

EXECUTIVE SUMMARY

The District of Oecusse, is an enclave of the Democratic Republic of Timor-Leste and was the landing place of the Portuguese almost 500 years ago. With an area of 814 km², it is divided into four Sub-Districts (Pante Macassar; Oesilo; Nitibe; and Passabe) and 18 villages, with a total population of 65,524. However, current estimates place the population at 70,350 and projections indicate that by 2025, the population will likely double. Subsistence farming, small-scale fishing and cattle trade characterise the Oecusse economy and labor is predominantly occupied in growing food crops, mainly for self-consumption. Despite the reliance on agriculture, Oecusse suffers from high levels of food insecurity while the Living Standards Survey of 2007 placed it at the bottom in terms of access to sanitation and among the lowest ranked districts in terms of access to electricity and drinking water. Owing to its geographical, historical and socio-economic conditions, the Constitution of Timor-Leste accords special status to Oecusse, stating that it shall be '*governed by a special administrative policy and economic regime*' (Article 71, Clause 2).

On 16th June 2013, a resolution was passed by the Government of the Republic of Timor-Leste through the Council of Ministers that Dr. Mari Alkatiri, the first elected Prime Minister of Timor-Leste, would lead the planning and investment program of the Special Zones of Social Markets Economy (ZEESM) in Timor-Leste, to be initiated first in Oecusse. Consequent to the resolution, work was initiated to develop a Master Plan for ZEESM in Oecusse, with the assistance of the Lusitania Foundation for University and Entrepreneurial Development (FLD), a Portuguese non-profit organisation. Promulgation of a Decree Law to provide legal cover for the establishment of a Special Economic Zone is on the anvil, while a draft law is under consideration in Parliament for according Oecusse a special administrative and economic governance regime in accordance with Constitutional provisions in this respect.

The Oecusse ZEESM initiative is embedded in the Timor-Leste Strategic Development Plan 2011-2030 and the Program of the Fifth Constitutional Government 2012-2017, both of which underline the importance of special economic zones as a policy instrument to spur sustainable economic growth, create jobs and enable social development. The vision of the Oecusse ZEESM however, represents a departure from the usual special economic zone models, in that it proposes an integrated approach to sustainable, social and economic development.

As per the Master Plan for the Oecusse ZEESM, the designated area for the special economic zone will cover 107 hectares in the village of Costa in Sub-district Pante Macassar. This designated zone would require an estimated US\$ 4.11 billion of investment over a 20 year period, of which 67% or approximately US\$ 2.75 billion will be private sector investment and the remaining 33% or US\$ 1.36 billion will be contributed by the public sector.

In order to gain a deeper understanding of the key issues facing the establishment of ZEESM, this situation analysis was undertaken by a 15-member team of experts. The analysis sought to (i) understand and analyse facts and conditions on the ground in key economic and social sectors relevant to the establishment and sustainability of ZEESM; (ii) review the impact of various initiatives, programs and projects; (iii) identify developmental challenges in Oecusse District and in particular, to give voice to community issues, concerns and aspirations; and (iv) propose a strategic framework for next steps. The analysis was structured around five sectors: land and property; institutions; economic development; social capital; and infrastructure. A mix of primary and secondary sources was used to gather and analyse information and extensive consultations were held with communities, representative groups and public servants at central and local levels.

Key Findings

The key findings that emerge from the situation analysis are:

Sector	Key Findings
<i>Land and Property</i>	1. Ownership/Possession of land in ZEESM area is varied and State land is negligible
	2. Land parcels in Pante Macassar are largely undisputed
	3. Most land claims are settled
	4. Communities are willing to allow use of their lands but have clear and specific expectations from Government
	5. Property valuation, leasing process do not appear to be rule-based and transparent
<i>Infrastructure</i>	1. The condition of roads is generally poor but plans are underway to improve certain segments
	2. Bridges are in a dilapidated condition
	3. Water Supply and Sanitation services and regulation need urgent attention
	4. Energy needs are largely unmet and supply is erratic
	5. The air and maritime port need complete overhaul
	6. Several telecom companies have established their presence
	7. Irrigation system suffers from underinvestment
	8. Natural resources for construction purposes are in adequate supply
<i>Economic Development</i>	1. Food inflation is hurting the poor
	2. Banking services exist but cater to a small segment of population
	3. District Revenues are low and have a narrow base
	4. National development programs are targeting infrastructure development but implementation is slow
	5. Access to capital and poor human resources are stalling growth of small scale commerce and industry
	6. Micro-enterprises are growing
	7. The Cooperatives Sector is small but facilitates entrepreneurs
	8. Agriculture needs immediate, substantial Government support
	9. Livestock has not received due attention and thus has witnessed a progressive decline
	10. Illegal cattle trade abounds
	11. Livestock needs better support systems and market-orientation
	12. Forest coverage is declining alarmingly
	13. Food industry has considerable potential
	14. Fisheries remain an underdeveloped resource
	15. Oecusse could be the next big tourism destination but it needs heavy upfront investments
<i>Social Capital</i>	1. Health services are minimal and of low quality
	2. Health problems are acute for children and women and linked to social and customary practices
	3. Education sector is characterised by poor quality of learning and infrastructure
	4. Unemployment is very high
	5. Vocational training facilities are scarce
	6. Environmental risks are not receiving due attention and thus pose several economic risks
	7. Social inclusion is promoted through various mechanisms, but gender inclusiveness remains a challenge
<i>Institutions</i>	1. Weaknesses in institutional capacity are potential risks for ZEESM
	2. Rule of Law, transparency and accountability not well established
	3. Intra-governmental coordination is a vital aspect of good governance, but not always evident
	4. Public institutions in Oecusse suffer from common problems, such as under staffing, poor logistic arrangements, inadequate capacity

Recommendations

Based on the findings of the situation analysis, two sets of recommendations have been framed: those which are of a strategic nature relating to the development of policy, institutional, legal and incentives frameworks for the Oecusse ZEESM and the Oecusse Regional Administration which would be established under a special law; and those which aim to strengthen public services, improve governance and enhance investments in social capital. The latter are presented for consideration of the line ministries for the immediate short term and will form part of the agenda for which the Oecusse Regional Administration will assume responsibility upon being established.

For the strategic recommendations, we adopt a **5R Framework** covering **Roles-Rules-Resources-Risks-Results**.

THE 5R STRATEGIC FRAMEWORK: ROLES-RULES-RESOURCES-RISKS-RESULTS RECOMMENDATIONS FOR THE OECUSSE ZEESM	
ROLES	
Achieve clarity on the nature and extent of autonomy proposed for Oecusse to ensure that the governance models of the regional administration and ZEESM are in sync. As part of this, develop policy options for decentralised governance within Oecusse	
Develop the Oecusse ZEESM governance model to identify institutional arrangements for development, management, financing and regulation of the zone	
Develop a proposal to Establish a Citizens' Advisory & Information Centre to serve as a means of providing information, advice and guidance to citizens on a range of issues	
RULES	
Develop a Special Economic Zone Policy for Oecusse to identify principles, vision, approaches and goals	
Develop an incentives framework after a comparator analysis	
Develop a Land Policy and a Land Acquisition Law for Oecusse to provide for land registration, titles, valuation and dispute resolution	
Carry out a comprehensive review of the business environment to identify major institutional, legal, fiscal and economic barriers to investment, trade and growth	
Develop a policy note on <i>Shared Value in Oecusse ZEESM</i> to lay down a framework for corporate responsibility; propose mechanisms for turning citizens into shareholders; and identify how environmental benefits could accrue to the public	
Develop social safeguards standards and an environmental protection policy to ensure infrastructure development does not come at the cost of loss of biodiversity, environmental degradation and rights of citizens	
RESOURCES	
Develop a strategy for creating a sustainable funding model for the Oecusse ZEESM	
Develop a proposal for establishing an Oecusse Talent Management Agency to build skills, provide training and serve as a job centre and placement agency and	
Develop a proposal for establishing a <i>Social Development Fund</i> for investments in health, education and social protection; an <i>Innovation Fund</i> to support innovations in policy and delivery; a <i>Social Enterprise and Economic Development (SEED) Fund</i> to act as a Venture Capital vehicle; and a <i>Change Management Fund</i> that includes a Technical Advisory Services and Knowledge (TASK) Facility allowing for responsiveness to immediate implementation, technical evaluation and procurement, environment and social safeguard issues.	
RISKS	
Carry out regular risk analysis and review effectiveness of mitigation strategies	
RESULTS	
Develop a strong business case for the Oecusse ZEESM setting clear goals, benchmarks and oversight mechanisms	
Develop a marketing strategy based on the business case	
Develop a communication and advocacy strategy to enable continuous engagement with various stakeholders, presenting coherent, targeted messages to different audiences and build confidence and trust through openness and communication	
Create an inter-Ministerial and stakeholder coordination group—the Change Ambassadors that will serve to develop a shared understanding of key issues, risks and opportunities and allow for joint action	

Phasing

There are five clusters of distinct, yet inter-related activities for which a phased action plan is required:

Cluster	Nature	Number of Phases	Period	
Cluster 1	Infrastructure Development under the Master Plan for the Oecusse ZEESM	3	Phase I	2014 to 2019
			Phase II	2020 to 2021
			Phase III	2022-2025
Cluster 2	Institutional, Policy, Legal, Fiscal and Social Development Frameworks under the Oecusse Regional Administration	3	Phase I	2014 to 2015
			Phase II	2016 to 2017
			Phase III	2018 to 2019
Cluster 3	Development and Operationalisation of the Oecusse ZEESM governance model	3	Phase I	2014 to 2015
			Phase II	2016 to 2017
			Phase III	2018 to 2019
Cluster 4	Short to Medium Term Investments in Social Capital and Governance	3	Phase I	2014 to 2015
			Phase II	2016 to 2017
			Phase III	2018 to 2019
Cluster 5	The 500 Year Celebrations and Related Investments in Infrastructure and Services	1	Phase I	2014 to 2015

The phased action plan presented in this report attempts to bring all these clusters together. The approach followed is that from 2014-2019, the focus is on institutional aspects, both for the regional administration and for the economic and social market zone. Parallel to this institution building, immediate gaps in social sectors would be addressed, and the process of implementation of the Master Plan for the Oecusse ZEESM initiated. The aim would be that by the end of 2019, most of the key institutional, policy, legal, economic and fiscal issues would be addressed, paving the way for the completion of the physical infrastructure development of the Zone as well as its promotion and operationalisation.

The phased action plan indicates difficulty levels associated with each action, as well as their likely resource impact.

Activities under Cluster 4 are ones whose responsibility will be gradually assumed by the Oecusse Regional Administration, once it is established, while activities under Cluster 5 are not strategically linked to the other clusters, but their outputs (highway, airstrip, hospital, hotel etc.) would serve as useful initial investments for the broader Master Plan implementation.

Risks

The situation analysis identifies a large number of risks, ranging from the political, to the economic, institutional, social and fiscal. Some of the key risks are highlighted below, but a detailed risk analysis, is included in the Phased Action Plan in this report.

#	Description	Type	Impact and Probability	Mitigation Strategy
1	Political commitment for a special governance regime in Oecusse in line with Constitutional provisions, wanes due to dissent within government	Political	Impact: The entire project is dependent on a special governance regime for the region in line with the Constitutional provisions. Any change in the current political environment which is inclusive and positive, would greatly reduce the scope of the project. Probability: 1	Deep political engagement is required to ensure political agreement on this key issue
2	A special governance regime is conceived under legislation passed by Parliament, but does not devolve political power	Political	Impact: Any form of autonomy sans devolution of political power would effectively place the Oecusse Regional Administration under central government control. Probability: 4	The opposition party enters into political negotiation with the government, resulting in political devolution to be enshrined in the law on special governance regime. This would allow it to frame policies and strategies without having to seek central government approval.
3	There is lack of clarity in roles and responsibilities of central government and the Oecusse Regional Administration	Institutional	Impact: Unclear mandates will cause institutional overlaps, weak decision making and delays in implementation, leakages and opportunities for rent seeking. Probability: 3	Through political and technical dialogue, ensure that the special governance regime is unencumbered and key powers are transferred to the regional administration, including for financial and human resource management, and inter governmental coordination.
4	Institutional capacities for delivering public services are not built up	Institutional	Impact: Mismatch between institutional capacities for service delivery, planning, budgeting, regulation and human resource management and public expectations for efficient services could lead to public dissatisfaction and foment social unrest. Probability: 4	Develop an institutional capacity building plan that adopts innovative models of delivery and are focused on building systemic capacity at various levels.
5	A global or economic downturn occurs	Economic	Impact: A global recession or a marked slowing down of growth in key markets such as China, India and the US, would greatly impact the feasibility of the ZEESM initiative. Probability: 3	
6	Fiscal powers are either not granted to the Oecusse Regional Administration or are heavily circumscribed.	Fiscal	Impact: The inability to impose taxes and retain revenues from it would make the administration fiscally unsustainable and make it reliant on central transfers from the central government, effectively constricting its decision making powers. Probability: 3	The Oecusse ZEESM office enters into political and technical dialogues with the central government to ensure fiscal decentralisation.
7	The governance model developed is non-inclusive and land issues are not adequately addressed.	Social	Impact: Absence of a Land Policy and Land Acquisition Law will lead to arbitrary acquisition, unfair compensation, displacement and social unrest. Probability: 3	