The Resource Curse in Timor-Leste

by Charles Scheiner
La'o Hamutuk

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Topics to discuss

2002: Newly independent - starting in a good place

2004-7: Established model petroleum regime and Petroleum Fund.
Oil and gas revenues begin to come in.

2008-14: Revenues and state spending grow rapidly.
Regulatory regime gets weaker.

2015-22: Oil revenues fall as fields are depleted.
The "non-oil" economy is shrinking; poverty persists.

Future: Dreams of more oil rents could be illusory.
Petroleum Fund has $18 billion, which might last 10 years

Observations and conclusions

Starting in 2002

- After 400+ years of Portuguese colonial rule and 24 years of Indonesian occupation and war, Timor-Leste's people wanted peace and prosperity for their new state.
- Indonesia had destroyed their economy and infrastructure, and they had no foreign debt, and no experience with self-government or democracy.
- Timor-Leste and its international advisors hoped that undeveloped offshore oil and gas fields would jump-start their state and economy.
- They were determined to avoid the "paradox of plenty", where people in extractive-dependent nations live with poverty, conflict, corruption, inequality and autocracy.

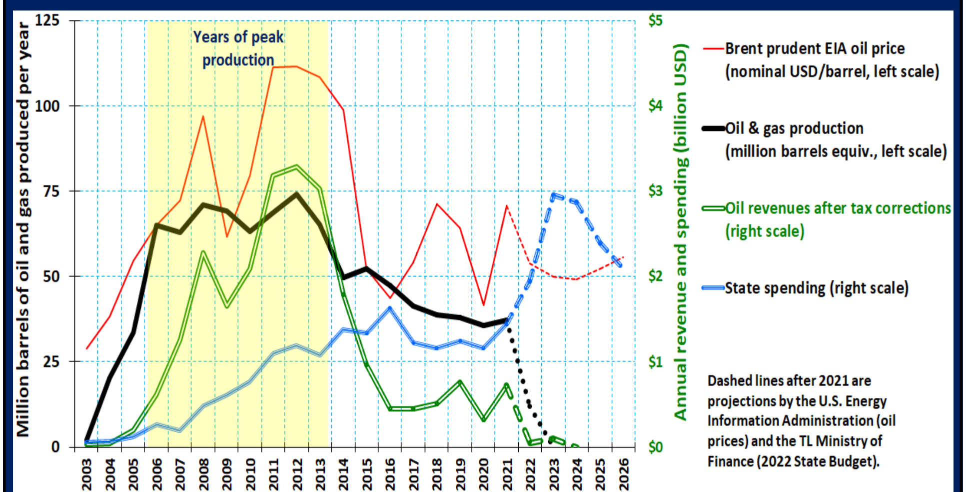
TL set up a model petroleum regime.

- Production-Sharing Contracts with oil and gas companies are standard, published, with no bonuses.
- All oil and gas revenues go into the Petroleum Fund, which is in tradable overseas investments, transparent, and independently managed. Investment returns are deposited into the PF.
- Money can be withdrawn only to finance the state budget, with Parliamentary approval and sustainable rules.

It worked well for a while.

- Oil production began in 2004 and gas in 2006, while global oil prices surged, and revenues were higher than expected – reaching $2 billion/year in 2008 and peaking at $3.3 billion in 2012 (three times non-oil GDP).
- Bidding rounds for new offshore areas in 2005-6 were open and transparent, and several companies conducted seismic exploration and drilled test wells.
- The balance in the Petroleum Fund rose to $12 billion by 2012.
- After civil unrest in 2006 and elections in 2007, the new government rapidly increased spending and adopted an ambitious, oil-fueled, development plan.

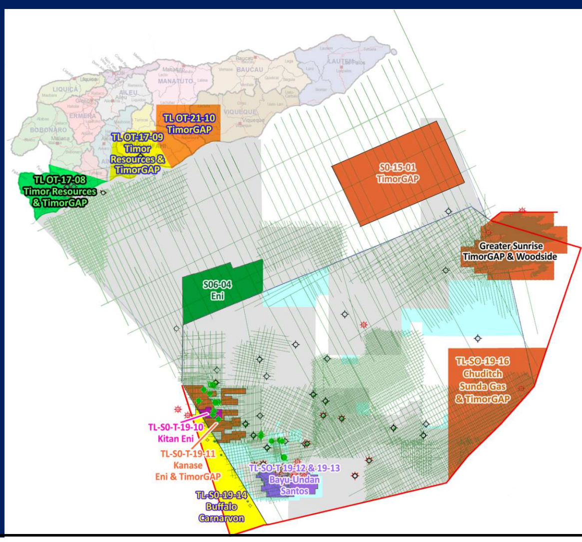
Oil prices and production, revenues and spending



Petroleum dependency dominates.

- PF withdrawals always exceeded sustainable levels. In 2010-2015, they were 154% of ESI, paying for 89% of state spending.
- High investment returns grew the PF, but more slowly. It reached $17 billion in 2015, where it stayed for four years.
- The PF law was amended in 2011 to enable higher withdrawals and riskier investments. By 2014, 40% was in the stock market.
- Economic disparity increased, with a growing middle class in Dili but unchanging widespread poverty among the rural majority.
- Nevertheless, peace and democracy prevails, corruption is relatively small, and people enjoy their human rights.

Past and present oil and gas exploration contracts

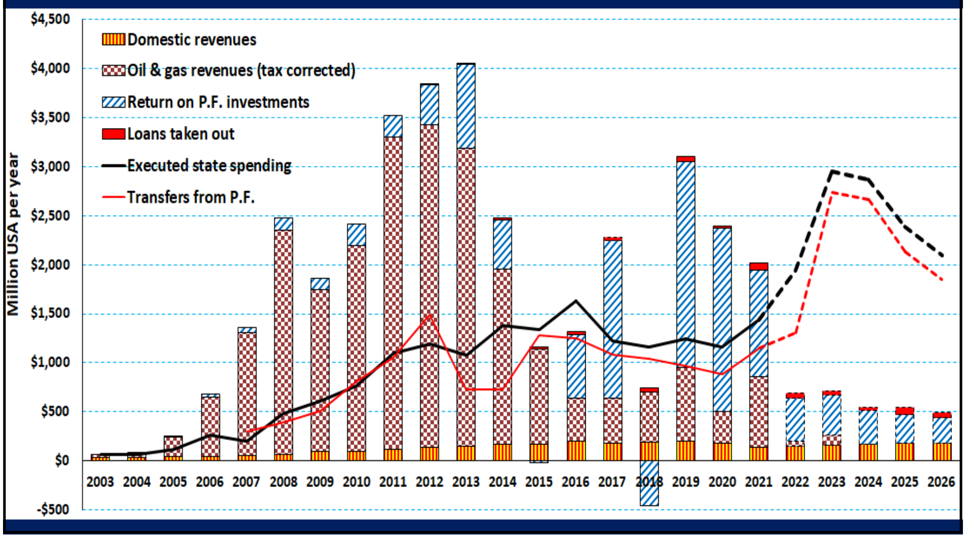


The petroleum regime decays.

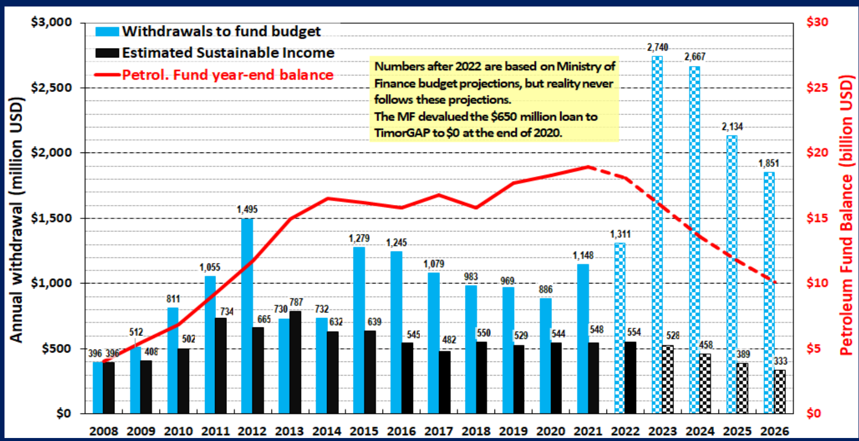
- After 2012, oil and gas production fell; revenues dropped rapidly. No commercially viable fields have been discovered since 2011.
- TL's Resource Governance Index dropped from 12th best in the world in 2010 to 43rd in 2017.
- Petroleum laws were amended again in 2018-19 to undercut sustainability, reduce oversight and weaken protections.
- ConocoPhillips, the oil company with the biggest stake in Timor-Leste, sold all their interests, as did Shell.
- Greater Sunrise, which many hoped would be developed after the 2019 Boundary Treaty with Australia, remains stuck.
- The PF loaned $650 million to TimorGAP to buy 57% of Sunrise. A year later, Sunrise was revalued to zero.

Income to the state

(including the Petroleum Fund)



Withdrawals from the Petroleum Fund



- Withdrawals from the PF are twice the sustainable level and finance more than 80% of state spending, which is going up since 2019.
- Although the Petroleum Fund balance rose to $19 billion in 2021, it is falling rapidly as stock prices drop and withdrawals increase.

The petroleum era is ending.

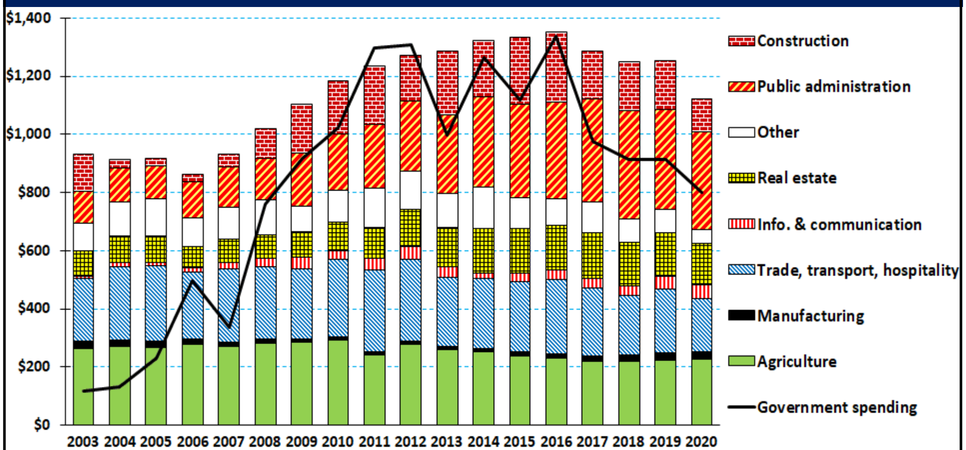
- Timor-Leste has received 99% of the money it will get from existing fields.
  Increased oil prices do not help because production is low.
- Sunrise may never be developed because no investors have come forward.
  Climate change concerns have curtailed new fossil fuel projects.
- Test wells at potential new fields have not found viable reserves, although exploration continues.
- If every new field meets its proponents' optimistic projections, they might bring in up to $1 billion in total.
  This could finance the state budget for six months.

But little exists to replace it.

- TL's trade deficit is around $1 billion every year, including many imports which could have been produced locally.
- Private sector employment has been dropping since 2014. The productive economy is smaller than at independence.
- Spending on education and health is below international norms. Child malnutrition is among the worst in the world.
- Timor-Leste's Human Development Index dropped from 128th in the world in 2010 to 141st in 2020.
- The Petroleum Fund pays for more than 80% of the budget. It could be used up within a decade.

Sectoral contributions to non-oil GDP per capita

Constant 2015 prices, production approach



The non-oil productive economy is smaller than it was at independence.

What's happening?

- It's easier to pay for something – an overseas scholarship or a foreign investment contractor – than it is to build a university or local business.
- Most local companies and workers seek petroleum rents (through public contracting), rather than developing the productive economy.
  It's more certain and more lucrative … for now.
- Prices on the petroleum and stock markets are volatile and uncontrollable.

Retrospective observations

- In a democracy with five-year terms of office, politicians have a short planning horizon.
- They prioritize visible benefits (physical infrastructure) over long-term investments (human resources).
- Legislated protections can easily be repealed.
- The petroleum industry is capital-intensive, employing hardly any Timorese workers or subcontractors.
- Non-renewable resources inevitably run out.

The independence struggle left scars.

- TL proved the 'experts' wrong by winning independence and by forcing Australia to accept a maritime boundary.
- Many international agencies sent incompetent 'experts', further devaluing the concept of expertise.
- Therefore, some Timorese believe they can accomplish anything, regardless of physical or commercial realities.
- National leaders excelled at clandestine resistance, a different skill set than is needed to govern in a peacetime democracy.
- Endemic PTSD and trauma undercut long-term planning.
- Nationalism often outweighs economic and technical concerns, leading to sub-optimal decisions.

Another world is possible.

- Although 2/3 of Timor-Leste's petroleum-funded period has passed, there is still time and money.
- If democracy and peace continue, the PF could support transformation to a more permanent, equitable economy.

The Petroleum Fund from 2005 thru February 2022:

$24.3 bn oil & gas revenues
+$ 8.0 bn investment returns
- $13.6 bn withdrawn
$18.7 bn remaining

- More than half of the population was born after the Indonesian occupation.
  They have had more educational opportunities and exposure to the world than their elders did.
- Sustainable, equitable development will require major changes in thinking and direction.

Thank you.

You can find more and updated information at

- **La'o Hamutuk's website**
  http://www.laohamutuk.org
- **La'o Hamutuk's blog**
  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: laohamutuk@gmail.com