The 'Resource Curse' in Timor-Leste

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Timor-Leste is one of the world's most petroleum-export-dependent countries. Although petroleum revenues and savings benefit many citizens, they also distort economics, public finances, politics and personal behaviour. The phrase 'resource curse' is often used to describe how people in nearly every nation which depends on exporting non-renewable resources become worse off than people not 'blessed' with mineral and oil wealth. This *In Brief* describes how the 'resource curse' will lead to devastating consequences in Timor-Leste unless the state moves quickly to diversify and strengthen the non-oil economy. It is based on analysis by La'o Hamutuk, a civil society organisation which has researched policies and outcomes in Timor-Leste since 2000.[1]

Oil Swamps the Economy

Timor-Leste's oil and gas reserves are limited, and its petroleum dependency results from its very small non-petroleum economy. Timor-Leste's gross domestic product (GDP) was US$4.5 billion in 2011, of which 77 per cent (%) was from the petroleum sector, with most of the remainder driven by state spending. Although political leaders proclaim that 'non-oil GDP' has grown at 'double-digit rates', this obscures the fact that productive sectors — agriculture and manufacturing — comprise only 4% of GDP and have not increased significantly since 2002. All the growth in 'non-oil GDP' comes from the state spending oil money: public administration, infrastructure construction, and supplying goods and services to the government.

Timor-Leste's oil wealth is leaking out rapidly. In 2013, Timor-Leste spent US$535 million on imported goods, while non-oil exports totalled only US$16 million, nearly all coffee. Similarly, US$627 million was paid for overseas services in 2013, while most of the US$45 million in service 'exports' was for tickets on international airlines. Many consumer products which could be produced in Timor-Leste are imported, including chickens from Brazil, rice from Vietnam, eggs from Singapore, water from Indonesia, and fruit juice from Cyprus and Holland.

Exacerbating petroleum dependency, the developed formal economy employs less than one-third of the working-age population: 9% work for companies (half of which depend on state contracts); 10% work for the state directly and 8% work for themselves (as taxi drivers, or market, street or kiosk vendors, for example); 36% are subsistence farmers or fisher-people; another 34% are not working; and 3% are students, overseas, or working for agencies. When the oil is gone, jobs and imports will disappear, and productive private sectors will have to fill the gaps in livelihoods and necessities.

Oil Fuels the State Machinery

Money from converting Timor-Leste's oil and gas wealth into dollars sustains the state. During 2014, the Ministry of Finance projects that 61% of state revenues will come from oil and gas exports. Another 32% will be from investing past petroleum income, with only 7% from non-oil sources. Timor-Leste's business taxes are very low, because little importance is given to non-oil revenues.

Oil revenues peaked in 2012. After five years of rapid budget escalation, spending moderated in 2013 due to infrastructure delays, but will resurge if political leaders carry out their plans. Recurrent expenditures (salaries, goods, services, public grants) grew about 20% per year between 2008 and 2014. Although health and education are gradually getting more, Timor-Leste still invests 40% less on them than well-managed developing countries. Timor-Leste's post-1999 'baby boom' are not getting adequate nutrition or education, which will have long-lasting consequences. Agriculture receives only US$34 million (2% of state spending), while veterans get US$87 million in pensions and more in preferential contracts and scholarships.

Timor-Leste created its Petroleum Fund in 2005 to serve as a buffer between fluctuating oil income and the annual state budget. All petroleum revenues go into the fund, and money is withdrawn to fill the budget deficit. Returns from the fund's investments were intended to replace oil revenues after the fields run dry. Guidelines for annual withdrawal were meant to provide a constant revenue flow indefinitely, but they have been exceeded almost every year.

The Resource Curse Has Many Faces

Timor-Leste has prevented some impacts of the resource curse. By using an international currency, it has moderated inflation and partially hedged against currency exchange fluctuations. Despite this, inflation continues because there are more dollars than goods. Oil operations bring other problems, including the amorality of international oil companies, environmental destruction, and their capital-intensive, high-skill nature. Timor-Leste's size, poverty, and recent emergence from occupation and war exacerbate the damage.

These factors, combined with human behaviour, make it almost impossible to develop a sustainable, equitable economy. In all democracies, politicians seek results before the next election, and oil income allows leaders to replace long-term planning with dreams and promises. Megaprojects like Tasi Mane and the Oecusse Special Economic Zone ignore economic viability while exaggerating job and spin-off prospects. In search of quick results, policymakers neglect poverty reduction, import substitution and food sovereignty.

With US$16 billion in the Petroleum Fund, decision-makers see money as the universal solution — purchasing short-term substitutes for a few is easier than creating durable results for everyone. For instance, the state spends 35% more on overseas scholarships than on its national university, which has four times as many students. While some well-connected citizens fly to overseas hospitals at public expense, most people cannot access decent health care. While roads and bridges for VIP visitors to Dili are frequently rebuilt, rural infrastructure is missing or neglected. Airports, highways and ports will consume over a billion dollars, yet very few Timorese people fly or own cars. When the oil is gone, Timor-Leste will be unable to cover the eight-fold increase in trade deficit predicted by port planners, or to repay lenders.

In addition, special interest groups — veterans, contractors, people displaced by the 2006 unrest, former office holders, soldiers who deserted, political party leaders — claim privileged entitlement to public funds. Since there are few taxpayer voters to demand that their money be used prudently or honestly, money is often diverted, misdirected or wasted.

Petroleum usurps attention and resources from sustainable, realisable plans. Oil attracts the most persuasive, creative and ambitious people, leading to a brain drain from more productive or service-oriented professions. The talented oil advocates persuade decision-makers to pay for flashy concept studies, leading to billion-dollar proposals. When they compete against ideas for farming, schools, clinics, tourism, food processing or light industry, the playing field is tilted.

Few leaders anywhere have the foresight and courage to overcome such challenges.

The Future is Predictable

Development of Greater Sunrise oil and gas is stalled due to disputes with Australia over maritime boundaries and with the oil companies, who want to liquefy the natural gas at sea, rather than pipe it to Timor-Leste. Even if this project proceeds with an LNG plant in Timor-Leste, total oil and gas revenues will average US$1 per person per day for four decades, about one-third of the 2014 budget.

With half of Greater Sunrise, Timor-Leste has about 800 barrels per citizen in known oil and gas reserves, 30% less than Australia. This will last 14 years at 2012 production rates. Although petroleum officials promise that large fields await discovery, the country's constrained area, geology and 120 years of exploration make this unlikely.

By modelling current trends, external factors and policy choices, one can anticipate future outcomes. A 'best-guess' scenario, too optimistic for prudent planning, shows that spending will exceed revenue in 2019, and the Petroleum Fund will start to shrink (Scheiner in press). It will be empty by 2026, before today's toddlers finish secondary school, and state spending will have to be cut by two-thirds. If the non-oil economy hasn't developed by then, many more will join the swelling majority who live below the poverty line.

This can only be avoided by rapidly moving toward sustainable, equitable development: increasing food production, cutting wasteful spending and cancelling unviable megaprojects. Timor-Leste must fortify its strongest resource — its people — by investing in education, nutrition and health care.

Timorese people proved their unity and persistence during the long struggle for political sovereignty, but economic sovereignty may be even harder to achieve.

Author Notes

Charles Scheiner is a researcher with La'o Hamutuk, the Timor-Leste Institute for Development Monitoring and Analysis. The article this In Brief *is adapted from,* <www.laohamutuk.org/econ/exor/14ExorcisePaper.htm>, *includes a reference list.*

Endnote

1 La'o Hamutuk's analysis uses data from the Timor-Leste government and international agencies.

Reference

Scheiner, C. in press. How Long Will the Petroleum Fund Carry Timor-Leste? Timor-Leste Studies Association. <www.laohamutuk.org/econ/model/13PFSustainability.htm>.

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