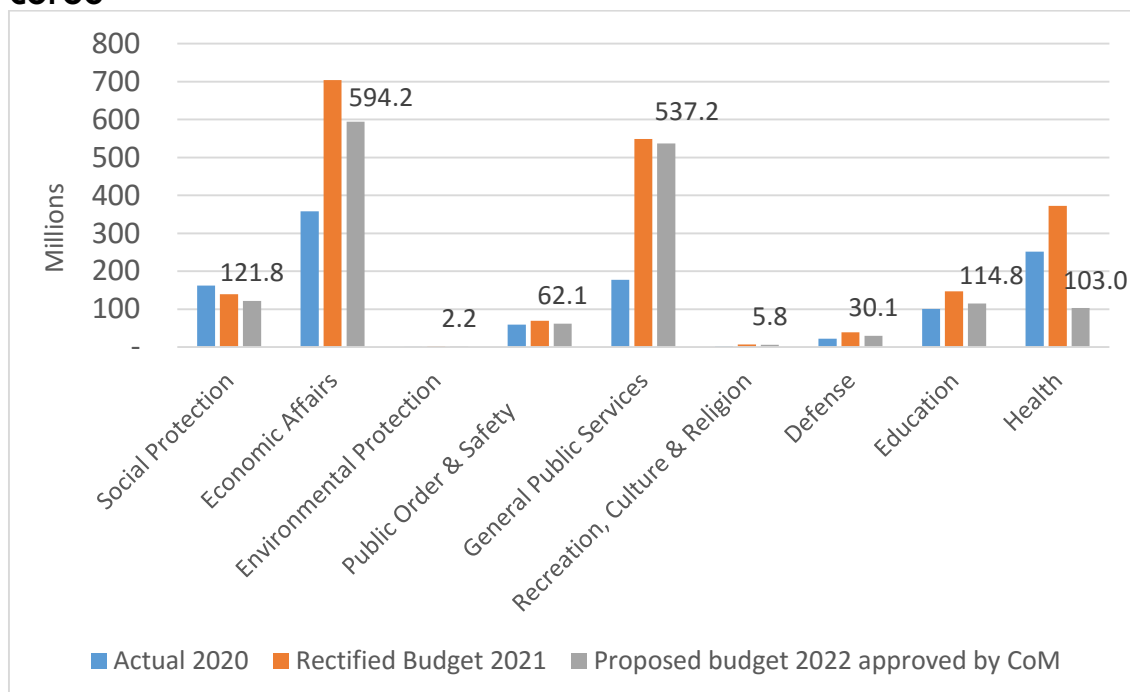


Source: General Directorate of Planning and Budget, Ministry of Finance 2022. Please note that all 2022 Infrastructure Fund allocations are preliminary and may change.

Following instead the international sectorial and more detailed classification COFOG (Classification of the Functions of Government), it can be observed that the General Public Services sector remains the largest, in line with previous year, followed by Economic Affairs, although both sectors see a significant reduction in appropriations. The decreasing trend in Health continues in 2023 mainly due to the progressive phase-out of the COVID-19 Fund. On the other hand, Social Protection and Education receive substantial increases in their funding for 2023 when compared to 2022, due to new GOP established priorities.

⁴ Since consolidated budget execution data including Social Security actual expenditure for 2021 was not available at the time of carrying out the analysis, 2021 Social Security budget was considered instead.

Figure 51: Comparison of 2021 Expenditure, Rectified 2022 GSB and proposed 2023 GSB by COFOG



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

7.2 2023 General State Budget (GSB) Proposal

The VIII Constitutional Government has approved a rectified Budget ceiling of \$3.2bn (excluding the social security fund). A simulated disaggregation according to spending categories is reported in the table below, although it must be noted that for 2023 GSB strict ceilings at the economic category level has not been imposed. In the spirit of program-based budgeting, entities with budgetary autonomy have more flexibility to allocate the available resources to the inputs that better contribute to deliver their programs at the exchange of achieving the pre-agreed results in terms of outcomes and outputs. Therefore, the disaggregation below is likely to change in the final approved GSB.

Table 10: Proposed 2023 Budget by Appropriation Category, \$ Millions

Appropriation Category	Proposed 2023 Budget
Salary and Wages	285.4
Goods and Services	448.6
Public Transfers	799.1
HCDF	17.7
RAEOA (Recurrent)	84
Social Security (Recurrent)	73.7

Total Recurrent Expenditure	1,708.5
Minor Capital	6.1
Capital and Development (IF includ. loans)	201.7
Capital and Development (LM, PDIM)	41.4
FCLN	1.000
RAEOA (Capital)	36
Social Security (Capital)	162
Total Capital Expenditure (including loans)	1,447.2
Loan Disbursements (included in IF above)	74.1
Support from DBS (included in app cat above)	4.9
Total Budget Ceiling	3,155.7

Source: General Directorate of Planning and Budget, Ministry of Finance 2022.

Recurrent expenditure amounts to \$1,708.5 billion. This is a 0.2% change compared to the rectified 2022 budget. Salaries and wages increase by a maximum of 6.1% to accommodate new recruitment, mainly in PNTL and FALINTIL F-FDTL, and civil servants' promotions. Goods and Services and Public Transfers are expected to get a substantial cut to allow this, falling 8.1% and 16.4% respectively. It should be noted, however, that the \$1bn allocated to the FCLN has been reclassified from transfers to capital expenditure in 2022 and 2023. Otherwise, the fall in transfers would get down to 59.1%. Moreover, RAEOA is set to receive \$84 million for recurrent expenditures in 2023, approximately the same amount as set in the rectified 2022 budget, although it should be noted that such amount used to gather recurrent and capital expenditures together and now RAEOA capital expenditure is set aside in FEDRAEOA. Something similar happens with Social Security, which has been budgeted \$73.7 million in recurrent expenditures. Its previous total appropriation amounted \$229.3 million but that also included the capital expenditure that in 2023 is set aside in the FRSS.

The Capital and Development fiscal ceiling is preliminarily set at \$1,447.2 million, including loan disbursements of \$74.1 million, which represents a decrease of -2.2% compared to 2022. However, after excluding the expenditure in financial assets carried out by the FCLN and the FRSS, the Capital and Development ceiling falls to \$279.1 million, decreasing by 41.8% respect to 2022. This amount is to be allocated according to the table below, where 72.3% falls under the Infrastructure Fund management and includes the budget for loan disbursements, and the rest is allocated to Line Ministries, RAEOA, SFAs and Municipalities. New capital measures will be discussed and presented in the expedited Budget Review Committee.

Table 11: Proposed Allocation of the Capital and Development 2023 Budget by Institution, \$ Millions

Institution	Proposed 2023 Budget
Infrastructure Fund (New and Ongoing Measures)	201.7

<i>Infrastructure Fund, out of which Loans</i>	74.1
Line Ministries, Autonomous Agencies	36.4
FEDRAEOA	36
Integrated Municipal Development Plan	5
Total	279.1

Source: General Directorate of Planning and Budget, Ministry of Finance July 2022.

The sources of financing of the proposed GSB are outlined in the table below. 20.9% 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; 79.1% come from oil and external sources, specifically excess withdrawals from the Petroleum Fund (34.8%). Cash balances from Treasury and RAEOA/ZEESM are forecast to contribute 10.1%, largely due to the low rates of execution of the current year's budget. FCLN (31.7%), loan disbursements (2.3%) and Direct Budget Support from the EU and Australia (0.2%) make up the remaining amount.

It is important to note that even under current expenditure levels, the expected total withdrawals (ESI and excess withdrawals) from the Petroleum Fund are \$1,581 million. This is already exceeding the \$1 billion cap on total annual withdrawals.

Timor-Leste's remains highly dependent on oil-derived (ESI and Excess Withdrawals) financing streams. Fiscal Sustainability analysis on the proposed ceiling predicts that the Petroleum Fund could be depleted by the year 2035, 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. Considering the Petroleum Fund return of 4.3% and the country's access to concessional debts streams with a financial cost below such rate, together with a forecasted debt over GDP of only 21% for 2023, the substitution of Petroleum Funds withdrawals by concessional borrowing will improve fiscal sustainability. However, expanding the sustainable, domestic, and non-oil revenue base remains key to ensure the country's long-term sustainability and development.

Table 12: Revenue and Financing Source of the Proposed 2023 General State Budget*, \$ Millions

	Proposed 2023 Budget
Government Expenditure	3,155.7
Revenue	658.5
Domestic Revenue	174.9
Estimated Sustainable Income	483.6
Fiscal Balance	(2,497.2)
Financing	2,497.2
Excess Withdrawals from the Petroleum Fund	1,098.2
FCLN	1,000
Loan Disbursements	74.1
Cash Balance	320
<i>From Treasury</i>	200
<i>From RAEOA/ZEESM</i>	120

	Proposed 2023 Budget
Direct Budget Support	4.9
From EU	3.3
From Government of Australia	1.6
Development Partner Commitments (not included in government expenditure)	120.9

Source: General Directorate of Planning and Budget, Ministry of Finance 2022. *Please note that all figures will be recalculated before the final budget proposal.

Disaggregation of the proposed 2023 General State Budget by receiving Public Entity

The tables below present the proposed 2023 GSB divided by Line Ministries, SFAs, and Municipal Authorities' allocations, comparing it with actual expenditure in 2021 and the approved rectified 2022 GSB. Only 21 Entities with Budgetary Autonomy (EBA) out of 100 see a reduction in their budgets compared to 2022, while 8 entities acquired budgetary autonomy for the first time in 2023, making a total of 108 institutions inside the budget perimeter. Given that the total budget ceiling is falling 7.58%, some entities if not all of them had to take a cut in their total appropriations. Nevertheless, for 2023 funding was reallocated across the budget perimeter considering past financial performance, budget rigidities determined by minimum functioning expenditures, contractual and legal obligations, and policy priorities set in GOP. Consequently, budget cuts were unequally distributed across EBAs with some of them reducing their appropriation and others increasing them. Indeed, when comparing to actual spending in 2021, fewer EBA, 12, see a reduction in their budget for 2023, which is a consequence of having considered financial performance – execution rates - in the model to disaggregate the budget ceiling. In general, for each institution the budget cut (increase) that they are getting for 2023 is smaller (larger) when compared to the actual expenditure in 2021 than to the rectified budget in 2022. An exception can be found in the “*Fundo COVID-19*”, but this is explained by the improvement in the COVID-19 pandemic.

Focusing on Line Ministries, 10 see a reduction in their budget when compared to the rectified 2022 GSB, 6 in the institutional framework sector, 3 in economic development, and 1 in social capital. The three institutions within this category getting the largest cuts are the “*Secretaria de Estado de Cooperativas*” (-89%) and the “*Ministério do Turismo, Comércio e Indústria*” (-73%), because of the phase-out of the unconditional cash-transfer program “*Cesta básica*”, together with “*Dotação Geral do Estado*” (-48%). On the other hand, the Line Ministries getting the largest increases are the “*Ministério do Plano e Ordenamento*” (105%), the “*Ministério da Educação, Juventude e Desporto*” (60%), and the “*Ministério da Solidariedade Social e da Inclusão*” (35%). The two latter see such an increase in their budget when compared to the 2022 rectified GSB because of the implementation of the policy measures prioritized in GOP.

When comparing the 2023 proposed GSB to the 2021 actual expenditure, only 6 Line Ministries see a reduction in their total appropriations, 3 in economic development, and one in each other sector. The three Line Ministries seeing the largest reductions are the “*Primeiro-Ministro*” (-55%), which is a consequence of several entities before depending on its budget getting now budgetary autonomy, the “*Secretaria de Estado da Juventude e Desporto*” (-21%), as a consequence of other institutions implementing largest shares of the educational sector budget, and the “*Secretaria de Estado de Cooperativas*” (-17%), again as a consequence of the “*Cesta básica*” phase-out. On the other hand, the “*Ministério da Defesa*” (144%), the “*Ministério da Solidariedade Social e da Inclusão*” (125%), the “*Dotação Geral do Estado*” (103%) see the largest increases in the 2023 GSB when compared to their actual expenditure in 2021.

Table 13: Proposed Allocation to Line Ministries, \$

Sector	Name	Actual 2021	Rectified 2022	Proposed 2023	Change from Actual 2021	Change from Rectified 2022
Capital Social	Secretaria de Estado da Juventude e Desporto	6,578,206	6,933,318	5,199,989	-21%	-25%
	Secretaria de Estado para a Igualdade e Inclusão	2,009,450	2,027,440	2,152,264	7%	6%
	Ministério do Ensino Superior, Ciência e Cultura	5,515,761	5,186,739	5,931,424	8%	14%
	Ministério da Saúde	48,988,226	52,181,675	60,004,384	22%	15%
	Ministério para os Assuntos dos Combatentes da Libertação Nacional	97,387,330	99,684,114	119,620,937	23%	20%
	Ministério da Solidariedade Social e da Inclusão	13,663,952	22,727,705	30,717,108	125%	35%
	Ministério da Educação, Juventude e Desporto	102,184,232	83,191,769	133,059,557	30%	60%
Desenvolvimento de Infra-estruturas	Ministério dos Transportes e Comunicações	10,886,027	11,534,455	11,558,253	6%	0%
	Ministério das Obras Públicas	210,633,457	160,431,417	176,811,256	-16%	10%
	Ministério do Plano e Ordenamento	8,202,388	6,480,851	13,314,298	62%	105%
Desenvolvimento Económico	Secretaria de Estado de Cooperativas	5,889,058	44,605,547	4,914,715	-17%	-89%
	Ministério do Turismo, Comércio e Indústria	8,984,288	56,003,356	15,002,853	67%	-73%
	Ministério do Petróleo e Minerais	78,923,813	82,620,903	74,120,903	-6%	-10%
	Ministro Coordenador dos Assuntos Económicos	1,634,206	2,103,170	2,121,445	30%	1%
	Secretaria de Estado da Formação Profissional e Emprego	5,561,507	4,815,221	5,116,172	-8%	6%
	Secretaria de Estado do Ambiente	2,646,597	2,753,596	3,078,236	16%	12%
	Ministério da Agricultura e Pescas	19,974,437	23,592,218	27,345,619	37%	16%
Enquadramento Institucional	Dotação Geral do Estado	135,766,371	525,254,428	275,116,438	103%	-48%
	Primeiro-Ministro	8,436,834	4,915,494	3,800,630	-55%	-23%
	Ministério do Interior	18,800,917	30,516,862	25,023,827	33%	-18%
	Ministério das Finanças	21,993,519	29,869,289	26,001,967	18%	-13%
	Polícia Nacional Timor-Leste	34,087,363	41,758,491	40,082,642	18%	-4%
	Ministérios dos Assuntos Parlamentares e Comunicação Social	6,598,329	9,066,076	8,706,165	32%	-4%

Provedoria dos Direitos Humanos e Justiça	1,588,749	1,697,168	1,803,241	14%	6%
Ministério da Justiça	10,996,058	12,751,594	13,548,569	23%	6%
Ministério dos Negócios Estrangeiros e Cooperação	21,327,530	24,684,687	27,770,273	30%	13%
Ministério da Administração Estatal	57,508,373	103,323,731	116,239,197	102%	13%
Ministério da Defesa	9,047,111	18,784,731	22,088,548	144%	18%
FALINTIL F-FDTL	21,647,966	25,527,233	33,022,685	53%	29%
Secretaria de Estado das Comunidades Timorenses no Exterior	-	-	500,000	N.A.	N.A.

Source: General Directorate of Planning and Budget, Ministry of Finance 2022.

For self-funded agencies, 10 see a fall in their budget ceilings when comparing the proposed 2023 budget to the rectified 2022 budget, 4 in the infrastructure development sector, 3 in social capital, 2 in economic development, and 1 in institutional framework. The three SFAs experiencing the largest budget reductions are the “*Instituto Nacional de Segurança Social*” (-68%), the “*Fundo COVID-19*” (-51%), and the “*Fundo das Infraestruturas*” (-39%). The reduction in the “*Instituto Nacional de Segurança Social*” comes from splitting the institution between the Institute and the Social Security Reserve Fund, but when considering both together their budgets increase respect to 2022. The cut suffered by the “*Fundo COVID-19*” is the natural consequence of the recovery from the pandemic and the coming back to normal financial management of health expenditures. Finally, the cut in the “*Fundo das Infraestruturas*” was made considering its poor financial implementation of previous contracts and the need to reallocate funds to meet the new GOT policy priorities in other sectors. On the other hand, the 3 SFAs seeing the largest budget increases compared to 2022 are the “*Imprensa Nacional de Timor-Leste, I.P.*” (114%), because of the operational need to cover two election rounds in 2023, the “*Serviços de Apoio à Sociedade Civil e Auditoria Social*” (104%), and the “*Administração dos Portos de Timor-Leste (APORTIL), I.P.*” (88%).

When we compared SFA’s 2023 proposed budget to 2021 actual expenditure, only 6 institutions see a reduction in their total appropriations, 3 in the sector of social capital and 3 in the sector of economic development. The largest reductions regard the “*Instituto Nacional de Segurança Social*” (-91%) and the “*Fundo COVID-19*” (-58%), again, plus the “*Centro Nacional de Emprego e Formação Profissional, I.P.*” (-12%). The latter is the consequence of GOP prioritizing the educational expenditure in pre-school and primary education before vocational education and training. However, it should be noted that the “*Centro Nacional de Emprego e Formação Profissional, I.P.*” sees a budget increase of 5% when compared to its 2022 budget. On the other hand, the three SFAs seeing the largest budget increases compared to 2021 actual expenditure are the “*Imprensa Nacional de Timor-Leste, I.P.*” (158%) and the “*Administração dos Portos de Timor-Leste (APORTIL), I.P.*” (232%), again, plus the “*Centro Logístico Nacional*” (214%). However, the latter sees a reduction of 18% compared to its 2022 budget.

Table 14: Proposed Allocation to SFAs in GSB 2023, \$

Sector	SFA	Actual 2021	Rectified 2022	Proposed 2023	Change from 2021 Actual	Change from Rectified 2022
Capital Social	Instituto Nacional de Segurança Social	177,579,000 ⁵	229,285,500	73,707,655	-58%	-68%

⁵ 2021 Budget

	Fundo COVID-19	202,235,478	37,625,198	18,312,599	-91%	-51%
	Centro Nacional Chega!	1,959,630	2,547,331	2,088,811	7%	-18%
	Serviço Autónomo de Medicamentos e Equipamentos de Saúde, I.P.	9,632,864	9,235,500	9,235,500	-4%	0%
	Arquivo e Museu da Resistência Timorense	1,870,879	1,868,527	1,868,527	0%	0%
	TATOLI - Agência Noticiosa de Timor-Leste, I.P.	571,494	647,806	647,806	13%	0%
	Laboratório Nacional de Saúde, I.P.	572,044	823,345	823,345	44%	0%
	Serviço Nacional de Ambulância e Emergência Médica, I.P.	851,011	1,291,141	1,291,141	52%	0%
	Instituto Politécnico de Betano	886,847	1,201,241	1,211,679	37%	1%
	Instituto Nacional de Ciências e Tecnologia	517,061	490,824	552,177	7%	13%
	Universidade Nacional de Timor Lorosa'e	15,101,145	16,576,893	18,649,005	23%	13%
	Instituto Nacional de Saúde	822,329	1,030,292	1,159,079	41%	13%
	Hospital Nacional Guido Valadares	8,722,260	11,170,875	12,567,234	44%	13%
	Agência Nacional para Avaliação e Acreditação Académica	368,483	368,416	442,099	20%	20%
	Fundo de Desenvolvimento de Capital Humano	8,768,759	12,000,000	17,748,526	102%	48%
	Centro Nacional de Reabilitação, I.P.	1,088,892	898,200	1,400,000	29%	56%
	Serviços de Apoio à Sociedade Civil e Auditoria Social		10,151,000	20,717,247	N.A.	104%
	Fundo de Reserva da Segurança Social	-	-	162,007,651	N.A.	N.A.
	Instituto Nacional de Combate ao HIV-SIDA, I.P.	-	-	500,000	N.A.	N.A.
	Instituto Para a Defesa dos Direitos da Criança, I. P.	-	-	300,000	N.A.	N.A.
Desenvolvimento de Infra-estruturas	Fundo das Infraestruturas	80,639,963	332,453,139	201,743,720	150%	-39%
	Agência de Tecnologia de Informação e Comunicação, I.P. – TIC TIMOR	2,198,478	6,353,916	4,765,437	117%	-25%
	Autoridade Nacional para a Eletricidade, I.P.	257,383	543,000	445,260	73%	-18%
	Agência de Desenvolvimento Nacional, I.P.		4,567,240	4,525,430	N.A.	-1%
	Instituto de Gestão de Equipamento de Timor-Leste, I.P.	2,990,341	4,113,844	4,113,844	38%	0%

	Autoridade Nacional de Comunicações, I.P.	885,838	1,288,608	1,288,608	45%	0%
	Autoridade da Aviação Civil de Timor-Leste, I.P.	629,933	685,226	691,180	10%	1%
	Autoridade Nacional de Água e Saneamento, I.P.	490,107	592,000	666,000	36%	13%
	Administração dos Portos de Timor-Leste (APORTIL), I.P.	1,651,559	2,925,042	5,486,286	232%	88%
Desenvolvimento Económico	Centro Logístico Nacional	1,728,552	6,620,745	5,429,011	214%	-18%
	Agência de Promoção de Investimento e Exportação de Timor-Leste, I.P.	613,185	791,514	672,787	10%	-15%
	Autoridade de Inspeção e Fiscalização da Atividade Económica, Sanitária e Alimentar, I.P.	1,061,278	1,006,370	1,015,115	-4%	1%
	Instituto Nacional de Desenvolvimento de Mão-de-Obra	443,107	497,529	501,852	13%	1%
	Centro Nacional de Emprego e Formação Profissional, I.P.	1,173,658	979,354	1,028,322	-12%	5%
	Instituto Para a Qualidade de Timor-Leste, I.P.	1,250,226	1,042,858	1,108,037	-11%	6%
	Serviço de Registo e Verificação Empresarial, I.P.	1,694,562	2,537,259	2,695,838	59%	6%
	Instituto de Apoio ao Desenvolvimento Empresarial	1,015,868	1,091,269	1,227,678	21%	13%
	Inspeção-Geral do Trabalho	437,459	490,868	589,042	35%	20%
	Instituto de Pesquisa, Desenvolvimento, Formação e Promoção do Bambu	610,875	616,420	739,704	21%	20%
	Centro Nacional de Formação Profissional - Becora, I.P.	660,893	613,187	735,824	11%	20%
	Instituto de Petróleo e Geologia, I.P.		4,000,000	6,000,000	N.A.	50%
	Autoridade Nacional do Petróleo e Minerais, I.P.		-	8,500,000	N.A.	N.A.
	Enquadramento Institucional	Comissão Anti-Corrupção	1,495,879	2,632,856	2,158,942	44%
Parlamento Nacional		11,537,174	16,210,224	16,210,224	41%	0%
Presidência da República		6,026,449	10,088,413	10,088,413	67%	0%
Instituto Nacional da Administração Pública		794,420	1,028,885	1,037,825	31%	1%
Inspeção-Geral do Estado		540,790	932,054	940,153	74%	1%
Presidência do Conselho de Ministros		4,502,127	4,717,347	4,758,338	6%	1%

Tribunais	5,203,765	7,351,187	7,516,068	44%	2%
Procuradoria-Geral da República	4,386,797	4,415,573	4,675,170	7%	6%
Comissão da Função Pública	2,280,706	2,782,071	2,955,950	30%	6%
Conselho de Imprensa	690,331	865,935	920,056	33%	6%
Instituto de Defesa Nacional	1,169,642	1,577,149	1,675,721	43%	6%
Conselho Para a Delimitação Definitiva das Fronteiras Marítimas	947,607	980,725	1,043,686	10%	6%
Polícia Científica de Investigação Criminal	1,981,143	1,795,233	2,019,637	2%	13%
Serviço Nacional de Inteligência	1,386,957	1,406,500	1,582,313	14%	13%
Secretariado Técnico da Administração Eleitoral		1,576,870	1,773,979	N.A.	13%
Comissão Nacional de Eleições	8,206,131	8,558,935	10,270,722	25%	20%
Arquivo Nacional de Timor-Leste, I.P.		401,400	481,680	N.A.	20%
Imprensa Nacional de Timor-Leste, I.P.	399,058	481,506	1,029,718	158%	114%
Agência Nacional de Planeamento, Monitorização e Avaliação	-	-	800,000	N.A.	N.A.

Source: General Directorate of Planning and Budget, Ministry of Finance 2022.

Regarding municipalities, all see an increase in comparison to the current year's budget with the largest raise for "Administração Municipal de Viqueque" (50%) and the smallest for "Administração Municipal de Díli" (8%), although this one has still a budget two of three times larger than any other municipality. The 1% cut for RAEOA becomes a 42% increase when we account for the creation of the FEDRAEOA. Also note that another special fund is created for Ataúro with a total appropriation of \$13 million, making a 523% total budget increase for that municipality.

A similar situation arises when comparing the 2023 GSB proposal with the 2021 actual expenditure. All the municipalities see an increase in their budget ranging from 20% for "Autoridade Municipal de Baucau" to 77% for "Administração Municipal de Viqueque". RAEOA sees an increase of 244% that, in the reality, is a 392% when we include the FEDRAEOA.

Table 15: Proposed Allocation to Municipal Authorities, \$

Municipal Authority	Actual 2021	Rectified 2022	Proposed 2023	Change from 2021 Actual	Change from Rectified 2022
Autoridade da Região Administrativa Especial de Oe-Cusse Ambeno	24,383,698	84,436,784	84,000,000	244%	-1%
Autoridade Municipal de Díli	6,816,419	10,231,640	11,064,640	62%	8%
Autoridade Municipal de Baucau	4,813,128	4,931,124	5,764,124	20%	17%
Autoridade Municipal de Bobonaro	4,215,429	4,727,883	5,560,883	32%	18%
Autoridade Municipal de Ermera	3,904,589	4,662,818	5,530,114	42%	19%
Administração Municipal de Ataúro		2,574,860	3,064,145	N.A.	19%
Administração Municipal de Lautém	3,699,987	4,056,049	4,889,049	32%	21%
Administração Municipal de Covalima	3,985,211	3,990,360	4,823,360	21%	21%

Administração Municipal de Manatuto	2,994,422	3,815,911	4,648,911	55%	22%
Administração Municipal de Manufahi	3,724,390	3,666,128	4,499,128	21%	23%
Administração Municipal de Ainaro	2,976,385	3,243,066	4,076,066	37%	26%
Administração Municipal de Liquiçá	2,577,632	3,186,810	4,019,810	56%	26%
Administração Municipal de Aileu	2,811,826	3,034,303	3,867,303	38%	27%
Administração Municipal de Viqueque	3,395,558	4,005,625	5,996,531	77%	50%
Fundo Especial de Desenvolvimento de Ataúro	-	-	13,000,000	N.A.	N.A.
Fundo Especial de Desenvolvimento da Região Administrativa Especial de Oe-Cusse Ambeno	-	-	36,000,000	N.A.	N.A.

Source: General Directorate of Planning and Budget, Ministry of Finance 2022.

When looking at the budget composition, the percentage out of the total budget allocated to Line Ministries has decreased compared to the 2022 rectified GSB but, at the same time, is better aligned with the percentage of the actual expenditure that they implemented in 2021. “*Dotação Geral do Estado*” (12.76%), “*Ministério das Obras Públicas*” (8.20%), and “*Ministério da Educação, Juventude e Desporto*” (6.17%) are the individual institutions appropriating the largest percentages of the 2023 proposed GSB. Nevertheless, the “*Dotação Geral do Estado*” has seen the largest percentage point decrease, equal to -8.99 percentage points, when compared to the 2022 rectified GSB. “*Ministério das Obras Públicas*” (1.56 percentage points) and “*Ministério da Educação, Juventude e Desporto*” (2.73 percentage points) are, on the other hand, the institutions seeing the largest percentage points point increase compared to 2022 together with “*Ministério para os Assuntos dos Combatentes da Libertação Nacional*” (1.42 percentage points).

SFAs see the largest reduction of their budget as percentage of the 2021 actual expenditure, -4.64 percentage points, and as percentage of the 2022 rectified GSB, -1.12 percentage points. The proposed 2023 GSB allocates to them 31.13% of the total budget. On the other hand, municipalities see a substantial raise of their weight over the total budget, appropriating 9.31% of it, because of their role in the implementation of the “*Merenda Escolar*” program. This represents a percentage point increase equal to 5.01 compared to their weight over the actual expenditure in 2021 and equal to 3.49 compared to their weight over the rectified 2022 GSB.

Table 16: Comparison of 2021 Expenditure, rectified 2022 GSB and proposed 2023 GSB by Budget %

Name	Actual 2021	Rectified 2022	Proposed 2023	% Point Change from 2021 Actual	% Point Change from Rectified 2022
Secretaria de Estado das Comunidades Timorenses no Exterior	0.00%	0.00%	0.02%	0.02%	0.02%
Provedoria dos Direitos Humanos e Justiça	0.10%	0.07%	0.08%	-0.01%	0.01%
Ministro Coordenador dos Assuntos Económicos	0.10%	0.09%	0.10%	0.00%	0.01%
Secretaria de Estado para a Igualdade e Inclusão	0.12%	0.08%	0.10%	-0.02%	0.02%
Secretaria de Estado do Ambiente	0.16%	0.11%	0.14%	-0.02%	0.03%
Primeiro-Ministro	0.52%	0.20%	0.18%	-0.34%	-0.03%
Secretaria de Estado de Cooperativas	0.36%	1.85%	0.23%	-0.13%	-1.62%

Secretaria de Estado da Formação Profissional e Emprego	0.34%	0.20%	0.24%	-0.10%	0.04%
Secretaria de Estado da Juventude e Desporto	0.40%	0.29%	0.24%	-0.16%	-0.05%
Ministério do Ensino Superior, Ciência e Cultura	0.34%	0.21%	0.28%	-0.06%	0.06%
Ministério dos Assuntos Parlamentares e Comunicação Social	0.40%	0.38%	0.40%	0.00%	0.03%
Ministério dos Transportes e Comunicações	0.67%	0.48%	0.54%	-0.13%	0.06%
Ministério do Plano e Ordenamento	0.50%	0.27%	0.62%	0.11%	0.35%
Ministério da Justiça	0.67%	0.53%	0.63%	-0.05%	0.10%
Ministério do Turismo, Comércio e Indústria	0.55%	2.32%	0.70%	0.15%	-1.62%
Ministério da Defesa	0.55%	0.78%	1.02%	0.47%	0.25%
Ministério do Interior	1.15%	1.26%	1.16%	0.01%	-0.10%
Ministério das Finanças	1.35%	1.24%	1.21%	-0.14%	-0.03%
Ministério da Agricultura e Pescas	1.22%	0.98%	1.27%	0.04%	0.29%
Ministério dos Negócios Estrangeiros e Cooperação	1.31%	1.02%	1.29%	-0.02%	0.27%
Ministério da Solidariedade Social e da Inclusão	0.84%	0.94%	1.42%	0.59%	0.48%
FALINTIL F-FDTL	1.33%	1.06%	1.53%	0.20%	0.47%
Polícia Nacional Timor-Leste	2.09%	1.73%	1.86%	-0.23%	0.13%
Ministério da Saúde	3.00%	2.16%	2.78%	-0.22%	0.62%
Ministério do Petróleo e Minerais	4.84%	3.42%	3.44%	-1.40%	0.02%
Ministério da Administração Estatal	3.53%	4.28%	5.39%	1.87%	1.11%
Ministério para os Assuntos dos Combatentes da Libertação Nacional	5.97%	4.13%	5.55%	-0.42%	1.42%
Ministério da Educação, Juventude e Desporto	6.26%	3.45%	6.17%	-0.09%	2.73%
Ministério das Obras Públicas	12.91%	6.64%	8.20%	-4.71%	1.56%
Dotação Geral do Estado	8.32%	21.75%	12.76%	4.44%	-8.99%
Total Line Ministries	59.92%	61.92%	59.55%	-0.37%	-2.37%
Total SFA	35.77%	32.26%	31.13%	-4.64%	-1.12%
Total Municipalities	4.31%	5.82%	9.31%	5.01%	3.49%
Total	100.00%	100.00%	100.00%	0.00%	0.00%

Source: General Directorate of Planning and Budget, Ministry of Finance 2022. Calculations exclude the FCLN.

8 Loans and Public Private Partnerships

8.1 Loans

The Government currently still depends on foreign loans 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.

8.1.1 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 67% of the total loan amount followed by WB and JICA. Below are the terms of the loans:

Table 17: Terms of Loans

Lender	Currency	Approved loan US \$m	Grace Period (year)	Initial Amortization (year)	Year Complete	Interest rate FY 2021
ADB	USD, SDR	488.65	5.3	20	2044	1.30%
WB	USD, SDR	174.20	8	20	2060	2.69%
JICA	JPY	68.72	10	20	2042	0.60%
Total		731.58				

Source: Ministry of Finance, July 2022

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 (1.50 %) is currently lower than the estimated sustainable return (or ESI) from the Petroleum Fund (3%) ensuring that the future debt repayments remain well within the country's capacity to pay.

Table 18: Cost of borrowing vs PF return

Description	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Cost of borrowing (effective rate)				1.02%	1.42%	1.68%	2.06%	2.34%	2.03%	1.50%
PF historical return	4.1%	4.4%	4.2%	3.8%	3.8%	4.4%	3.8%	4.5%	4.84%	4.91%

Source: Ministry of Finance, July 2022.

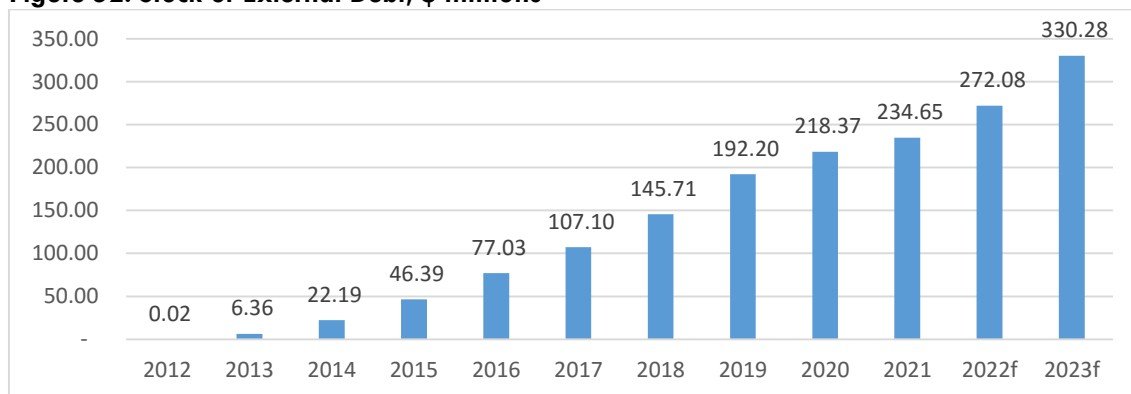
8.1.2 Portfolio Management

The management of public debt plays a critical role in determining the sustainability of fiscal policy. Due to a 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, who revised down the rating from medium to weak leading to lower debt burden thresholds. Similarly, 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 \$234.65m in 2021 from \$218.37m at the end of 2020. The 8% increase is attributable to the total new disbursement of \$22.65m from multilateral and bilateral institutions including ADB, WB and JICA for ongoing and new projects. Interest and other fee related payments declined from \$3.90m in 2020 to \$3.40m as at end of 2021 due to low execution. This amount is relatively small compared to the amount the government currently owes to these lenders.

Figure 52: Stock of External Debt, \$ millions



Source: Ministry of Finance, July 2022.

While the impact of Covid-19 outbreak and recent flood disaster in April 2021 was delaying a number of key capital projects, disbursements in 2022 are expected to increase by 32% compared to the previous year. Further increase of disbursement of loans is also expected in 2023, with loan disbursements forecast to reach \$74.11 million, leading to an estimated total debt stock of \$330.28 million by the end of 2023.

Debt Indicators

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

Table 19: External Debt Indicators for the period 2018-2023, % of GDP and Revenue

	2018	2019	2020	2021	2022f	2023f
Total External Debt to GDP	9.20%	11.12%	13.44%	13.05%	14.07%	16.53%
Total Debt Service to Revenue	0.42%	1.00%	1.08%	1.40%	2.74%	3.32%
In millions of US dollars, unless otherwise indicated						
Memorandum items:						
Total external debt	145.71	192.20	218.37	234.65	272.08	330.28
Debt Service	3.12	7.18	7.84	9.77	19.29	21.65
GDP (nominal)	1583.2	1727.9	1624.3	1798.3	1933.9	1998.1
Revenue (ESI + domestic revenue ex RAE OA)	741.45	715.50	726.82	698.51	704.46	653.01

Source: Ministry of Finance, July 2022.

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 countries⁶. While the ratio has consistently increased from

⁶ Further reference on this subject: "Guidance Note the Bank-Fund Debt Sustainability Framework for Low Income Countries", February 2018.

9.2% in 2018 to 13.05% in 2021, the values are far below 30%. This marginal increase was due to an increase in disbursement and a downward trend in GDP growth. While there was a slight recovery between 2018 and 2019, the percentage increase in external debt was still higher than GDP growth, leading to a higher external debt to GDP ratio.

Debt Service to Revenue – The debt service to revenue ratio is expected to increase from 1.1% in 2020 to 1.40% in 2021. This was primarily due to an increase in debt service payments. Principal repayment started in September 2017 on ADB loan 2857. Despite the increase, this percentage of debt service to revenue is still well-under the 14% threshold.

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 20: Debt Service Forecasts, \$m

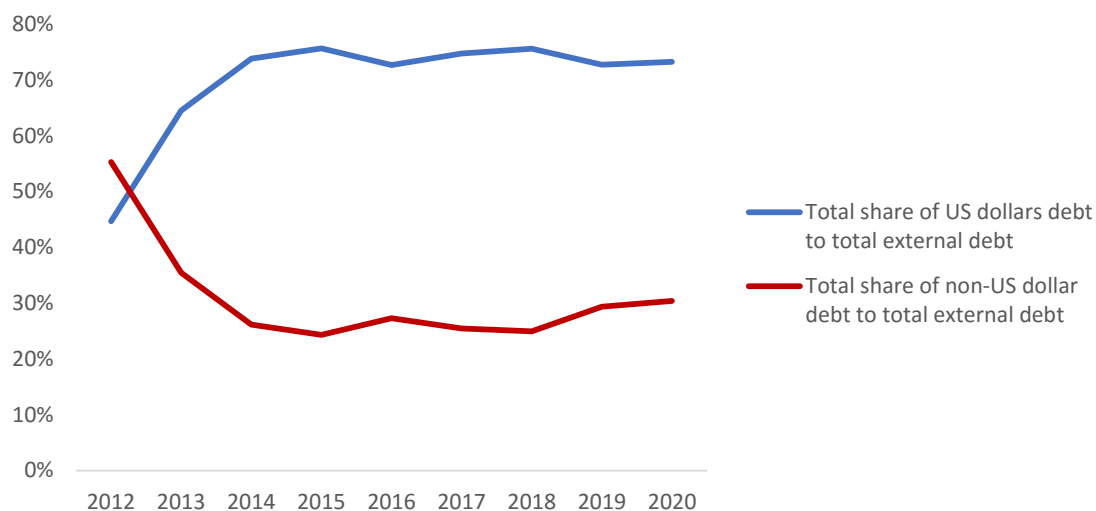
Lender	Debt Service	2020 Actual	2021 Actual	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.
ADB	Principal	3.11	5.55	8.84	10.84	12.74	13.48	14.84
	Interest	2.39	1.79	3.38	2.71	4.44	5.63	6.70
	Charges	0.11	0.10	0.10	0.49	0.17	0.11	0.06
WB	Principal	0.83	0.83	2.19	2.81	2.81	2.81	2.81
	Interest	0.85	0.92	1.19	1.14	1.15	1.10	1.04
	Charges	0.38	0.40	0.95	1.09	1.09	1.11	1.12
JICA	Principal	0.00	0.00	2.34	8.84	2.26	2.26	2.26
	Interest	0.15	0.17	0.29	3.38	0.29	0.28	0.26
	Charges	0.02	0.02	0.01	0.00	-	-	-

Source: Ministry of Finance, July 2022.

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 dollarized economy, the large share of US dollar currency debt in the portfolio (68 percent in 2021) cushioned the Government from extreme exchange rate movements. The policy to retain a larger share of debt in US dollars is set to continue at least in the short to medium term.

Figure 53: US dollars debt vs non-US dollars Debt

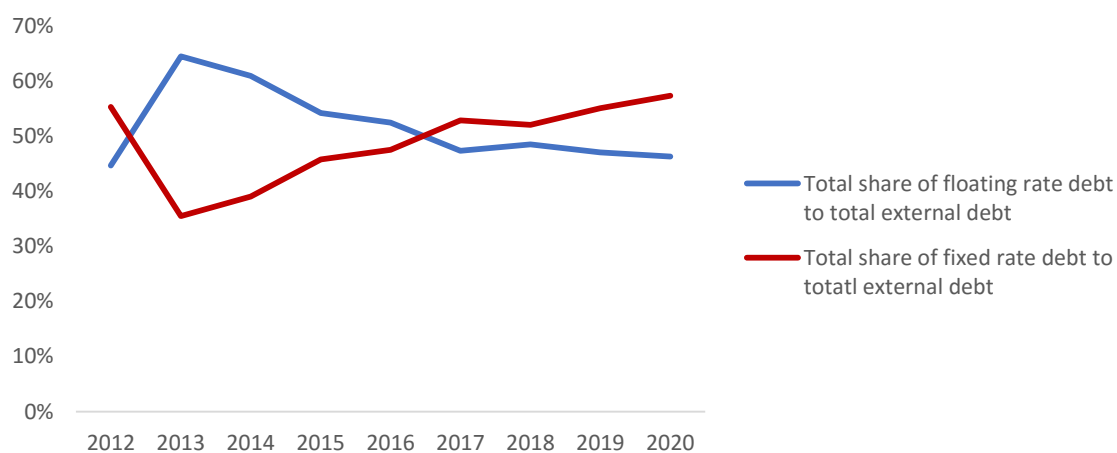


Source: DNPME, Ministry of Finance, July 2022

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 government’s ability to manage interest rate risk independently by converting the priority for disbursement from variable rate to fixed rate accounting for market interest rate fluctuation.

The cost of borrowing is expected to continue to rise as TL is now classified as a blend country⁷ and is slowly being phased out from concessional financing by its external creditors. To limit the exposure to interest rate shocks, there needs to be an expansion in concessional financing from bilateral loan providers.

Figure 54: Fixed vs Floating Debt



Source: DNPME, Ministry of Finance, June 2022.

⁷ Being a blend country, TL has a limited access to concessional lending with a fixed interest rate.

8.1.3 Current Project Status

There are currently 15 ongoing road projects funded by concessional loans of which 12 projects have either achieved (or are close to) completion. These include roads connecting Tibar-Liquica/Tibar-Gleno, Manatuto-Laclubar junction, Laclubar junction Natarbora, Manatuto-Baucau Solerema-Ainaro corridor, Hera-Manatuto, and Tasitolu-Tibar. Other projects that most likely to be concluded by 2022 are roads from Baucau-Lautem, and Maubara-Karimbala+Atabae-Motaain, bringing the total percentage of completed projects to 87% by end the year.

Total capital contribution made by this investment is \$429.85m. Concessional loans accounted for approximately 61.97% of this figure. Of this, \$196.39m has been disbursed leaving a balance of \$70.03m 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 \$29.18m for further disbursement.

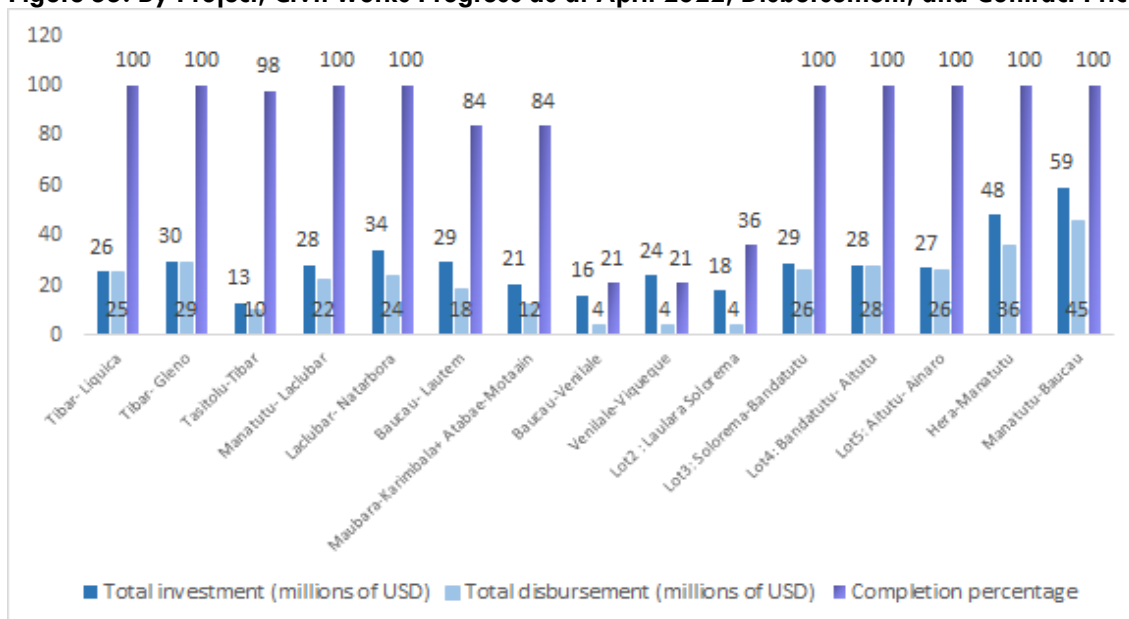
New projects include Gleno-Letefoho-Hatubuilico road section, Water Supply and Sanitation for Baucau Viqueque, Lautem and Manufahi municipalities, Basic Education Strengthening and Transformation (BEST), Nicolau Lobato International Airport and Power Distribution Modernization. The key challenges in 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 is explained by the trends illustrated in the graph below, in which projects progress was relatively high, in comparison to disbursements.

Table 21: Total investment in Civil Works

Source of Fund	Total Investment in Civil Works	Disbursement as at April 2022	Contract Balance
Loan Fund	266.40	196.39	70.03
State Contribution	163.45	134.27	29.18
Total	429.85	330.66	99.21

Source: Ministry of Finance, April 2022.

Figure 55: By Project, Civil Works Progress as at April 2022, Disbursement, and Contract Price



Source: DNPME, Ministry of Finance, April 2022.

There is about US \$40m 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 US \$20.04m in saving while other projects such as Manatuto-Natabora, Baucau-Viqueque, Manatuto- Baucau, and Tacitolu-Tibar accounted for the remaining balance.

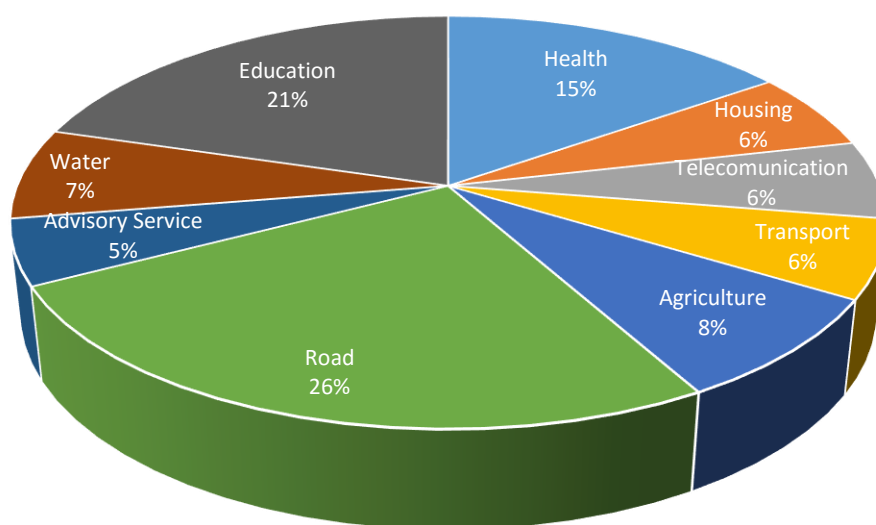
As a borrower, the Government can decide whether to fully utilise the saving or simply cancel the amount by complying with public debt law No.13/2011 and other relevant laws. For this purpose, the Government has already requested ADB to maximise the use of some of this saving to fund for the construction 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.

8.1.4 Future Loans

Infrastructure development will continue to play a key role in the country’s economic development success in the medium term. New strategic sectors such as water, education, health, housing, and agriculture, 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, the 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 2021 which is 13.05%. 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 \$490m for new concessional foreign loans to be negotiated in 2023.

Figure 56: Sectoral Allocation of Proposed Loan Ceiling for 2023



Source: DNPME, Ministry of Finance, April 2022.

8.2 Public Private Partnerships

8.2.1 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.

8.2.2 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.

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 2022, the total amount disbursed from VGF was USD 84.142 million and total expenses of the project was USD 207.74 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. Financial Advisory Service Agreement between GoTL and IFC expired in 30 June 2022. Now, the Government need to retain the services provided by IFC and 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 scale 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 international visitors coming 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 the final Feasibility Study and Transaction Structuring phase. The project, however, is experiencing delays due to several issues that are currently being closely addressed by the team.

Presidente Nicolau Lobato International Airport Development

The Master Plan for the development of Presidente Nicolau Lobato International Airport ("the Airport") was approved in October 2019 by the Council of Ministers (CoMs). Further, through technical assistance of ADB, the Government had also prepared feasibility study for the entire project with focus on several key components, such as runway, aprons, parallel taxiways and control tower which is planned to be financed through ADB loan.

The project will be implemented in phases. Phase I includes (i) Construction and extension of runway, apron, control tower, ground lighting, taxiways & parallel taxiway; (ii) Construction of passenger terminal; (iii) Construction of essential infrastructures; (iv) Construction of VIP Terminal; (v) LACSP and Environmental License; (vi) PPP process for Operation, Maintenance and Finance – Concession. The project involves a number of stakeholders focusing on the preparation works, implementation and financing of above components, including the Asian Development Bank (ADB), International Finance Corporation (IFC), Japan International Cooperation Agency (JICA), Department of Foreign Affairs and Trade (DFAT) and Australia Infrastructure Fund Facility (AIFF). Phase II covers further extension of the runway 400 meters seawards by 2032, while expansion of the passenger terminal will depend on the traffic growth.

In terms of financing, a total of \$350.1 million has been secured from development partners. It comprises of loans from ADB (38.2%) and AIFF-Australia (14%), grants from Government of Japan (10.8%) and DFAT-Australia (6%) and Infrastructure Fund of the GoTL (31%). This financing structure has been adjusted through aligning with policy decision and understanding reached with development partners. In this connection, a total of 12 essential components that were allotted under GoTL financing were shifted to Australia’s DFAT grants and AIFF loan financing package. The initial budget allocated for preparation of feasibility studies and detail-engineering design (DED) has been replaced by AIFF (grant) and loan financing from AIFF. Therefore, initial budget line under previous PBS has been adjusted to reflect such changes.

Table 22: Budget Summary

BUDGET SUMMARY (\$'million)											
No		2021	2022	2023	2024	2025	2026	2027	Total Amount (\$)	%	Source of Fund
1	ADB	0	0	16.3	51.4	33.2	33.6	0.5	135	38.2	Loan
2	JICA		0	10	15	8	5	0	38	10.8	Grant
3	DFAT	0	0	8	9	3	0	0	20	6	Grant
4	AIFF	0	0	8	10	15	10	7	50	14	Loan
5	IF/GoTL	0.6	12.08	35.37	33.87	19.04	4.14	2	107.1	31	IF/GoTL
	Total	0.6	12.08	77.67	119.27	78.24	52.74	9.5	350.1	100	

Loan negotiation between ADB and GoTL was successfully conducted on 17 and 18 of May 2021, while negotiation of JICA grant component was also concluded during mid 2021 that led to signing of Loan Agreement with ADB and “Exchange of Note” (EN) between GoTL and Government of Japan on the 1st of October 2021. A high-level commitment had also been reached between the GoTL and Government of Australia on essential components of the airport’s infrastructures to be financed through loan and grant from the Australian Infrastructure Fund Facility (AIFF) and Department of Foreign Affairs and Trade (DFAT). It is anticipated the loan and grant agreements between the two countries to be signed during last quarter of 2022. As reflected in the below table, the high budget allocation for the following years was based on the implementation plan for different components of the project under different financing and implementation arrangements.

The project is at different stages of implementation. For instance, procurement for recruitment of Design Build Contractor (DB) and Consultant Supervision (CSC) under component 1 and Project Management Consultancy (PMC) had been launched and contracts will be awarded during the last quarter of 2022. 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.

Implementation of the FASA agreement is well on schedule with the completion and approval of feasibility study and transaction structuring report (TSR) by the Inter-ministerial Commission and Council for Administration of Infrastructure Fund (CAFI). These approvals include decision on the suitable PPP options that meets GoTL's aspiration for operation and maintenance of the entire airport as well investment for phase II extension of the runway and expansion of the passenger terminal building. In terms of disbursement, the project has disbursed \$0.6 million for stage 1 FASA implementation during 2021, while the remaining balance of \$0.5 million for stage 2 procurement is targeted to be executed during late 2022 and early 2023.

Another key element of the project is the implementation of Land Acquisition, Compensation and Support Plan (LACSP). Data collection and verification for phase 1 LACSP have been completed. Prior to that, an independent market appraisal was conducted and completed during 1st quarter of 2022. Presentation on the LACSP scope, processes and unit prices for land, agricultural plants and structures by the Joint Committee for LAC to the IMC and CAFI was conducted on the 30 March and 8 July 2022 and decisions were secured for unit prices for land and other assets of the affected communities. Preparation of a Government Resolution for Unit Price and compensation of assets and properties is underway and expected to be presented to the Council of Minister's (COM) by end of July 2022. Once COM approves the proposed Unit Prices for LACSP, the Joint Committee for LAC will immediately initiate socialization processes and acquisition of land and properties with completion target date within the fiscal year of 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 November 2022, handling of all international cargo will move to Tibar Bay Port. As such, Dili Port will be vacant and will solely be used for handling of domestic cargo as well as 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 commercial urban development and 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 increased from 2022 in 2016 to 3467 and 6172 in 2018 and 2019 respectively, representing more than 200% of increase in only 3 years between 2016 and 2019. Other potential activities that can be pursued when the development is materialized is Dili becoming host to international yacht race as well as other marine tourism excursions such as whale and dolphin watching.

As a historic site, on the other hand, the development of Dili Port should be planned carefully as not to ruin its characters. In 2022, several discussions were held with State Secretary of Art and Culture (SEAC – Portuguese Acronym) and Centru Nacional Chega! (CNC – Portuguese Acronym) to ensure that the development of the feasibility study does not lose sight on the need to preserve historical, cultural and archaeological values of the site. During these discussions, it was clarified that from SEAC and CNC point of view, the development can proceed as identified in the Feasibility Study with concerns to be addressed including:

- Excavation during construction activities should adhere to best practices regarding archaeological findings;

- Design should incorporate cultural and historical elements to ensure seamless integration with surrounding areas;
- There should be a place for monument to commemorate events at the start of Indonesian invasion;
- There should be a place set aside to sell merchandise for veteran groups.

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 PPP projects in certain sectors. 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 is currently being prepared 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 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 and maintaining prudent practices including conduct of feasibility study and open tender. Close coordination is currently happening with MTCI and MCAE within the context of Inter-Ministerial Commission for Tourism Development.

8.2.3 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 2022, interest earned amounted to **\$8.72m**, 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, 2020 and 2021 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, Dili water supply PPPs and affordable housing PPP, 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 2023 budget contains similar provisions (except for operational Budget of DNPPP and PMU TBP is not reported as it was centralized in the General Directorate of Corporate Service) 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 2023 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. Transport sectors and new initiatives are likely to require allocation of budgets from 2023 onward.

The following are actual expenditure for 2017 to 2021, estimated expenditure for 2022, and estimated budget allocation for 2023 onward.

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

	2017 Actual	2018 Actual	2019 Actual	2020 Actual	2021 Actual	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	130.57	186.1	98.4	70.28
Dotação Todo Governo										
PMU Cristo Rei Project					0.02	0.14	0.15	0.116	0.02	0.02
PMU Dili Airport Project					0.65	1.93	1.85	1.85	1.85	
Medical Diag. – Service Payment					1.5	2	12	17.9	17.9	17.9
PMU Affordable Housing							0.18	0.18	0.18	0.18
PMU Dili Port							0	0.2	0.76	0.76
SUB TOTAL	0	0	0	0	2.17	4.07	14.13	20.23	20.8	18.94
Infrastructure Fund										
TBP PPP										
PT FASA*	0.15	0.15								
IE* payment		0.31	0.32	0.32	0.43	0.55	0.21			
Roundabout (Inc. Resettlement)				0.25	0.25	1.47	1.3			
EDTL Dist. Line from Substation Liquica				0.32	0.32	1.04	3.65			
SUB TOTAL	0.15	0.46	0.32	0.89	1	3.06	5.16	0	0	0
Medical Diag. PPP										
FS FASA & PT FASA*	0.1		0.2		0.09	0.48	0.66	0.3	0.3	0.3
IM* payment						0.3	0.3	0.3	0.3	0.3
SUB TOTAL	0.1	0	0.2	0	0.09	0.78	0.96	0.6	0.6	0.6
Affordable Housing PPP										
FS FASA & PT FASA*				0.12	0.26	0.45	1.15	0.15		
Resettlement – Site Clearance						0.5				
Construction (VGF, Infra., E&S cost)					0	2	30.2			

SUB TOTAL	0	0	0	0.12	0.26	2.95	31.35	0.15	0	0
Tourism PPP										
FS, TSR* and Resettlement to Cristo Rei PPP					0.11	0.3	0.4	0	0	0
Construction (Capex & Opex Cristo Rei)						0.15	0.25	0	0	0
SUB TOTAL	0	0	0	0	0.11	0.45	0	0	0	0
President Nicolau Lobato International Airport Hybrid PPP										
DB & CSC - ADB Loan						0	16.3	51.8	33.2	33.1
JICA Grant					0.36	0	10	15	8	5
DFAT Grant					0.51	0	8	9	3	0
AIFF-Australia Loan					5	0	8	10	15	10
Counterpart funding to ADB Loan (LACSP)					0	8.63	0	0	0	0
Counterpart funding to ADB Loan (Civil works runway, apron, control tower, taxiway etc.)						0	8	10	3.37	0
Counterpart funding to AIFFP						0	2	3	2.5	0
Parallel/Co-financing with JICA						0	2	3	4	1
FASA (IFC) FS & TSR						0.5	1.5	0	0	0
LACSP Phase I & II*						0	15	8	4.2	0
LACSP budget increase and apply \$40 pro-rata basis						2.2	0	0	0	0
VIP Terminal						0	2	3	1.1	
PMC						0.75	1.87	1.87	1.87	1.14
Electricity Sub-Station						0	2	2	0	0
Demolition						0	1	1	0	0
Others						1	0	0	0	0
SUB TOTAL	0	0	0	0.6	7.13	13.08	77.67	117.7	76.2	50.24
Transport PPP										
Restructuring and commercialisation of Dili Port (Dili Port PPP – FS, TSR, PT FASA and property acquisition).						0.1	0.5	0.25	0.25	0
Restructuring and commercialisation of Dili Port (Dili Port PPP – CAPEX)						1	0.5	46.8	0	0
SUB TOTAL	0	0	0	0	0	1.1	1	47.05	0.25	0

New Initiatives										
Estudo preparativus (Pre-FS)							0.3	0.4	0.5	0.5
SUB TOTAL	0	0	0				0.3	0.4	0.5	0.5

Source: DNPPP, Ministry of Finance, July 2022. DNPPP= Directorate National for Public Private Partnership, 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.

Table 24: 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 Airport 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- Car Park 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

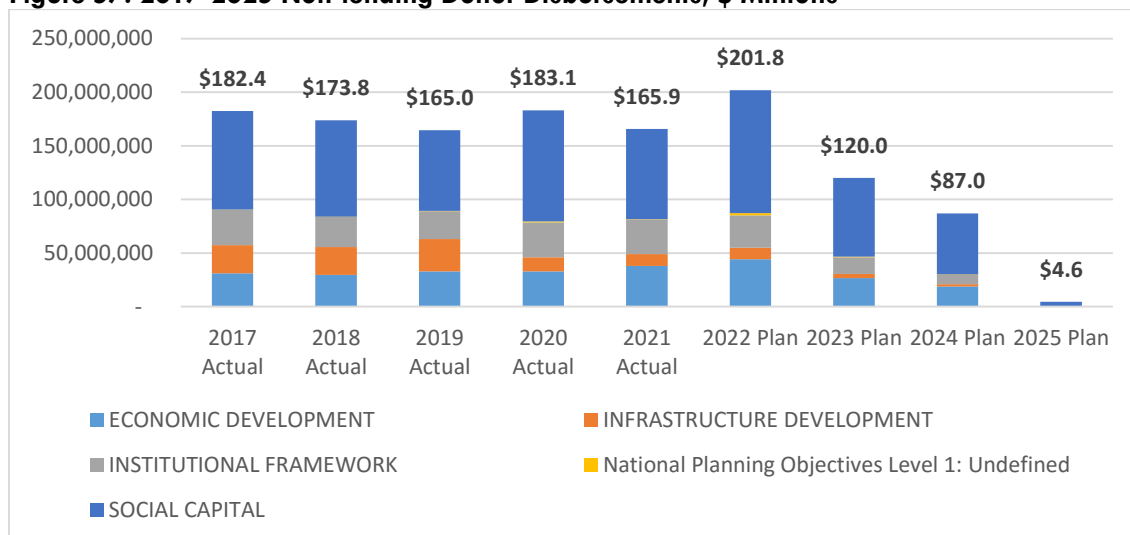
Source: PPPU, Ministry of Finance, July 2020. PPPU = Public Private Partnership Unit, PMU TBP = Project Management Unit Tibar Bay Port, *PT FASA = Post Transaction Financial Advisory and Service Agreement; IE = Independent Engineer; FS FASA = Feasibility Study FASA; IM=Independent Monitoring; TSR = Transaction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

9 Development Partners

9.1 Non-lending Forecasts

The graph below shows that there has been a steady decline in donor disbursements from 2017 until the arrival of 2020. The uptick in figures is likely stemming from urgent support that was provided throughout the Covid-19 pandemic. On average, Social Capital represents the highest concentration area of donor support, totalling 51.1% 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 57: 2017-2025 Non-lending Donor Disbursements, \$ Millions



Source: Aid Transparency Portal, report generated on July 20, 2022.

Table 25: Planned Disbursements by Donors group for 2023

Donor Group	2023 Planned
Australia	\$35,623,574
United Nations	\$18,074,948
Portugal	\$17,602,358
Japan	\$8,901,092
EU	\$7,173,487
USA	\$6,576,302
World Bank	\$5,853,710
Green Climate Fund	\$5,618,000
New Zealand	\$4,456,351
Korea	\$3,524,901
The Global Fund to Fight AIDS, Tuberculosis and Malaria	\$ 3,009,131
Global Environmental Facility	\$1,825,478
Asian Development Bank	\$1,750,000
TOTAL	\$119,989,949

Source: Aid Transparency Portal, Ministry of Finance, 20 July 2022.

Table 26: Planned Disbursements by SDP Sub-pillar and Pillar for 2023,

SDP	SDP Sub-pillar	2023 Planned
Social Capital	Education and Training	\$31,880,270
	Health	\$27,143,585
	Social Inclusion	\$6,652,009
	Environment	\$2,599,342
	Undefined	\$156,720
Subtotal		\$73,347,760
Economic Development	Agriculture	\$12,608,759
	Rural Development	\$11,249,905
	Tourism	\$2,691,447
Subtotal		\$26,550,112
Institutional Framework	Public Sector Management and Good Governance	\$9,411,280
	Undefined	\$3,886,361
	Security	\$1,408,866
	Justice	\$611,750
	Foreign Affairs	\$267,235
Subtotal		\$15,585,491
Infrastructure Development	Water and Sanitation	\$1,887,874
	Roads and Bridges	\$1,426,476
	Sea Ports	\$556,533
	Electricity	\$125,000
Subtotal		\$3,995,883
SDP Undefined		\$510,087
TOTAL		\$119,989,332

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

Table 27: Top 10 Projects 2023, \$ Millions

Project Title	Development Partner	SDP Sub-pillars	2022 Total in USD Millions
5530-Escola Portuguesa Ruy Cinatti – Centro de Ensino e Língua Portuguesa	Portugal	Education	\$11.0
Australia - Timor-Leste Partnership for Human Development - Health Sector	Australia	Health	\$8.4
Australian NGO Cooperation Program (ANCP)	Australia	Agriculture Education and Training Health Justice Public Sector Management and Good Governance Social Inclusion Water and Sanitation	\$7.7
Safeguarding rural communities and their physical assets from climate induced disasters in Timor-Leste. 107294	UNDP with Green Climate Funding	Rural Development	\$5.7
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	\$5.1

Project Title	Development Partner	SDP Sub-pillars	2022 Total in USD Millions
Governance for Development/ Prosiyu	Australia	Public Sector Management and Good Governance	\$4.9
Timor-Leste: Sustainable Agriculture Productivity Improvement Project (SAPIP) - P155541 - TFOA2869 & TFOA0236	World Bank	Agriculture	\$4.2
Strategic Priority 1: 2020-21 TLS ACTIVITY WORKPLAN SP-1 Universal Health Coverage (UHC)	WHO	Health	\$3.1
Australia - Timor-Leste Partnership for Human Development - Education Sector	Australia	Education	\$3.0

Source: Aid Transparency Portal, Ministry of Finance, 20 July 2022.

9.2 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. The European Union's Direct Budget Support programs for Nutrition and Decentralization are scheduled to continue in 2023.

The DNGEMAE continues to strive to improve development partner and Government coordination. As such, this year, the DNGEMAE has begun a new series of bi-monthly technical meetings to better harmonize development partner support and encourage improved coordination.

9.3 Direct Budget Support

Timor-Leste has previously received direct budget support from the European Union, Government of Australia and the International Labour Organization (one-off support in 2020). DBS is considered as a financing for 2023 State Budget because it uses Government systems (the money is in a Treasury sub-account) and on-budget, where the money is used directly by the beneficiary ministries. In this context, the funds are directly given to the country's government without prior earmarking.

European Union

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 for a period of 5 years. The agreement had been implemented since 2017 until 2021, with its main objective is to improve public service delivery through better planning, management, auditing, monitoring, accountability and oversight of public finance utilization.

EU DBS 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). The total amount of DBS that the EU committed for 2022 General State Budget last year was \$8.96 million. Of this, \$2,240,000 allocated to Ministry of Health, \$2,800,000 for Ministry of State Administration and \$3,920,000 to the Ministry of Finance.

However, the disbursement of the budget support is subject to the fulfilment of certain conditions assessed by independent evaluators that are contracted by the EU. The disbursement for a variable tranche, for example, depends on the attainment of 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.

For Budget 2023 EU DBS will be as following: \$1.1m for Decentralization programme for Ministry of Health and \$2.2m for Nutrition programme with the Minister of Health.

Government of Australia

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 Jersaun 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 Jersaun Foun investment will concentrate on directly funding cash transfers as well as supporting the operational costs of the programme delivery. PNDS received \$3.3m in 2022 while Bolsa Da Mae Jersaun Foun received \$3.3m in 2022. \$1.6m is related to Bolsa da Mae as of July but is subject to change.

The total amount of DBS commitments (EU and Australia) for State Budget 2023 as of July stands at \$4.9m but will be finalized prior to finalising the budget.