**Sustainability of Timor-Leste’s State Finances**

**Presentation by Charles Scheiner**

**ANU Timor-Leste Update**

21 June 2018

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**What is La’o Hamutuk?**

- Timorese and international people "walking together" on the journey to create a new Nation.
- An independent, Timorese, non-governmental organization which does research, policy analysis, public education and advocacy.
- A force for participatory, equitable, sustainable and evidence-based policies and practices.

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**Imminent fiscal cliff?**

Or intrinsically unsustainable economy dependent on government spending of limited petroleum wealth.

**World Bank Fact Sheet: APEC Economic Update April 2013**

GDP growth is expected to have fallen sharply in 2017 to -1.8 percent, driven by a decline in public spending as the government has not been able to secure a legislative mandate. To resolve the ongoing political impasse, new elections will be held in May 2018 and, following the formation of a new government, public spending is expected to moderate upwards again later in 2018. The budget continues to consume more resources that can be sustainability drawn from the Petroleum Fund, with the risk of a damaging fiscal cliff in the medium-term when state resources are depleted.

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**I made this prediction in 2013. Oil prices and state spending have been lower than expected.**

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**Executed State Budgets 2002-2017**

**Budgeted & executed spending**

Expenditures (including auton. agencies)

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**Graphs by Léo Huard based on DIT, Ministry of Finance budget books and Transparency Portal. February 2018**
Executive Summary

The 2017 Budget still neglects farmers, students, and health care.

Allocation of the approved 2017 State Budget (US $1.387 million)

<table>
<thead>
<tr>
<th>Allocation</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Natural Resources</td>
<td>31%</td>
</tr>
<tr>
<td>Social safety</td>
<td>24%</td>
</tr>
<tr>
<td>Health</td>
<td>14%</td>
</tr>
<tr>
<td>Education</td>
<td>14%</td>
</tr>
<tr>
<td>Economic development</td>
<td>11%</td>
</tr>
<tr>
<td>Agriculture</td>
<td>10%</td>
</tr>
<tr>
<td>Development Capital</td>
<td>4%</td>
</tr>
<tr>
<td>Transfers</td>
<td>1%</td>
</tr>
<tr>
<td>Salaries &amp; Wages</td>
<td>1%</td>
</tr>
</tbody>
</table>

The money doesn’t match the promises.

- Appropriated spending in the 2017 State Budget: $1.387 billion
- The Government says its priorities are education, health, agriculture, and water. All together, they will get less than 1% of state expenditures.
- Recent budget execution

The treasury balance is the lowest in eight years, due to minority government.
80% of this is from countries with ASEAN FTAs

About 30% is paid by the govt to itself: $73.1 million
80% of this is from countries with ASEAN FTAs

About 20% is paid by public employees & contractors

Operational cost to generate: $62 million
Interest: $30.3 million

Income taxes: $43.2 million

Loans: $27.2 million
Interest: 13% will be repaid with interest
Only South Sudan, Libya (and Equatorial Guinea?) are more dependent on oil and gas exports than Timor-Leste was.

- State revenues in 2017: $2,217 million
- $1,612 million (73%) was from oil and gas revenues
- $422 million (19%) was from investing the Petroleum Fund ($1,295m unrealized)
- $183 million (8%) was from non-petroleum sources

- Executed 2017 State Budget: $1,289 million
- $1,079 million transferred from the Petroleum Fund
- $183 million from non-petroleum (domestic) revenues
- $27 million from loans which will have to be repaid ($102m planned)

- State activities, paid for with oil money, are nearly half of the "non-oil" economy because some of this money circulates in the local economy.

- Petroleum and investment "income" goes to the state, not the people.

Oil and gas income has been falling since 2012. Production is dropping faster than prices, and will not go back up. The price will be irrelevant when we have nothing left to sell.

Bayu-Undan quarterly production. Liquids are almost done; gas will continue for 1-2 years.

Financial Assets (Treasury + PF)
(Billion USD nominal – unchanged in four years)

Australia and Timor-Leste have agreed on a boundary and on Sunrise revenue split – but the gas pipeline is still unresolved.
Oil revenues still to come in

Already received
• $21.6bn from B-U, Kitan and EKKN
• $4.6bn from return on PF investments

Expected
• $1.9bn Bayu-Undan drops (90% under Timor Sea Treaty)
• $0.11bn Bayu-Undan drops (10% under boundary treaty)
• $0.7bn Buffalo second life

Eventually
• $8-20bn Greater Sunrise upstream (estimate)

Total about the same as what has already been received

Possible someday
• New offshore or onshore oil discoveries?
• Other minerals or extractives?

Possible revenues under new treaty

Expected annual revenue from different fields

<table>
<thead>
<tr>
<th>Field</th>
<th>Revenue (in $bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bayu &amp; Kitan</td>
<td>$20.171m</td>
</tr>
<tr>
<td>Buffalo</td>
<td>$664m</td>
</tr>
<tr>
<td>Sunrise downstream</td>
<td>$3,075m</td>
</tr>
<tr>
<td>Sunrise upstream</td>
<td>$15,371m</td>
</tr>
</tbody>
</table>

Our seas have been explored for half a century.
There may be no other fields.

Since 1910, oil companies have drilled 95 exploration wells here. They found eight commercially viable reserves. Kitan is the only one discovered in the last 20 years.

We’re spending down our birthright.

Historic and planned withdrawals from the Petroleum Fund

The Petroleum Fund peaked at $17.1 billion in mid-2015. At the end of March 2018, it was $16.8b.

We’ve moved from oil dependence to relying on our declining savings.

Balance in Timor-Leste’s Petroleum Fund

The balance is lower than it was 2½ years ago.
Rights and Sustainability - La'o Hamutuk

**TL will soon be a net oil importer**

<table>
<thead>
<tr>
<th>Year</th>
<th>Million US$/year (pretax)</th>
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<tbody>
<tr>
<td>2008</td>
<td>$2,500</td>
</tr>
<tr>
<td>2009</td>
<td>$2,000</td>
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<tr>
<td>2010</td>
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<td>2011</td>
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<td>2019</td>
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<tr>
<td>2020</td>
<td>$0</td>
</tr>
<tr>
<td>2021</td>
<td>$0</td>
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</tbody>
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*Graph by La'o Hamutuk, from official sources (June 2016).*

- Oil and gas revenue to TL: 2008-2010 from MoEVT, Petroleum Ministry (projections).
- Oil and gas import value and public expenditure through 2013: TIMOREST Trade Statistics.
- 2014-2021: explored by La'o Hamutuk based on U.S. AID assistance agency projections.

The Strategic Development Plan

- Issued July 2011, hopes to make TL an Upper Middle Income Country by 2030.
- A vision and dream, not a realistic plan.
- Focuses on physical infrastructure, not sustainable development.
- Will require loans and spending beyond TL’s means
- Promised reviews are not being done.

Tasi Mane petroleum infrastructure project

- In 2010, TL began the South Coast Petroleum Corridor.
- During 2011-2017, Timor-Leste spent $373 million on it.
- The 2017 budget anticipates $1.62 billion more in 2018-2021, but leaves out the most costly items.
- Total project costs could be $15 billion (more if Timor-Leste pays for the refinery, pipeline or LNG plant). No investors are interested.

The largest contract in TL history was signed in 2015: $719 million to build the Suai Supply Base.

A court rejected it in 2015 but was reversed in 2017. It’s not clear if the company is still interested.

Problems with the Tasi Mane project

- It makes TL more dependent on the oil and gas sector.
- Dubious concepts and planning; it is unlikely to provide a reasonable return on investment.
- It neglects sustainable development (agriculture, tourism, small industries etc.), exemplifying the obsession with oil.
- Nearly all the billions spent will go to foreign companies, providing hardly any local jobs or subcontracts.
- It will create social conflict, take up land, displace people, worsen health and degrade and endanger the environment.
- Cost projections leave out most expenditures, including nearly all of the highway, LNG plant and refinery.
- What if Sunrise gas doesn’t come to Timor-Leste?

The Government has made many unrealistic promises to local communities about profit-sharing, jobs and other benefits.

The Tasi Mane Project includes the Suai supply base, Betano refinery, Beauch LNG plant, 156-km highway, onshore and offshore pipelines, 2 airports and 2 seaports.

Special Market Zone in Oecusse

- In 2014-17, RDTL spent $544 million on ZEESM with no accountability. Oecusse has 6% of Timor-Leste’s population.
- What are Oecusse’s competitive advantages?
- Can ZEESM justify a $4 billion investment?

Who benefits: residents of Oecusse or Fretilin leadership?
Overbuilding ports and airports

- Oecusse and Suai have new, virtually unused, "international" airports.
- Timor-Leste hopes to expand Tibar port and Dili airport far beyond realistic traffic projections.
- How will the country pay for a $6 billion annual trade deficit after the oil is gone?

Timor-Leste is going deeper into debt.

- Laws in 2009 opened the door to foreign loans.
- In 2012, Timor-Leste signed contracts to borrow $107 million from Japan and from the ADB.
- In 2013, TL signed for $90m more from ADB and World Bank.
- In 2015, TL signed for $12m more from ADB.
- In December 2015, TL borrowed $50m from China's Ex-Im bank. (pending court approval)

In March 2016, TL signed for another $76m from the ADB.
- In December 2016, TL signed for $50m more from the ADB.
- In June 2017, TL signed for $35m more from the World Bank.

Loans will have to be paid back.

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Important to consider

- Implementing the SDP will require billions of dollars in loans, probably at commercial rates.
- Even at concessional rates, repaying a loan will permanently reduce money in the Petroleum Fund.
- TL's oil and gas reserves are limited, non-renewable, and 98% depleted already.
- TL will have to prioritize repaying loans above spending on people's needs or developing other sectors.
- Our children and grandchildren will inherit the debt after the oil wells have run dry.

If current plans continue, TL may be unable to finance its budget in a decade. The Boundary Treaty and Sunrise help a little, but not enough.

Scenarios from outgoing Finance Minister

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What is to be done?

- Forego spending on expensive, dangerous white elephant projects.
- Invest in people – the country’s most valuable resource – by improving education, nutrition and health care.
- Diversify the economy, focusing on productive sectors which replace imports.
- Stop imagining that new resource extraction will bring in more easy money.
- Plan and budget for reality, not fantasies.

Thank you.

You can find more and updated information, including this presentation at

- La'o Hamutuk’s website [http://www.laohamutuk.org](http://www.laohamutuk.org)
- La'o Hamutuk’s blog [http://laohamutuk.blogspot.com/](http://laohamutuk.blogspot.com/)

Timor-Leste Institute for Development Monitoring and Analysis
Rua D. Alberto Ricardo, Bebora, Dili, Timor-Leste
Mailing address: P.O. Box 340, Dili, Timor-Leste
Telephone: +670 7723 4330 (mobile) +670 3321040 (landline)
Email: info@laohamutuk.org

The graph shows legal goods trade only. Three-fourths of donor spending and two-thirds of state spending leaves the country.
In 2015-16, more money went out than came in.

<table>
<thead>
<tr>
<th>2016 trade</th>
<th>services</th>
<th>non-oil goods</th>
<th>total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Imports</td>
<td>$603m</td>
<td>$559m (99% coffee)</td>
<td>$1,162m</td>
</tr>
<tr>
<td>Exports</td>
<td>$77m</td>
<td>$9m</td>
<td>$97m</td>
</tr>
<tr>
<td>Deficit</td>
<td>-$526m</td>
<td>-$539m</td>
<td>-$1,063m</td>
</tr>
</tbody>
</table>

Timor-Leste’s External Balance of Payments

Many children have become youth.

Dili is very different from the districts.

60% of Dili’s population are among the wealthiest 20% of Timorese, while only 7% are below the poverty line.

More than half of families outside Dili live in poverty.

What do 672,000 Timorese people aged 15-64 do for work?

Oil GDP fell 85% between 2012 and 2016, and will continue to fall.

The non-oil, non-state GDP per capita is stagnant.

Timor-Leste is struggling to find jobs for around 20,000 people who enter the work force every year.

In 2016, total private sector employment was $8,200, 7% lower than it had been in 2014.
Businesses don’t invest in themselves.

How businesses spent the money they received in 2016

- Profits taken out
- Reinvested
- Other expenses
- Purchases of finished goods
- Buy supplies & materials
- Labor costs

Graph by La'o Hamutuk based on OEC Business Activities Survey, 2016

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