

Document of
The World Bank

FOR OFFICIAL USE ONLY

Report No: 31924-TP

DEMOCRATIC REPUBLIC OF TIMOR-LESTE
JOINT STAFF ADVISORY NOTE
ON THE
POVERTY REDUCTION STRATEGY PAPER

(In Two Volumes) Volume 1

April 29, 2005

Poverty Reduction and Economic Management
East Asia and Pacific Region

This document has a restricted distribution and may be used by recipients only in the performance of their official duties. Its contents may not be otherwise disclosed without World Bank

FOR OFFICIAL USE ONLY

INTERNATIONAL MONETARY FUND AND
INTERNATIONAL DEVELOPMENT ASSOCIATION

DEMOCRATIC REPUBLIC OF TIMOR-LESTE

Joint Staff Advisory Note on the Poverty Reduction Strategy Paper

Prepared by the Staff of the International Development Association
and the International Monetary Fund

Approved by Jemal-ud-din Kassum (IDA) and,
Daniel Citrin and Carlo Cottarelli (IMF)

April 29, 2005

	Contents	Page
I.	OVERVIEW	1
II.	THE NATIONAL DEVELOPMENT PLAN	2
	A. NDP Design and Implementation	2
	B. Poverty and Growth Diagnosis Underlying the NDP	4
	C. Main Pillars of the Strategy.....	5
III.	IMPLEMENTATION CHALLENGES.....	6
	A. Encouraging Macro-Economic Stability and Growth through the Effective Use of Oil and Gas Wealth.....	6
	B. Building Institutional Capacity for Service Delivery and Providing Quality Basic Education	7
	C. Strengthening Governance, Especially the Justice Sector and Customs.....	9
	D. Supporting Job Creation by Improving the Investment Climate	10
IV.	CONCLUSIONS AND ISSUES FOR DISCUSSION	10

This document has a restricted distribution and may be used by recipients only in the performance of their official duties. Its contents may not be otherwise disclosed without World Bank authorization.

Overview

1. **The authorities are presenting the Democratic Republic of Timor-Leste's National Development Plan 2002 (NDP) and associated implementation documents to the Boards in order to indicate the progress achieved by the country during the past three years.** This Joint Staff Advisory Note (JSAN) has four sections: Section I provides an overview. Section II outlines key elements in NDP design and implementation. Section III identifies key challenges faced in NDP implementation and provides suggestions for both strengthening the strategy and addressing implementation risks. Section IV concludes and proposes issues for discussion by the Boards.

2. **In 1999, the citizens of Timor-Leste voted for independence in an UN-managed referendum.** The country was under UN administration until May 2002, when the first Government assumed power. It was during this period that the National Development Plan (NDP) was developed. Since then, the government has produced a Road Map and Stability Program for NDP implementation in 2003, and developed Sector Investment Plans (SIPs) to further guide this process in 2004.

3. **The NDP presents Timor-Leste's long-term development vision and its development strategy for the period 2002-2007, which coincides with the mandate of the country's first elected Government.** Preparation began in September 2001, under the direction of the Second Transitional Government. A program of nation-wide consultations was launched in early 2002, culminating in a series of national workshops. The NDP was approved by Parliament at Independence in May 2002 and the key messages were disseminated to all households and schools in a booklet entitled "East Timor 2020: Our Nation, Our Future." The NDP builds on the results of poverty diagnosis and a participatory planning process, laying out a poverty reduction strategy which recognizes the multiple dimensions of poverty. The poverty reduction strategy is translated into development goals, guiding principles, outlines of sector strategies and a macro-economic and medium-term expenditure framework for the first five years after independence. The NDP is a living plan which has guided policy development and implementation since 2002.

4. **In 2003 and in the aftermath of riots in December 2002 related to slow progress on poverty reduction, the government produced a Road Map to NDP implementation and an associated Stability Program which identify "priorities of priorities" within the NDP.** These documents focus on the areas considered essential to preserve economic and social stability, elaborate on prioritization and sequencing issues, and provide a costed implementation program for each ministry for the period 2003-2007.

5. **The development of seventeen SIPs and an accompanying medium-term expenditure framework has further facilitated NDP implementation.** During 2004, the government completed preparation of SIPs as well as two umbrella reports which provide the overall framework for the individual papers and outline a process for moving forward with implementation. The seventeen SIPs build on sector strategies to provide costed sector programs within a consistent macro-economic framework. Agency-level annual action plans (AAPs) linked to budgets provide the basis for policy implementation on a yearly basis.

6. **The NDP and subsequent implementing documents have also provided the framework for coordination of external assistance.** By articulating the Government's priorities and strategy, these documents have guided the realignment of external assistance from reconstruction to development. They have also served as an operational tool, helping external partners identify priorities and programs where they have a comparative advantage and minimizing the duplication and overlap often seen in small, post-conflict countries. The continued support and coordination of the donor community will be needed if the government's ongoing effort to ensure the alignment of external assistance with national priorities is to be achieved.

7. **Since its independence, Timor-Leste has made progress in NDP implementation by maintaining peace and stability, building state institutions and improving service delivery.** The country has made strides in healing past divisions and building the political unity necessary for nation-building. Key state organs including the Executive, Parliament, Judiciary, and the Office of the President have been endowed with policy and legislative frameworks, human and financial resources and physical infrastructure. There has also been progress in the area of service delivery. Many health facilities across the country have been rehabilitated, immunization and birth attendance rates have increased and infant and child mortality have declined. Schools have been rehabilitated, teachers are in place and primary school enrolment rates have increased nationwide. Roads and water supply systems have been rehabilitated in parts of the country and more reliable energy supply has been restored to Dili since the rehabilitation of its power station and the institution of a cost recovery system. In the agriculture sector, production of rice has recovered owing to the rehabilitation of irrigation systems while livestock health services have been restored.

8. **While there has been progress in implementation, significant challenges remain.** Key constraints to achieving sustainable growth, poverty-reduction and improved governance in Timor-Leste include: weak capacity, reflecting its embryonic institutions and limited human resources; a stagnant economy, with high levels of poverty and unemployment; unrealistic expectations about what can be achieved in the short term; and the challenge of managing oil/gas resources soundly in this difficult environment. Therefore, the remainder of the document will discuss the principal challenges ahead and the priority measures needed to address them. The Bank and Fund staffs believe these principal challenges are: i) encouraging macro-economic stability and growth through the effective use of oil and gas wealth; ii) building institutional capacity for service delivery and providing quality basic education; iii) strengthening governance and the judiciary; and iv) supporting job creation by improving the investment climate.

II. THE NATIONAL DEVELOPMENT PLAN

A. NDP Design and Implementation

9. **The NDP was prepared through a broad-based government-led consultative process.** Plan preparation was coordinated by cross-sectoral working-groups, led by Ministers. Technical work was informed by a participatory poverty assessment, followed by country-wide consultations which solicited input from over 38,000 people in 980 public

meetings. The NDP was discussed at a two-day workshop with a broad set of stakeholders, including civil society, the Catholic Church, and development partners. The workshop results were incorporated into the final version of the NDP, which was approved by Parliament at independence.

10. **The NDP sets out the country's vision for development, its main objectives and targets, key sector policies and a medium-term macro-fiscal framework but, like most PRSPs, it does not include a costing of the sector strategies needed to implement the plan.** The elaboration and costing of sector strategies and their integration into a medium-term fiscal framework has advanced through the development of the the Road Map, SIPs and medium-term expenditure framework. This planning and budgeting process was outlined in the NDP, but has mainly emerged during its implementation phase.

11. **Since 2002, the Government has put in place annual planning routines as part of the budget process, and the staffs recommend that further work be done to link plans, budgets, outputs and performance.** Each ministry prepares an Annual Action Plan (AAP) to inform budget preparation. Progress in implementation is monitored through Quarterly Reporting Matrixes (QRMs). Most AAPs and QRMs provide considerable detail on the activities planned and undertaken at departmental level, but little information on the quantity and quality of the services provided to the public. The Ministry of Health has made progress in establishing a performance monitoring framework linked to key service delivery indicators. The staffs encourage the government to extend this practice to other service delivery sectors. Ultimately, a few key performance indicators for each program should be presented in the budget documents, thereby linking resource allocations to the services provided and program level performance. In the meantime, the contribution of QRMs to the monitoring process could be fostered by strengthening their analytical component and using their information as an input into the budgeting process.

12. **The Sector Investment Programs (SIPs) provide an opportunity to align resource allocations with NDP and sector priorities, and the staffs recommend that they be prepared on a rolling basis.** Preparation of the SIPs on a rolling basis would provide the basis for strengthening medium-term budgeting and improving the alignment between sector strategies, plans, budgets and external assistance. It would also support the government's ongoing efforts to develop a Combined Sources Budget that covers its own resources as well as those of development partners.

13. **The recent establishment of joint government-donor Sector Working Groups (SWGs) to support SIP implementation and monitoring is a very positive development, and the staffs recommend extending their membership to civil society organizations.** The staffs commend the Government's initiative in establishing SWGs in agriculture, infrastructure, and health and encourage the establishment of the remaining groups. The staffs also recommend that the groups' sector monitoring function be fully exploited and encourage the Government to extend their membership to civil society organizations as originally envisaged in the NDP. The SWGs provide an avenue to institutionalize the participatory process initiated with the development of the NDP and the staffs encourage the Government to make full use of this opportunity.

14. **The staffs encourage the government to complete the monitoring and evaluation framework envisaged in the NDP by assigning responsibility for this function to a specific unit and charging it with tracking a small number of core NDP indicators.** The role of this central unit, the Office of National Statistics and line ministries should be clearly defined and coordination mechanisms clearly spelled out. This unit should lead the upcoming NDP assessment exercise and devise mechanisms to foster feedback loops into policy-making.

B. Poverty and Growth Diagnosis Underlying the NDP

15. **The NDP drew on a Poverty Assessment (2001) that provides a detailed picture of the nature and extent of poverty in Timor-Leste.** The report reviews the main determinants of poverty and assesses its regional and gender dimensions. The results of this assessment are presented in the “State of the Nation Report” of April 2002, which provides the analytical basis for the policy options presented in the Plan. In addition, since 2002, there has been an extensive program of survey work which provides a potentially rich resource for poverty and policy analysis. A Multiple-Indicator Cluster Survey was undertaken in 2002, a Demographic and Health Survey in 2003 and the first Population Census in 2004, while a second round of the living standards survey is tentatively scheduled to begin field operations in January 2006.

16. **Based on this and subsequent assessments, Timor-Leste is among the poorest countries in the world.** The GDP per capita is US\$ 405, one in five people lives on less than one dollar per day and two in five live below the national poverty line. Inequality is also high, with the poorest 40 percent of the population having an expenditure share of less than 18 percent. Two out of five adults are illiterate, half of children under five are stunted and the under-five mortality rate is 83 deaths per 1,000 live births. In urban areas, around 70 percent of the population has access to electricity and safe drinking water, but in rural areas, access rates are only 43 percent for drinking water and 11 percent for electrification. Moreover, high fertility and population growth rates compound the challenges of improving the welfare of the poor in Timor-Leste.

17. **The poverty reduction goals and targets set in the NDP are aligned with the MDGs but are often over-ambitious and could usefully be revisited.** Achievement of some of the targets set is unlikely to happen over the plan period. For instance, while no new survey data are available to conclusively verify this, with the estimated decline in non-oil per capita income since 2002, the incidence of poverty is likely to have increased. Similarly, in the health and education sectors, improvements are likely but the achievement of the ambitious targets set in the NDP remain unlikely. Therefore, there is a case for a review of poverty reduction goals as part of the upcoming NDP assessment as well as a need to further specify targets in quantitative (and not just directional) terms.

18. **The medium-term macro-economic objectives included in the NDP remain broadly valid, but the recent large increases in international oil prices and the acceleration of the oil production schedule present new opportunities and challenges.** As envisaged in the NDP, following independence, non-oil economic activity decelerated in response to the end of the emergency reconstruction phase and the related reduction in

international presence. The economy recovered only modestly in 2004, as a rebound in agriculture following a drought offset a further drawdown in the UN presence. Supported by the dollarized monetary regime and cautious macroeconomic policies, inflation declined to below 3 percent. The start of oil revenue inflows combined with high oil prices led to a sharp narrowing of the external current account deficit in 2004, while a sizable fiscal surplus of about 70 percent of non-oil GDP is expected for the current fiscal year. However, the development of non-oil private economic activity has not yet started and the execution of budgetary public investment has been low because of limited capacity.

19. **Although the initial effort in poverty diagnostics has been strong, staffs encourage deepening understanding of the determinants of growth and poverty patterns in Timor-Leste.** While these initial diagnostics provide a snapshot of the current situation, the elaboration of poverty trends will require institutionalizing the surveying effort. The challenge in this regard will be to maintain donor support and participation by a small population which may increasingly suffer from ‘survey fatigue.’ Development of domestic capacity for poverty analysis, fostering feedback loops into policy-making and strengthening dissemination efforts will also be critical to ensuring poverty diagnostics have the desired impact.

C. Main Pillars of the Strategy

20. **The NDP identifies sustainable growth and poverty reduction as its overriding goals.** Sustained economic growth is seen as a precondition for poverty reduction, with citizens and the private sector as the driving force and the government as the facilitator including through the execution of a well focused public investment program aimed at basic service delivery and the establishment of essential infrastructure. To ensure that growth has a significant impact on poverty reduction, the NDP proposes a poverty reduction strategy with four pillars: creation of opportunities for economic participation; delivery of basic social services; provision of security of person and property, and protection against unforeseen shocks; and empowerment of citizens and communities.

21. **Within this broad framework, the Road Map and Stability Program focus on three areas of the longer-term program where the government intends to have an immediate impact: governance, service delivery for poverty reduction, and job creation.** Good governance encompasses strengthening the administrative structures of the state, the justice system and the security forces. Service delivery is aimed at reducing poverty by supporting education, health, food security and enhanced access to markets for rural producers. Job creation centers on maintaining stability by supporting agriculture and private sector development and emphasizing youth and veterans of the resistance.

III. IMPLEMENTATION CHALLENGES

A. Encouraging Macro-Economic Stability and Growth through the Effective Use of Oil and Gas Wealth

22. **The NDP and more recently the SIPs acknowledge that to reach the country's ambitious growth targets and poverty-reduction objectives strong commitment to prudent macroeconomic policies and the continuation of donor support are needed.** The authorities have preserved their commitment to the dollar currency regime, which has been critical to maintaining low inflation, together with a prudent fiscal policy. In addition, the absence of external and domestic debt provides the government with a degree of freedom in economic management unavailable to most low-income countries. At the same time, the targeted medium-term non-oil growth of 6 percent that is needed to absorb a rapidly increasing labor supply is not likely to be achieved without more effective efforts in two areas. First, an adequate environment needs to be created for the development of private sector non-oil activity, including in the rural regions. Second, difficulties in budget execution constraining development spending, particularly infrastructure expenditure, for more rapid economic growth and poverty alleviation need to be addressed. At the same time, financing of the central government budget will not pose difficulties as annual fiscal surpluses of 34-40 percent of non-oil GDP are expected over the medium-term, based on most recent oil price projections. Despite these surpluses, Timor-Leste will need the continued support of the donor community for some years to come to assist in the design and execution of development projects for which domestic capacity is not yet available.

23. **The onset of substantial oil/gas production from Bayu Undan in 2004 and much higher international oil prices than envisaged in the NDP create new opportunities, while raising new challenges for the government.** Recent estimates of revenue for Timor Leste from currently assessed oil and gas reserves in Bayu Undan range between US\$ 2 to 5 billion over the 20 years production life of the field, on the basis of oil prices in the range of US\$25 to 45 per barrel. These large oil/gas revenue inflows provide much-needed financial resources, but also present the challenge of managing transparently and effectively large and volatile oil/gas revenue for current and future generations of Timorese. In addition, the large revenue inflows further emphasize the need to place a high priority on establishing a supportive environment for private sector activity in order to avoid adverse effects on the non-oil economy.

24. **Timor-Leste has made significant progress in designing a system to handle its new oil/gas wealth responsibly and the staffs commend the government on its plans to proceed with implementation in the year ahead.** Oil/gas taxation has been streamlined, the draft Petroleum Fund Act to establish a Norwegian-style petroleum fund-based on high standards of transparency and accountability—has been submitted to Parliament and is expected to be operational by July 2005, and a long-term savings policy has been adopted. The new sustainable income fiscal policy sets annual budget spending equal to the sum of domestic non-oil revenue and the estimated permanent annual income from the oil wealth.

With the creation of the petroleum fund and adherence to the new savings policy, Timor Leste will have established the long-term fiscal strategy needed to ensure productive and transparent use of oil/gas wealth while safeguarding fiscal stability. Nonetheless, risks at the implementation stage are possible, given limited administrative and financial management capacity. Should the establishment of the fund be delayed, the already large revenue inflows underscore the need to follow the fund's basic principles of transparency and accountability. The staffs also look forward to the establishment of the investment advisory board, the petroleum fund consultative council, and a framework for regular reporting to the public in time to support the launch of the petroleum fund.

25. **Against the background of the better-than-expected outlook for fiscal revenue, a significant increase in total expenditure is targeted for the medium-term.** Given the considerable development needs in Timor Leste, the staffs support moving toward the sustainable spending level (estimated at about \$130 million annually) as quickly as administrative and absorptive capacity in the economy would allow without aggravating either nonpriority spending levels or inflationary pressures. Nonetheless, the rapid overall proposed spending increases appear ambitious, barring a sharp improvement in spending capacity. Increases in this range also raise the risk of less well prioritized spending and of triggering inflationary pressures, given still limited absorptive capacity in the domestic economy. Therefore a more gradual but steady movement toward reaching the sustainable spending level would be advisable.

B. Building Institutional Capacity for Service Delivery and Providing Quality Basic Education

26. **Improving the availability, efficiency, and quality of public services will be essential to delivering tangible results to the population.** Ensuring affordable access to quality services in education, health, agriculture, and infrastructure in the context of a rapidly growing and dispersed population, however, will be a major challenge. The challenge will not initially be one of resource availability but rather of government capacity to manage resources available to effectively deliver the desired services.

27. **Enhanced service delivery will require, in the long run, enhanced institutional capacity and, in the short run, the establishment of partnerships.** Current capacity is weak and vulnerable to the departure of a large number of international advisers. Over the next few years, strengthening government capacity to design, manage, implement and monitor its policies and budgets will be the central challenge. Over the short run, however, much could be done to improve budget execution while enhancing service delivery to the population. Therefore, the staffs encourage the government to consider possibilities that would allow for effective service delivery in the short-run while building up sustainable government capacity in the medium-term. In this regard, the government may wish to consider establishing creative partnerships with civil society, the church and the private sector while state capacity is strengthened. Elaborating and implementing capacity-building strategies for key government ministries, possibly in conjunction with development partners,

would also be an important building block to improving institutional capacity for service delivery.

28. Public finance management poses a particular challenge to service delivery as budget execution capacity is extremely limited and the staffs encourage the government to streamline public finance management systems. A combination of complex and over-centralized processes, and weak human resource and institutional capacity on the one hand, and a high level of commitment to fiduciary accountability on the other, results in very low levels of budget execution. As a result, a high percentage of budgeted resources remain unspent with implications for service delivery. In this regard, strengthening the Government's institutional capacity will require increased individual skills and knowledge, improved systems and processes and supportive attitudes and behaviors. In particular, the Government should consider filling existing vacancies, preparing succession plans for the departure of international advisers and increasing delegation of public expenditure management functions within ministries and elaborating plans for decentralization to line ministries and districts. Moreover, enhanced coordination between line ministries, the Ministry of State Administration and the Ministry of Planning and Finance would be an important contribution to improving public finance management and service delivery. At the same time, the commitment to fiduciary accountability should be maintained even as the reforms to improve budget execution are undertaken. The support of the donor community to develop a comprehensive program for strengthening public finance management will be critical to address this bottleneck to NDP implementation.

29. An educated population will be the best asset to support economic growth and good governance in Timor-Leste. Although some progress has been made over the past three years, Timor-Leste's literacy rate is only 60 percent and the sector faces enormous challenges. Considerable progress has been made since the destruction of 1999 in the physical reconstruction of schools and in teacher deployment and student enrollment rates have expanded. Moreover, a National Education Policy, a Basic Education Law and the framework for the primary education curriculum have been drafted. The key challenge ahead will lie in further increasing enrollment rates while reducing currently high drop-out and repetition rates. These improvements will require the adoption and implementation of a medium to long-term program to improve access to and quality of basic education. To achieve this, the Ministry has set a target of universal primary school completion by 2015 and is developing an Education for All (EFA) strategy that will direct the majority of government and donor resources for the sector to primary education. Key to the success of the EFA program will be improved donor coordination in the sector as well as enhanced Government capacity to develop, implement and monitor its policies and budgets. The Government may also wish to consider revising its policy on primary education user fees, which weigh heavily on the poor while a high percentage of the education sector budget goes unspent.

C. Strengthening Governance, Especially the Justice Sector and Customs

30. **In the area of governance, the architecture of checks and balances set out in the Constitution remains to be completed and strengthened and decisive action will be needed to combat corruption.** Strengthening governance will require the reinforcement of non-executive state institutions such as the Parliament, the judiciary, the Provedor dos Direitos Humanos e da Justiça, and the Consultative Council that will be established to oversee the management of the Petroleum Fund. Good governance also depends on independent audit and the development of professionalism and a spirit of public service within Government agencies.

31. **In the year ahead, priority attention should be devoted to the justice sector and customs administration.** All acting Timorese judges have failed their qualifying test and will need to be replaced while they undergo training. Therefore, the planned elaboration of a medium-term human resource development plan covering both the recruitment of international and the training of Timorese court actors will be of the utmost importance. Developing a resource mobilization strategy to support this plan before the withdrawal of UNMISSET, which currently funds and recruits international court actors, will also be necessary. Finally, the design of a case management system and, more broadly, sound systems and processes will also be needed to improve the performance of the sector.

32. **Customs has registered significant improvements and the staffs encourage the government to proceed with the second stage of their reform program.** Over the past year, the collection of import duties has increased, the value of Customs exemptions and the time required for Customs clearance have been significantly reduced and the effectiveness and integrity of staff have increased. These improvements are largely due to new leadership in Customs, the introduction of ASYCUDA (automated system of customs data administration) and accompanying reforms. In a second stage to begin this year, further reforms are envisaged under the ASYCUDA program, including the installation of a management information system, computerized risk assessment system and cargo manifest, the institutional strengthening of the Customs service, the extension of the new systems and reforms to the rest of the country (outside Dili), and a thorough training in systems and ethics.

33. **Transparency and communications and fostering external scrutiny will be critical to the achievement of these goals.** Transparency and communications with regard to public activities, oil revenues, expenditures, and financial management are particularly critical assets for good governance in an environment of still-fledgling institutions. In particular, the staffs commend the Government on its commitment to publish detailed accounts of all revenues received by the petroleum fund and encourage the publication of budgets and executed budget figures. Moreover, the development of external scrutiny will be essential to balancing out a strengthening state. This development should be encouraged by creating the enabling environment for a healthy and dynamic civil society, private sector and media. Finally, much of the progress made in Timor-Leste over the past three years has centered on developing the policy framework and establishing state institutions. While positive and necessary, these gains are largely invisible to the population. Therefore,

effective communication and genuine participation are critical to shoring up popular support for the national development process while service delivery capacity is strengthened.

D. Supporting Job Creation by Improving the Investment Climate

34. **Job creation in the private sector will be critical for the achievement of poverty reduction goals and maintaining economic and political stability in the long run.** Over half the population is under 15, a percentage which will continue to increase due to a population growth rate of over 3 percent per annum. This large and growing group of young people will continue to enter the labor market each year requiring significant growth in job creation. Moreover, lack of economic opportunities in rural areas is leading to high levels of migration to urban centers. Urban youth unemployment was 43% in 2001, and has probably increased since. Therefore, growth in labor-intensive agriculture and agro-industry in rural areas will be essential to reducing poverty and inequality throughout the country. Poor performance in this area could lead to mounting pressure for Government to relax its savings policy and fiscal discipline and expand the size of the public sector. It could also undermine social and political stability.

35. **Job creation, however, remains a major challenge and the staffs encourage the government to enact measures to improve the legislative and regulatory environment for businesses.** Timor-Leste suffers from a combination of relatively high wages and energy prices, poor communications, high administrative costs of doing business and legislative and regulatory uncertainty. Improvements in infrastructure will be critical to lowering the costs of doing business as well as enhancing market access for the rural population. The role of government institutions will also be key to improving the investment climate, as will be intensive dialogue between government and the private sector. Providing the necessary political and budgetary support to the recently-established Investment and Export Promotion Agency will be important, as will be the continuation of dialogue with the private sector. In this regard, the first national-level Business-Government Dialogue forum, scheduled for mid-April 2005, is expected to focus on reducing the costs of and the regulatory burden on doing business and the staffs encourage the government to carefully consider and act upon the recommendations emerging from this forum.

IV. CONCLUSIONS AND ISSUES FOR DISCUSSION

36. **The NDP and subsequent strategy and policy documents provide a sound framework for poverty-reduction while the institutional and regulatory framework for the management of oil and gas resources constitutes best practice.** The government has also made progress in the planning, budgeting and reporting areas and has a high level of fiduciary accountability, in particular for a low-income country.

37. **Implementation, however, remains a challenge.** The poverty situation in Timor-Leste is extremely challenging while administrative capacity is low. To support the government in addressing these challenges, the staffs have identified five priority areas for

effective NDP implementation. These areas are: (i) building institutional capacity for effective service delivery; ii) encouraging more rapid economic growth by effectively managing oil and gas resources and ensuring macroeconomic stability; (iii) strengthening governance; iv) providing high-quality basic education; and v) establishing an enabling environment for private sector activity to enhance job creation.

38. **It is proposed that the document produced for discussion at the annual Timor-Leste Development Partners meeting be used for PRS reporting purposes.** This document outlines progress in the previous year and sets out the main policy and budget guidelines for the year ahead. The proposed route to reporting would have the twin advantages of supporting the ongoing improvement of the quality of existing reporting documents while not burdening the government with additional reporting requirements.

39. **Do the Executive Directors concur with:** (i) the broad direction of the proposed strategy as outlined in the NDP; (ii) staffs' characterization of implementation challenges; and (iii) staff's recommendations for strengthening the implementation, monitoring and evaluation of the NDP?

EAST TIMOR

NATIONAL DEVELOPMENT PLAN

After independence on 20 May 2002, the draft Plan will be presented to the Parliament for consideration and adoption.

Planning Commission
Dili
May 2002

Table of Contents

LIST OF ACRONYMS AND GLOSSARY	III
Foreword.....	VI
Foreword.....	VII
VISION.....	VIII
EXECUTIVE SUMMARY	
INTRODUCTION	1
DEVELOPMENT STRATEGY.....	1
POVERTY REDUCTION STRATEGY	2
CAPACITY BUILDING FOR PLAN IMPLEMENTATION	3
MONITORING, EVALUATION, AND PLANNING REVIEW	5
MACROECONOMICS AND PUBLIC FINANCE POLICY FRAMEWORK	5
MEDIUM TERM ECONOMIC AND FINANCING OUTLOOK	6
POLITICAL DEVELOPMENT, FOREIGN RELATIONS, DEFENCE AND SECURITY.....	7
POVERTY REDUCTION, RURAL AND REGIONAL DEVELOPMENT.....	8
HUMAN DEVELOPMENT: EDUCATION AND HEALTH	9
AGRICULTURE, FISHERIES AND FORESTRY	10
NATURAL RESOURCES AND ENVIRONMENT	11
INDUSTRY, TRADE AND THE PRIVATE SECTOR.....	11
INFRASTRUCTURE	12
PART 1 VISION AND STRATEGIES	
1. INTRODUCTION	
BACKGROUND.....	14
THE PLANNING PROCESS.....	14
ORGANIZATION OF THE DOCUMENT.....	15
2. VISION, GOALS, PRINCIPLES AND INDICATORS	
THE LAND AND THE PEOPLE.....	17
THE ECONOMY.....	18
THE DEVELOPMENT VISION	19
DEVELOPMENT GOALS.....	20
GUIDING PRINCIPLES	21
KEY DEVELOPMENT INDICATORS	23
3. THE DEVELOPMENT STRATEGY	
INTRODUCTION	24
THE DEVELOPMENT STRATEGY	25
Poverty Reduction.....	25
Gender Mainstreaming and Empowerment of Women	25
Human Resources Development.....	26
Language and Communication	27
Transforming Subsistence Production into a Market-based Economy.....	27
Improving Productivity and Modernising Production	28
Creating an Enabling Environment for the Private Sector to Flourish	28
Managing Public Finances	29

Administration of Oil and Gas Revenues	30
GOVERNANCE AND MACROECONOMIC MANAGEMENT	30
Governance	30
Macroeconomic Management.....	30
4. POVERTY REDUCTION STRATEGY	
INTRODUCTION	32
POVERTY IN EAST TIMOR	33
CAUSES OF POVERTY	34
CONSEQUENCES OF POVERTY	35
POVERTY REDUCTION STRATEGY.....	36
Opportunities for Economic Participation	37
Basic Social Services	38
Security	38
Empowerment.....	40
CONCLUSIONS.....	41
5. CAPACITY BUILDING FOR PLAN IMPLEMENTATION	
INTRODUCTION	42
GOVERNMENT AND GOVERNANCE	42
DECENTRALISATION	44
EMPLOYMENT.....	44
EDUCATION AND LITERACY	44
HEALTH	45
INFRASTRUCTURE	45
THE JUDICIARY	45
CONCLUSION	46
6. MONITORING, EVALUATION, AND REVIEW	
INTRODUCTION	47
MONITORING PERFORMANCE AND OBJECTIVES	48
Monitoring at the National Level.....	49
Sector-level Monitoring	50
Program-level Monitoring	50
Project-level Monitoring.....	50
EVALUATION OF PERFORMANCE RESULTS.....	51
Planned Objectives	51
Measurable Benchmarks	52
Methods of Analysis	52
Correction Process	53
PLANNING REVIEW	54
INSTITUTIONAL SETTING: MODEL OF PLANNING, MONITORING AND EVALUATION	54
CONCLUSIONS.....	55
PART 2 ECONOMIC OUTLOOK.....	57
7. MACROECONOMIC POLICY FRAMEWORK	
VISION	58
INTRODUCTION	58
GOALS	59
General Goals	59
Macroeconomic Goals	59
Public Finance/Fiscal Goals.....	59

GUIDING PRINCIPLES	59
CONSTRAINTS	60
OVERVIEW OF POLICY CHALLENGES	61
GOALS, POLICY ACTIONS AND PERFORMANCE INDICATORS	62
Goal No. 1: Institutional Strengthening	62
Goal No. 2: Poverty Reduction	62
Goal No. 3: Pursuit of Economic Growth	63
Goal No. 4: Pursuit of Low Inflation	64
Goal No. 5: Pursuit of more employment	65
Goal No. 6: Pursuit of stronger banking and finance sector	65
Goal No. 7: Pursuit of a stronger external sector	66
Goal No. 8: Pursuit of improved revenue collections	67
Goal No. 9: maximise collections and savings from timor sea revenues	67
Goal No. 10: pursue creative and effective expenditure programs	68
Goal No. 11: pursue appropriate deficit and financing policies	68
SUMMARY OF PROGRAMS / PROJECTS SPECIFIC TO MACROECONOMICS / PUBLIC FINANCE SECTOR	70
8. MEDIUM TERM ECONOMIC AND FINANCING OUTLOOK	
INTRODUCTION	72
ECONOMIC GROWTH	73
EMPLOYMENT/UNEMPLOYMENT	75
PRICES AND WAGES	77
FISCAL/BUDGET	78
Domestic Revenues	78
Timor Sea Oil and Gas Revenues	78
Total Expenditures	80
Recurrent and Capital / Development Shares of Total Combined Sources Expenditure..	82
Financing the Deficit and Aid	86
BANKING AND FINANCE	87
EXTERNAL/BALANCE OF PAYMENTS	87
TWO CRITICAL FINANCING ISSUES	88
PROPOSED MANAGEMENT APPROACHES AND OUTLOOK FOR OIL AND GAS REVENUES	89
Introduction	89
Proposed Management Approaches	89
Financial Outlook	91
AID MANAGEMENT POLICY AND THE PREFERRED FORWARD ODA PROGRAM	91
CFET Budget Support	91
Aid Policy	92
Future ODA Programs and Projects	93
PART 3 STRATEGIES FOR NATIONAL DEVELOPMENT: SECTORAL PLANS	105
9. POLITICAL DEVELOPMENT, FOREIGN RELATIONS, DEFENCE AND SECURITY	
VISION	106
INTRODUCTION	106
GOALS	107
OBJECTIVES	108
GUIDING PRINCIPLES	109

KEY DEVELOPMENT INDICATORS	111
Parliament	111
Public Administration	111
Security and Defence Forces	111
Foreign Affairs.....	111
Public Prosecution and Defence	111
Ombudsman’s Office	111
Promotion of Gender Equality	112
Media	112
Civil Society	112
PROBLEMS AND CONSTRAINTS	112
General constraints:	112
More specific constraints:.....	113
STRATEGIES	113
POLICIES	114
General Policies	114
Public Administration and Democratisation Policies	114
Security and Defence Forces	115
External Relations.....	115
Justice, Human Rights and Gender Equality	115
PROGRAMS	116
Public Administration and Governance	116
<i>Transparent governance</i>	116
<i>Institutional Development</i>	117
<i>Decentralisation and Participation</i>	117
Media Development.....	117
Security and Defence Forces	117
<i>Defence program</i>	117
<i>Police and Security Service Programs</i>	117
External Relations.....	118
Capacity Building Program	118
<i>Policy Development Program</i>	118
<i>Action Program</i>	118
Justice, Human Rights and Gender Equality	118
<i>Institutional Development Program</i>	119
<i>Legislative Program</i>	119
<i>Reconciliation Program</i>	119
<i>Rights and Equality Program</i>	119

10. POVERTY REDUCTION, RURAL AND REGIONAL DEVELOPMENT

VISION	121
INTRODUCTION	121
Poverty Reduction.....	121
Rural Development	122
Regional Development	122
GOALS	123
GUIDING PRINCIPLES	124
KEY DEVELOPMENT INDICATORS	125
PROBLEMS AND CONSTRAINTS	125
Resource Constraints	125
Social Aspects.....	126
Gender aspects	126
Capacity	126
Infrastructure.....	127

Rural-urban and regional disparities	127
Private sector	127
Governance	127
STRATEGIES AND POLICIES INCLUDING PROGRAMS AND PROJECTS	128
POVERTY REDUCTION	128
Creating economic opportunities	128
Providing social services.....	130
Enhancing security including disaster preparedness and safety nets	130
<i>Security</i>	130
<i>Disaster preparedness</i>	131
<i>Vulnerable groups</i>	132
<i>Empowering the people</i>	133
<i>Gender dimensions</i>	134
RURAL DEVELOPMENT.....	135
REGIONAL DEVELOPMENT	137
CIVIL SERVICE.....	138
Immigration Service.....	140
National Archives	140
Labour	141

11. SOCIAL AND HUMAN DEVELOPMENT: EDUCATION AND HEALTH

VISION	143
BACKGROUND AND STATUS	143
Education	143
Health	144
Gender	145
GOALS	145
GUIDING PRINCIPLES	145
KEY DEVELOPMENT INDICATORS	146
Education	146
Health	146
Labour	147
Economic, Social and Culture.....	147
Gender Equality	147
PROBLEMS AND CONSTRAINTS.....	148
Problems And Constraints Common To Both Sectors.....	148
<i>Literacy</i>	148
<i>Culture</i>	148
<i>Poverty</i>	148
<i>Poor nutrition</i>	148
<i>Infrastructure</i>	149
<i>Quality of services</i>	149
<i>Resource constraints</i>	149
<i>Legal Framework</i>	149
<i>Gender related issues</i>	149
<i>Sector Specific Problems And Constraints</i>	149
<i>Education</i>	149
<i>Health</i>	151
OBJECTIVES	152
Education	152
Health	153
POLICIES	154
Education	154
Health	154
STRATEGIES	155

Overall Strategies.....	155
Education.....	155
Health.....	155
Gender.....	155
Specific Strategies.....	156
Education.....	156
Health.....	157
PROGRAMS AND PROJECTS.....	160
Education.....	160
Program 1: Expand Access and Improve Internal Efficiency.....	160
Program 2: Improve the Quality of Education.....	160
Program 3: Build Internal Management Capacity and Improve Services Delivery.....	161
Program 4: Non-Formal Education and Adult Literacy.....	161
Program 5: Develop Tertiary Education.....	162
Program 6: Promote East Timorese Culture and the Arts.....	162
Program 7: Promote Youth Welfare.....	162
Program 8: Promote Physical Education and School Sports.....	162
Program Priorities.....	163
Health.....	163
Program 1: Child Health.....	163
Program 2: Maternal Health.....	163
Program 3: Reproductive Health.....	163
Program 4: Health Promotion.....	163
Program 5: Communicable Diseases Control, including:.....	163
Program 6: Environmental and Occupational Health.....	164
Program 7: Specialised Services Programs.....	164
Program 8: Medical Supplies Program.....	164
Program 9: Laboratory Services.....	164
Program 10: Health Facilities Rehabilitation and Development.....	164
Program 11: District Health Services.....	164
Program 12: Health Sector and Management Programs.....	164
Program 13: Health Policy and Planning Development.....	164
Program 14: Support to Administration and Finance functions.....	165
The Second Health Sector Rehabilitation and Development Project.....	165
PERFORMANCE INDICATORS.....	166
Gender Mainstreaming.....	169

12. AGRICULTURE, FISHERIES AND FORESTRY

VISION.....	171
INTRODUCTION.....	171
Poverty and the Agriculture Sector.....	172
MISSION.....	174
GOALS.....	174
GUIDING PRINCIPLES.....	175
Sustainability.....	175
Efficiency.....	175
Equity.....	175
Self-reliance.....	175
Values.....	175
Participatory Development.....	175
KEY DEVELOPMENT INDICATORS.....	175
PROBLEMS AND CONSTRAINTS.....	176
Capacity.....	176
Management and Entrepreneurial Skills.....	176
Data and Information.....	177
Financial Resources.....	177
Poor Transport, Communication, Marketing and Processing Infrastructure.....	177

Low Productivity.....	177
Poor Quality Produce	177
State of Irrigation Schemes	177
Land Tenure	177
Comparative Advantage and Diversity	178
Fisheries Legislation and Management.....	178
Forest Degradation.....	178
Forestry Legislation	178
Quarantine	178
STRATEGIC POLICY DIRECTIONS.....	178
PROGRAMS AND PROJECTS	179
Mission Statement.....	180
Problems, Goals and Policies.....	180
Crop Production Division	181
Program 1: Enhancement of Food Crops Production.....	181
Program 2: Enhancement of Horticultural Crop Production	182
Program 3: Enhancement of Industrial Crops Production	182
Program 4: Support to Farmers' Associations	183
Program 5: Crop Protection	183
Livestock Division	184
Program 1: Development of Livestock Production	184
Program 2: Prevention and Eradication of Livestock Diseases.....	184
Irrigation Division.....	185
Program 1: Rehabilitation of Existing Irrigation Schemes.....	185
Program 2: Establishment of Rural Water Harvesting Systems	186
Program 3: Maintenance and Repair Work.....	186
Performance Targets	186
Program 4: Sector Management Recovery and Development.....	186
Department of fisheries and marine environment.....	187
Mission Statement.....	187
Problems, Goals and Policies.....	187
Program 1: Fisheries and Marine Environment Management	189
Program 2: Fisheries Industry Development.....	189
Program 3: Aquaculture	189
Measurement	190
Department of forestry	190
Mission Statement.....	190
Problems, Goals and Policies.....	190
Program 1: Reforestation and Forest Rehabilitation.....	191
Performance Targets	192
Program 3: Forest Production and Utilisation.....	193
Research And Extension Centre	193
Program 1: Research and Laboratory.....	194
Program 2: Information and Extension	194
Program 3: Geographic Information System.....	195
Cadastral Unit	195
Program 1: Geography and Cadastre.....	196
Policy and Planning Unit	196
Program/Projects.....	200
APPENDIX 12.1: OVERVIEW OF DONOR FUNDED PROJECTS IN THE	
AGRICULTURE SECTOR	205
TFET PROJECT 1 OVERVIEW.....	205
BILATERAL PROJECTS OVERVIEW	206
MULTILATERAL PROJECTS OVERVIEW.....	209

13. NATURAL RESOURCES AND ENVIRONMENT	
VISION	210
INTRODUCTION	210
Poverty, Natural Resources and Environment	211
MISSION	212
GOALS	212
GUIDING PRINCIPLES	213
Sustainability	213
Efficiency	213
Equity	213
KEY DEVELOPMENT INDICATORS	213
Department of Natural and Mineral Resources	213
Division of Environment	213
PROBLEMS AND CONSTRAINTS	214
Capacity	214
Legal and Regulatory Frameworks	214
Data and Information	214
Financial Resources	214
Acknowledgment and Independence	214
GOALS OF EACH AGENCY	215
Department of Natural and Mineral Resources	215
Division of Environment	215
POLICIES	216
Department of Natural and Mineral Resources	216
Division of Environment	216
PROGRAMS AND PROJECTS	217
Department of natural resources and Minerals	217
Program 1: Institutional and Capacity Building	217
Program 2: Enabling Legal and Regulatory Framework	218
Program 3: Sectoral Development and Promotion	218
Division of environment	219
Program 1: Environmental Governance Framework for East Timor	219
Project 1: Development & implementation of environmental legislation	220
Project 2: Policy development for catchments and coasts	220
Project 3: Development of National Environmental Policy	220
Program 1: Environmental Governance Framework for East Timor	220
Department of Natural Resources & Minerals	222
Division of Environment	223
14. INDUSTRY, TRADE AND THE PRIVATE SECTOR	
VISION	224
INTRODUCTION	224
WORKING GROUP RESULTS	227
Key Development Indicators for the Five-year Plan:	228
Issues and Constraints	228
OFFICE OF THE DIRECTOR-GENERAL (ODG) – OVERVIEW	230
OFFICE OF THE DIRECTOR-GENERAL– PROGRAM SUMMARY	230
Programs of the ODG	230
Key Objectives:	230
Key Strategies:	231
Program 1: Coordination of Divisional Promotions	231
Program 2: Coordination of Policy and Regulatory Development	231
Program 3: Institutional Capacity Building	232
OFFICE OF THE DIRECTOR-GENERAL – OBJECTIVES	232

OFFICE OF THE DIRECTOR-GENERAL – STRATEGIES	232
OFFICE OF THE DIRECTOR-GENERAL – PROGRAMS AND PROJECTS	233
<i>Program 1: Coordination of Divisional Promotions</i>	233
<i>Program 2: Coordination of Policy and Regulatory Development</i>	233
<i>Program 3: Institutional Capacity Building</i>	234
OFFICE OF THE DIRECTOR-GENERAL – PERFORMANCE INDICATORS	235
DIVISION OF INDUSTRY (DoI) – OVERVIEW	235
DIVISION OF INDUSTRY - PROGRAM SUMMARY	236
Programs of the DoI	236
Objectives:	236
Strategies:	237
<i>Program 1: Industrial Development</i>	237
<i>Program 2: Policy and Regulatory Development</i>	237
<i>Program 3: Divisional Training and Development</i>	237
<i>Program 4: Micro-enterprise and SME Development</i>	238
DIVISION OF INDUSTRY - OBJECTIVES	238
DIVISION OF INDUSTRY - STRATEGIES	238
DIVISION OF INDUSTRY – PROGRAMS AND PROJECTS	239
<i>Program 1: Industry Promotion</i>	239
<i>Program 2: Policy and Regulatory Development</i>	240
<i>Program 3: Divisional Training and Development</i>	240
<i>Program 4: Micro-enterprise and SME Development</i>	240
DIVISION OF INDUSTRY – PERFORMANCE INDICATORS	241
Objectives	241
Performance Indicators	241
DIVISION OF INVESTMENT – OVERVIEW	242
DIVISION OF INVESTMENT – PROGRAMMATIC SUMMARY	243
Programs of the DI	243
Objectives:	243
Strategies:	243
<i>Program 1: Investment Promotion</i>	244
<i>Program 2: Policy and Regulatory Development</i>	244
<i>Program 3: Divisional Training and Development</i>	244
<i>Program 4: Foreign Investment Management</i>	244
DIVISION OF INVESTMENT - OBJECTIVES	244
DIVISION OF INVESTMENT - STRATEGIES	245
DIVISION OF INVESTMENT – PROGRAMS AND PROJECTS	245
<i>Program 1: Investment Promotion</i>	246
<i>Program 2: Policy and Regulatory Development</i>	246
<i>Program 3: Training and Development</i>	247
<i>Program 4: Foreign Investment Management</i>	247
DIVISION OF INVESTMENT – PERFORMANCE INDICATORS	248
DIVISION OF TOURISM – OVERVIEW	249
DIVISION OF TOURISM – PROGRAM SUMMARY	249
Programs of the DT	249
Objectives:	249
Strategies:	250
<i>Program 1: Tourism Promotion</i>	250
<i>Program 2: Policy and Regulatory Development</i>	250
<i>Program 3: Divisional Training and Development</i>	251
DIVISION OF TOURISM - OBJECTIVES	251
DIVISION OF TOURISM - STRATEGIES	251
DIVISION OF TOURISM – PROGRAMS AND PROJECTS	252
<i>Program 1: Tourism Promotion</i>	252
<i>Program 2: Policy and Regulatory Development</i>	252
<i>Program 3: Divisional Training and Development</i>	253

DIVISION OF TOURISM – PERFORMANCE INDICATORS	254
DIVISION OF TRADE - OVERVIEW	255
DIVISION OF TRADE – PROGRAM SUMMARY	256
Programs of the Division of Trade	256
Objectives:	256
Strategies:.....	256
<i>Program 1: Trade Promotion</i>	256
<i>Program 2: Policy and Regulatory Development</i>	257
<i>Program 3: Divisional Training Development</i>	257
DIVISION OF TRADE - OBJECTIVES.....	257
DIVISION OF TRADE - STRATEGIES	258
DIVISION OF TRADE – PROGRAMS AND PROJECTS	258
<i>Program 1: Trade Promotion</i>	258
<i>Program 2: Policy and Regulatory Development</i>	259
<i>Program 3: Divisional Training and Development</i>	260
<i>Program 4: Business Registration</i>	260
DIVISION OF TRADE – PERFORMANCE INDICATORS	262

15. INFRASTRUCTURE

VISION	263
INTRODUCTION	263
MAJOR GOALS OF INFRASTRUCTURE	264
GUIDING PRINCIPLES FOR DEVELOPMENT	265
DIRECTOR-GENERAL, DEPARTMENT OF WATER & PUBLIC WORKS (MINISTRY FOR WATER AND PUBLIC WORKS)	265
PUBLIC WORKS DIVISION	266
Public Works Objectives	266
Constraints, Problems, and Issues.....	267
Public Works Strategies.....	267
Public Works Programs & Projects	268
<i>Program 1: Institution Building</i>	268
<i>Program 2: Urban Planning</i>	268
<i>Program 3: Slums Improvement</i>	269
<i>Program 4: Provision of Government Buildings</i>	269
<i>Program 5: Public Education and Training</i>	269
ROADS, BRIDGES AND FLOOD CONTROL DIVISION.....	271
DRBFC Objectives	271
Constraints, Problems and Issues.....	271
DRBFC Strategies.....	272
DRBFC Programs & Projects	273
<i>Program 1: Road & Bridge Rehabilitation and Maintenance</i>	273
<i>Program 2: Flood Control and Erosion Prevention</i>	274
WATER AND SANITATION DIVISION.....	275
WSS Division Objectives	275
Constraints, Problems and Issues.....	276
WSS Division Strategies.....	276
WSS Division Programs and Projects	277
<i>Program 1: Institution and Capacity Building</i>	277
<i>Program 2: Urban Water Supply</i>	278
<i>Program 3: Urban Sanitation</i>	278
<i>Program 4: Community Water and Sanitation</i>	279
<i>Program 5: Water & Sanitation Support and Public Safety</i>	279
RESEARCH AND DEVELOPMENT DIVISION	281
Research and Development Division Objectives.....	281
Constraints, Problems and Issues.....	281

Research and Development Division Strategies	281
Research and Development Division Programs and Projects	282
<i>Program 1: Development of Appropriate Technology</i>	282
<i>Program 2: Material and Construction Testing</i>	282
DIVISION OF ENERGY (MINISTRY OF ECONOMIC AFFAIRS & PLANNING)	284
Division of Energy Objectives	284
Division of Energy Constraints, Problems and Issues	285
Division of Energy Strategies	285
Division of Energy Programs and Projects	286
<i>Program 1: Institutional Development</i>	286
<i>Program 2: Improvement of Services</i>	286
<i>Program 3: Capacity Building</i>	287
DEPARTMENT OF COMMUNICATIONS AND TRANSPORT	288
DIVISION OF LAND TRANSPORTATION	288
Division of Land Transportation Objectives	288
Constraints, Problems and Issues	289
Division of Transportation Strategies	290
Division of Transportation Programs and Projects	290
<i>Program 1: Institutional and Staff Development</i>	290
<i>Program 2: Traffic Management</i>	290
<i>Program 3: Vehicular Regulation and Safety</i>	291
DIVISION OF SEA TRANSPORTATION	292
Division of Sea Transportation Objectives	293
Constraints, Problems and Issues	293
Division of Sea Transportation Strategies	294
Division of Sea Transportation Programs and Projects	294
<i>Program 1: Institutional Development</i>	294
<i>Program 2: Port Rehabilitation and Development</i>	295
<i>Program 3: Port Services</i>	295
<i>Program 4: Capacity Building</i>	295
DIVISION OF CIVIL AVIATION	297
Division of Civil Aviation Objectives	298
Constraints, Problems and Issues	298
Division of Civil Aviation Strategies	298
Division of Civil Aviation Programs and Projects	299
<i>Program 1: Institutional Development</i>	299
<i>Program 2: Comoro Airport Operations</i>	299
<i>Program 3: Improvement of National Services</i>	300
<i>Program 4: Capacity Building</i>	300
TELECOMMUNICATIONS (SUB-SECTOR TO DIVISION OF TELECOMMUNICATIONS AND POST)	302
Telecommunications Objectives	302
Constraints, Problems and Issues	303
Telecommunications Strategies	303
Telecommunications Programs and Projects	304
<i>Program 1: Regulation</i>	304
<i>Program 2: Telecommunications Operations</i>	304
<i>Program 3: Capacity Building</i>	304
POSTAL SERVICES (SUB-SECTOR TO DIVISION OF TELECOMMUNICATIONS AND POST)	305
Postal Services Objectives	306
Constraints, Problems and Issues	306
Postal Services Strategies	307
Postal Services Programs and Projects	307
<i>Program 1: Restoration and Development</i>	307
<i>Program 2: Human Resource Capacity</i>	307
<i>Program 3: Innovations and Expansion</i>	308
DIVISION OF METEOROLOGY	309

Division of Meteorology Objectives.....	309
Constraints, Problems and Issues.....	310
Division of Meteorology Strategies	310
Division of Meteorology Programs and Projects.....	311
<i>Program 1: Operational Infrastructure</i>	<i>311</i>
<i>Program 2: Capacity Building</i>	<i>311</i>

LIST OF ACRONYMS AND GLOSSARY

ABBREVIATION	WORD DEFINITION
ADB	Asian Development Bank
ARP	Agricultural Rehabilitation Project
ASCs	Agriculture Service Centres
ASEAN	Association of South-East Asian Nations
AusAID	Australian Agency for International Development
BDCs	Business Development Centres
BDP	Bilateral Development Projects
BOT	Build, Operate and Transfer
BPA	Banking and Payments Authority
BRN	Business Registration Unit
CCCS	Consultative Commission for Civil Society on Development
CFET	Consolidated Fund for East Timor
CGIAR	Consultative Group for International Agriculture Research
CHCs	Community Health Centres
CIDA	Canadian International Development Agency
Clandestinos	Members of Clandestine Resistance Network
CoC	Chambers of Commerce
COM	Council of Ministers
CPLP	Community of Portuguese Speaking Nations
DAL	Department of Agriculture and Livestock
DI	Division of Investment
DLP	Distance Learning Program
DNMR	Department of Natural and Mineral Resources
DoE	Division of Environment
DoF	Department of Forestry
DoI	Division of Industry
DoL	Division of Labour
DoT	Division of Trade
DRBFC	Division of Roads, Bridges and Flood Control
DT	Division of Tourism
EDTL	Electricity Authority of East Timor

EIA	Environmental Impact Assessment
ESCAP	Economic and Social Commission for Asia and the Pacific
ESD	Ecologically Sustainable Development
FALINTIL	Armed Forces for the National Liberation of East Timor
FDI	Foreign Direct Investment
FDTL	East Timor Defence Force
FIL	Foreign Investment Law
FME	Department of Fisheries and Marine Environment
FY	Financial Year
GDP	Gross Domestic Product
GIS	Geographic Information System
HIV/AIDS	Human Immune Deficiency Virus/Acquired Immune Disease Syndrome
HRD	Human Resources Development
ICAO	International Civil Aviation Organisation
IEC	Information, Education and Communication
IMCI	Integrated Management of Childhood Illness
IMF	International Monetary Fund
IT	Information Technology
JPDA	Joint Petroleum Development Area
LDCs	Least Developed Countries
LPG	Liquid Petroleum Gas
MAF	Ministry of Agriculture and Fisheries
MCT	Ministry of Communications and Transport
MDGs	Millennium Development Goals
MEAD	Ministry of Economic Affairs and Development
MFAC	Ministry of Foreign Affairs and Cooperation
MoE	Ministry of Education
MoF	Ministry of Finance
MoH	Ministry of Health
MoJ	Ministry of Justice
MPFS	Macroeconomics and Public Finance Sector
MTFF	Medium Term Fiscal Framework
MWPW	Ministry of Water and Public Works
NCBA	National Cooperative Business Association
NEMP	National Environmental Management Plan
NGO	Non-government Organisation

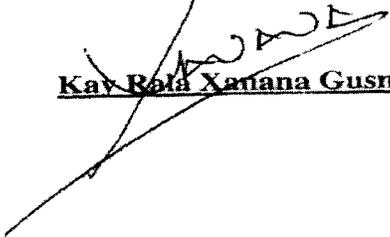
NICs	Newly Industrialised Countries
NRM	Natural Resources and Minerals
NTB	National Tourism Board
ODG	Office of Director-General
PA	Poverty Assessment
PNA	Protected Natural Area
PPA	Participatory Potential Assessment
SEP	Small Enterprise Project
SMEs	Small and Medium Enterprises
SSTL	Suco Survey of Timor Leste
STD	Sexually Transmitted Disease
STI	Sexually Transmitted Infections
TB	Tuberculosis
TBA	Traditional Birth Attendant
TEC	Trade Exposition Centre
TERADP	Timor Economic Rehabilitation and Development Project
TFET	Trust Fund for East Timor
TLSS	Timor Living Standard or Household Expenditure Survey
TSA	Timor Sea Arrangement
UNAMET	United Nations Mission to East Timor
UNTAET	United Nations Transitional Administration in East Timor
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
UNOPS	United Nations Office of Projects Services
USAID	United States Agency for International Development
VLW	Village Livestock Worker
WB	World Bank
WSS	Water Supply and Sanitation Division
WTO	World Trade Organisation

Foreword

Our National Development Plan charts an ambitious path to transform the lives of our people. The process of preparing the Plan gave thousands of East Timorese, from school children to elderly people, the opportunity to think about the kind of future they want for themselves and for future generations. For so many of them – in government, in civil society and in communities all over the country – it was the first chance they have had to share their aspirations with others and to think broadly about our nation’s development.

The vision which sprang from people’s participation in the planning process encapsulates all that is fundamental to development – peace, security, freedom, tolerance, equity, improved health, education, access to jobs and food security. Making the vision real is a bold and challenging task. It will require a sustained and combined effort from the public and private sectors and from civil society. It will also require the sustained help of our development partners – bilateral donor countries, the United Nations family, the International Financial Institutions and non-government organizations.

I am honoured to have led the consultation with our people which fed so directly into the Plan and now, as President-elect, I am committed to ensuring that this Plan and all that it represents be translated into actions that will transform people’s lives. In the year 2020, I hope that we will look back with pride on the development path we followed from our Independence.



Kay Rala Xanana Gusmão

Foreword

As Chief Minister and Chair of the Planning Commission, I am privileged to have overseen the production of our country's first National Development Plan.

This Plan is another milestone in our long journey to build our new nation. In this journey we have faced many challenges, but none that we have failed to overcome. As full independence approaches we find our responsibilities increasing, and these bring with them a host of new difficulties and new challenges. But I am confident that as a Government and as a people, we will remain undaunted by the need to make hard choices. Our Plan reinforces this belief.

As our struggle for independence is transformed into our striving for development, we continue to honour all the sacrifices that have been made by our people to bring us to this moment in our history, as we finally fulfil our destiny as a free people. The National Development Plan demonstrates that we remain faithful and true to the ideals that have for so long guided us, showing us the path we may follow to achieve our vision for the future of our nation.

Our planning for the medium-term will also enable donor agencies to effectively plan their programs for East Timor over the medium-term. As a Government we uphold principles of accountability and transparency, and the open, participatory and inclusive nature of our planning process is clear evidence of this. Moreover, just as the Government is keen to satisfy external agency requirements for accountability, each of our departments is learning how better to satisfy, and be accountable to, its own clients – the people of East Timor – the public who ultimately own, use and benefit from services Government provides.

East Timor's first National Development Plan reflects my Government's absolute commitment to involving all East Timorese in a planning process that will benefit all East Timorese. Over 120 Government officials have worked tirelessly throughout the planning process, in what was to many a new experience of learning by doing. Led by my team of Ministers, they examined, they analysed, they discussed and they debated the issues and problems now confronting East Timor. In the process of searching for solutions, we moved beyond the notion of looking for ways of how to better serve the public, to involving the public in the design of the service itself; the shape of services that they will actually receive over the next five years. We invited representatives of the Church and members of Civil Society, national and international NGOs, the private sector and public interests groups to become involved in a suite of National Sector and Cross-Sector workshops led by Government to help debate and formulate policy options, program priorities and implementation strategies for the National Development Plan.

Given the time-frame, what they have collectively accomplished is truly impressive. I must commend all involved and especially the Secretariat and staff of the Planning Commission. In particular, I pay tribute to our colleagues in the international community for their assistance. They stood by us in the past, and they stand with us now. I know we can rely on their friendship and solidarity for many years to come as we all work together to develop our new nation.

Mari Alkatiri

1st May 2002

VISION

FOR THE NEXT GENERATION, IN THE YEAR 2020

- ◆ East Timor will be a democratic country with a vibrant traditional culture and a sustainable environment;
- ◆ It will be a prosperous society with adequate food, shelter and clothing for all people;
- ◆ Communities will live in safety, with no discrimination;
- ◆ People will be literate, knowledgeable and skilled. They will be healthy, and live a long, productive life. They will actively participate in economic, social and political development, promoting social equality and national unity;
- ◆ People will no longer be isolated, because there will be good roads, transport, electricity, and communications in the towns and villages, in all regions of the country;
- ◆ Production and employment will increase in all sectors – agriculture, fisheries and forestry;
- ◆ Living standards and services will improve for all East Timorese, and income will be fairly distributed;
- ◆ Prices will be stable, and food supplies secure, based on sound management and sustainable utilization of natural resources;
- ◆ The economy and finances of the state will be managed efficiently, transparently, and will be free from corruption; and
- ◆ The state will be based on the rule of law. Government, private sector, civil society and community leaders will be fully responsible to those by whom they were chosen or elected.

EXECUTIVE SUMMARY

INTRODUCTION

1 The first National Development Plan (the Plan) for East Timor is a watershed event in the history and development of the world's newest nation. It is the first time that the people of East Timor have voiced their views about the future of their nation, based on democratic ideals and self-determination. The Plan has been a participative process, involving constituents in every sector of the economy to identify the problems they face and to suggest solutions to those problems. A vast number of people across the country participated in surveys and meetings to help shape a "national vision" for the new country. A Countrywide Consultation was conducted to reach thousands of people in every district and walk of life, resulting in the vision presented at the outset of this document

2. This planning document represents the views and efforts of those individuals who came together as "working groups" assisted by teams of planning consultants under the Planning Commission. It is important to emphasize that the Plan is the work of East Timorese people. For many, it is their first experience of planning on such a scale. It represents, therefore, the first important step in a process through which the development plan grows, matures, and improves over time.

3. The people of East Timor have many expectations, but these focus strongly on two over-riding development goals:

- a) To reduce poverty in all sectors and regions of the nation, and
- b) To promote economic growth that is equitable and sustainable, improving the health, education, and well being of everyone in East Timor.

DEVELOPMENT STRATEGY

4. East Timor's Development Strategy as described in this plan is to design programs and pursue initiatives that systematically address its main development goals. The first set of tasks during this early transition stage is to establish government capabilities, enabling legislation, and the institutions required to pursue development priorities. These are significant challenges that become unmistakably visible in each of the Plan sector strategies where the ministries and their directorates emphasize these priorities.

5. A second set of priority tasks is for every sector of government to pursue development activities that help reduce poverty. These are very often interdependent with priorities of economic growth, through which the nation's productive capacity is strengthened to create new jobs and higher levels of earned income, and, in time, a vibrant middle class. As the Plan shows, many economic development plans cannot be implemented without legal foundations and



governance that ensures private sector opportunities with a national infrastructure to support growth. Each sector addressed in the Plan has identified programs or projects that can help alleviate poverty while also supporting economic development priorities.

6. A third set of priority tasks consists of an extensive list of barriers that face every sector and all government agencies. These barriers are monetary, social, cultural, and structural impediments to economic growth and to the nation's efforts to reduce poverty. Many sector-specific objectives are subsequently focused on reducing or eliminating these barriers, so that progressive development programs can be implemented.

7. The overall structure of the Development Strategy orchestrates these high-priority development tasks, recognizing that they must be pursued concurrently. The Plan represents two phases of development. In the short-term, legislation and institutional capabilities will be addressed, together with progress in infrastructure, education, and health. In the longer-term, development can accelerate on the basis of these foundations.

8. The short-term phase is also a time of fragile and uncertain development. It is a period when funds are scarce, there are few industrial opportunities for growth or employment, demand on all government resources far outweighs the ability to supply, and questions of trade, investment, and foreign relations are unresolved. The nation will face its most severe challenges during the early years after independence. The longer-term stage represents a time of promise, when oil and gas revenues may provide the monetary base required for sustained growth, and when the nation can emerge from its early adversities with a strong sense of hope.

9. As the Plan unfolds and the nation progresses, the plans, goals, and aspirations will change, mature, and improve. The Plan therefore represents a starting point, particularly as it begins to be implemented. This document emphasizes that the Plan itself is organic – alive and capable of growing – yet only if government nurtures it and empowers people to take ownership of their own development initiatives.

POVERTY REDUCTION STRATEGY

10. A Poverty Reduction Strategy is focused on improving the productivity of the poor by achieving strong economic growth within an enabling environment. This will catalyze and sustain contributions of the poor to national development. Government is faced with providing basic social and economic services to the poor, nurturing and promoting their entrepreneurial initiatives, and prohibiting discrimination based on gender, ethnic origin, language, or geographic location. These issues recur throughout the Plan.

11. Because poor people in East Timor are engaged primarily in agriculture (including fisheries and forestry), improving productivity in this sector is a high priority. Proposed initiatives include rehabilitation and construction of irrigation systems and their improved operation, introduction of water harvesting techniques, wider distribution of improved seeds of cereal crops, fruits and vegetables, improved livestock health, improved management of fishing, and sustainable management of forests and other natural resources. These initiatives will be undertaken with the participation of the communities that depend on them. Improvements in marketing and infrastructure are also planned.

12. The micro-enterprise segment of society (a substantial part of the informal economy) has been an important contributor to growth in developing nations. A large number of people work in micro-enterprises or pursue very small independent activities to subsist. Expansion of

opportunities and productivity improvements in this sector are crucial, not only for rural families but for those in urban slums. Both dimensions of poverty are addressed in this plan, including proposals for training, quality-improving technologies, support services, and micro-credit.

13. A critical requirement for poverty reduction is to strongly enhance opportunities in the formal private sector, where growth and employment can be achieved in manufacturing, construction, trade, transport, tourism, and many domestic services. Priority policies and legislation are being formulated to improve the private sector and the ability of East Timor to sustain both domestic and foreign investment.

14 Poverty reduction cannot occur without the provision of infrastructure that includes an effective network of roads and bridges, efficient seaports and airports, reliable electric power, a telecommunications system, and postal services. Agricultural and business developments are crucially dependent on this infrastructure, and trade, tourism, and foreign investment cannot be encouraged without it. Consequently, a poverty reduction strategy is an integrated process that requires a pervasive effort by government and international donors who will play a major role in assisting East Timor's development.

CAPACITY BUILDING FOR PLAN IMPLEMENTATION

15. Promoting economic growth to reduce poverty will require the government to facilitate the delivery of basic social and economic services. This delivery will itself require enabling laws and regulations, and the empowerment of the population through community management and participation.

16. Currently, East Timor needs virtually everything – infrastructure, technology, training, capital and access to markets. To build capacity to meet all these needs during the next five years is clearly impossible. Consequently, prioritising needs for capacity building is essential for planning, as is the sequencing of the introduction of activities designed to provide these needs.

17. The Plan presents the main areas for capacity building and training, in several of its programs, in different sectors. These programs address both short-term implementation needs and capacity requirements for the coming years, at the central, district and local levels. Capacity building will be based extensively on government partnerships with civil society organizations, the church, non-government organisations (NGOs), the private sector, traditional institutions, informal networks, and mutual-help groups, particularly at the village level.

18. Capacity building at the government level is crucial for East Timor. The vast majority of current civil servants are neither adequately experienced, nor trained for the roles they will have to undertake. To address this problem, the former Cabinet endorsed a comprehensive ten-year program for Governance and Public Sector Management developed by the National Planning and Development Agency (NPDA) in 2001, with support from UNDP. The Plan builds on, and develops this program, by stressing the need to develop organizational and managerial values within a framework that respects East Timorese cultural values, whilst pursuing open, cost effective and accountable systems of government.

19. The Plan sets out strategies for developing and strengthening institutions for the post-transition period. It outlines how capacity can be built to enable the Government to assist in the development of a market-based economy. For each sector, the plan also provides strategies for strengthening capacities in policy development, co-ordination, and the core skills required for management. It shows how the East Timorese government can provide an enabling economic environment, deliver appropriate services, and establish relevant legal frameworks during the

post-independence period, outlining how capacity can be built within the civil service for drafting legislation, developing policy and upgrading skills at different levels.

20. The need for political decentralization is stressed in East Timor's Constitution. The Plan requires that capacity be built for this, through the provision of training for the administration of regional offices in some of the ministries, backed up by regional coordinating bodies with representatives from government, community groups, NGOs and civil society organizations. To further these proposals, training is required to improve the management skills of district and deputy district administrators, local development officers, and sub-district coordinators. In addition, at the suco level, there is a need to develop programs to increase village capacity for plan implementation, and to provide support for developing capacity in local training institutions to provide sustainable assistance to local administrators. NGOs, church organizations and civil society groups can assist in this process, as well as developing civic education programs to facilitate local communities to monitor plan outcomes, in relation to their original "vision" statements in the Countrywide Consultation.

21. Entrepreneurial, technical, and vocational skills are lacking in every sector of the East Timorese economy. To meet their needs, the Plan argues for an extension of the current on-the-job training undertaken in informal economy workshops throughout the country, the design and implementation of basic training programs by employers in the formal sector, and a further development of existing donor and church programs in vocational training. In addition, community-based training centres are to be set up in the countryside, to train people in the skills needed in the local informal economy, and to provide advice on employment.

22. Currently, standards of education in East Timor are among some of the lowest in the world. Consequently, the Plan focuses on capacity building for reconstructing and developing the education system – through prioritising strategies for teacher training, increasing primary school enrolment, improving retention rates, modernizing the curriculum, and enhancing community involvement in the management of schools. In addition, one of the most difficult tasks for schools in the years ahead will be to extend both the use of Portuguese language and the standardization of Tetun for use in schools. Again, the Plan offers programs and projects through which this can be achieved. Most importantly, the Plan also details projects to design a literacy manual, to extend existing donor literacy campaigns, and to develop new campaigns for implementation by the Ministry of Education.

23. Standards of health in East Timor are poor, and existing health provision is weak. To build capacity in this area will be extremely difficult, and the focus necessarily will be on the provision and delivery of services to meet basic needs. The Plan presents policies, and short and longer-term strategies for this. It prioritises ongoing, long-term programs in child, maternal and reproductive health. It also focuses on current needs to build capacity for the provision of support services and management systems for the delivery of these programs.

24. Infrastructure is in a poor state, and capacity in this sector is extremely weak. This is an issue of overarching importance for all sectors of the economy and society, since infrastructure is a key determinant of agricultural productivity, poverty reduction, investment, human development and government capacity to deliver services. The Plan specifies detailed programs for building capacity in the key areas of water supply and sanitation, road reconstruction, and the restoration of basic transport and communication facilities. For the longer term, it specifies programs for the development of a sustainable power infrastructure, with an accompanying institutional framework.

25. A crucial area for East Timor's development is an effective judicial system. Developing the judiciary will require rapid capacity building to prepare proposals for legislation and draft legislation, in addition to preparing legal opinions and advice.

26. In most of the areas for capacity building outlined above, during the coming years, East Timor will need continuing international support. At least in the short term, to further capacity building and human resource development, there are positions which need to be filled by international advisers, working closely with local staff. For plan implementation, it is crucial that the knowledge and skills appropriate for the attainment of economic growth, poverty reduction and human development be transferred and developed in an East Timorese context.

MONITORING, EVALUATION, AND PLANNING REVIEW

27. The Plan is a starting point for a structured planning process that includes monitoring and evaluation as critical components of successful national development. Ensuring that policy objectives are met – through program and project activities – requires adherence to a sound process of monitoring and evaluation. In addition, such a process meets the requirements of government, donors and other stakeholders for transparency and accountability. The main outcomes of strengthened monitoring and evaluation capabilities are improvements in project implementation and management, but most importantly, improvement in the Plan itself.

28. An institutional planning process is presented in this Plan as one that empowers the nation's leaders with responsibility for strategic planning. The process itself must ensure continuity of monitoring and evaluation, provide timely feedback on actual performance, and provide realistic analyses of what the nation faces in the coming years. This planning process also will permit adaptation of the existing plan, its goals, objectives, and strategies.

29. The planning process should not be budget-driven nor subordinated to international financial mandates. Instead, it should address the social, economic, and human development priorities of East Timor and, with appropriate diligence, consider what can be realistically accomplished given budget constraints. Ministries and their directorates are part of this on-going process with incremental annual action plans and achievable performance benchmarks. A process of periodic monitoring and evaluation reporting is suggested with annual planning reviews under an independent government body overseeing implementation in co-operation with government ministers, civil society organisations and the major stakeholders.

MACROECONOMICS AND PUBLIC FINANCE POLICY FRAMEWORK

30. The sector vision focuses on growth, employment, improved living standards and better public services delivery. Sustaining the culture and environment are important. Sound and transparent economic and financial management is essential.

31. The starting point for independent economic management is difficult and a period of consolidation is needed, particularly as the United Nations withdraws, before longer-term development is likely to take hold. The continuing support of donors in the transition phase before significant oil revenues begin to flow will be important.

32. Several core sector goals have been identified. These relate to: capacity building; poverty reduction; economic growth; low inflation; employment growth; a stronger banking sector; strengthening the external situation; improving revenues to enhance self reliance; effectively

managing oil revenues; responsibly managing budget expenditures; and effectively managing budget financing, especially aid.

33. Broad guiding principles revolve around an open market economic system but with important strategic and regulatory roles for government. The private sector (including agriculture) is provided with important responsibilities in the development effort. Provision of equal opportunities and improving living standards are important. Preservation of the environment and traditions are also important. Economic management will be transparent and corruption free.

34. Many constraints have been identified as needing to be addressed in the policy formulation stage. Without being exhaustive these include: coping with social and physical destruction; recognizing difficulties in transforming subsistence agriculture; limited experience in economic management; low domestic revenue base; a very weak banking and credit sector; an increase in wage levels under UNTAET along with a very strong US dollar has weakened international competitiveness; the private sector is weak as is the institutional and legal environment in which it operates; education, health and infrastructure services all need big improvements to support the development effort.

35. A detailed policy matrix is presented where the eleven core goals are assigned policy actions and performance indicators to measure the success of policies over time. A full range of macro, micro and institutional policies will need to be effectively implemented if the sector goals are to be achieved. Important policies that are set out include: budget policies (revenues; expenditures and financing); monetary and currency policies; wages policies; trade and investment policies; institutional and structural policies as well as capacity building initiatives.

36. The chapter concludes by setting out likely program and project funding for the sector during the plan. Significant additional resources are not called for and relatively speaking the sector should use less national resources over time. A large number of new project initiatives have been set out, the great bulk of which relate to systems and human capacity building measures in the Ministry of Finance (MoF) and the Banking and Payments Authority (BPA).

MEDIUM TERM ECONOMIC AND FINANCING OUTLOOK

37. This chapter provides the medium term economic and financing outlook. Many plans fail because they make unrealistic assessments of economic conditions and of domestic and foreign resources available. The links between medium term plans, budgets and economic policy frameworks are important ones. A base outlook for key components of the macro-economy is presented and indicates:

- a) Largely due to the phased withdrawal of UNTAET and TFET, economic growth is projected to be negative in 2002 and 2003, before commencing recovery in 2004. By the end of the plan there are prospects for solid, broadly based growth of 6% p.a.;
- b) The worst hit sectors during the downturn in late 2002/2003 are expected to be Transport, Communications, Trade, Hotels, Restaurants, Utilities, Construction, Finance, Rents, Business and Government Services;
- c) The sharp contraction is a reflection on the recent economic management period and makes a good argument for ongoing donor budget and project support to help smooth what will be a difficult transition;

- d) Sharp reductions in formal unemployment will be challenging to achieve. Excluding agriculture, around 40,000 private sector jobs will need to be created over the course of the plan if the open unemployment rate is to halve. Agricultural and informal employment will remain important social safety nets;
- e) Prices are expected to remain stable with inflation averaging 2% to 3% per annum. Public sector wage growth will be targeted at levels below that of inflation;
- f) Domestic revenues while growing will remain small. For FYs 2003 and 2004, donors are being asked to contribute around US\$40 million per annum to recurrent and capital budget support. Oil revenues are expected to strengthen sharply from FY 2005 and to average almost US\$100 million a year in the last 2 years of the Plan;
- g) Total sources expenditure will contract sharply over the course of the plan as UN and TFET contributions withdraw. After rapid growth in FY 2003, CFET expenditures are targeted to grow smoothly at 8% per annum nominal for the remainder of the Plan.

38. The Plan asks donors to maintain bilateral projects at around US\$75 million per annum throughout the Plan period. This is higher than levels previously discussed but is critical both for short-term economic management and long-term nation building. It also presents a case for significantly changing the composition of CFET expenditures over time, especially to find more resources for the key plan priorities of agriculture, education, health and infrastructure development. During the plan the BPA will develop the capacity to manage an independent monetary and currency policy.

39. Providing the stance of no public sector borrowing is maintained the external situation should remain manageable with a reasonable build-up in oil revenues saved in the offshore account (estimated to be US\$84 million by end 2007).

40. The Plan presents policies for the planned utilization and saving of oil revenues so as to preserve capital and earnings values for future generations. It also outlines aid policies and approaches to be pursued, which are critical both for short and medium term economic and financial management.

POLITICAL DEVELOPMENT, FOREIGN RELATIONS, DEFENCE AND SECURITY

41. The development of an effective administrative and governance structure to serve the needs and interests of the people and the nation is one of the most critical national priorities. Given the existing environment the priority medium-term programs will have to be the establishment and strengthening of the organs of state and of public administration, laying the foundations of good governance, creating the avenues for popular and community participation, developing the legal and regulatory framework, building the human resources capacity for policy formulation and execution as well as service delivery, strengthening oversight institutions and fostering the press and civil society.

42. The Plan emphasizes that transparency in governance is essential, including development of public information programs for civil service, activities of Parliament, and functions of the ministries. This will be reinforced by programs that reintroduce Portuguese and standardize Tetun as working languages of Parliament and public administration.

43. Decentralization and participation are critical to mobilize regional, community, and civil society organizations and entities. The Plan presents programs that will empower communities and strengthen grass-roots democracy. These are inclusive strategies that preserve the opportunity for everyone to have a voice in self-government.

44. The Plan also addresses civil priorities, such as identifying veterans and providing training and other assistance to re-integrate them into society. The plan underlines the importance of utilizing networks of diaspora organizations to represent East Timorese interests abroad.

45. The importance of a legislative agenda cannot be overstated as vital to the nation's ability to establish a society based on the rule of law, to foster domestic and foreign investment, to support private enterprise growth, and to protect the interests of the impoverished and disadvantaged.

46. The Plan includes the creation of an Ombudsman's office to raise the level of awareness of citizens' rights and respect for the law, to defend citizens from any abuse of power by public administration entities, and to safeguard against practices of corruption, nepotism and other abuses of power.

47. Not least of all, the Plan articulates development of protective services through the creation of refuge centres and support systems for victims of violence, and by creating programs for assistance and training of youth and women, particularly those who have become displaced by conflicts and inequitable social barriers.

POVERTY REDUCTION, RURAL AND REGIONAL DEVELOPMENT

48. More than two fifths of East Timorese live in poverty. The poorest households are those with little land, and no education. They are most likely to be farmers and fishers. More than three-quarters of the population live in rural areas. Poverty also occurs unevenly, with the western and central areas being poorer than the eastern areas

49. The main goals of poverty reduction within the Plan are to achieve rapid economic growth to deliver training and health services, establish social safety nets, and create skilled and professional human resources for an effective use of labour. Rural development will be integrated and regionally balanced, and governance for this development will be competent, efficient, accountable and transparent.

50. Rural and regional development will ensure the involvement of households and communities in all development activities in the villages. It will be integrated, equitable, and non-discriminatory.

51. The main resource constraints for rural development are detailed in the Plan. They focus largely on social and gender issues, but also list the main areas for capacity building, both within the Government and civil society organisations. Infrastructure constraints are viewed as particularly severe, limiting access to markets. The private sector has no meaningful framework for enabling rural development, and governance is restricted by limited co-ordination, inadequate targeting, a lack of transparency, and limited accountability.

52. Based both on the overall strategy for poverty reduction, outlined in chapter four, and on the mainstreaming of poverty in the Plan, the most important areas through which poverty can be reduced in the rural sector are presented and elaborated. Strategies are outlined for the creation of

economic opportunity, the provision of specific social services, the enhancement of security, capacity building for disaster preparedness, the provision of assistance to vulnerable groups, the empowerment of villages and communities, and the creation of equal opportunities for women in work, training and participation in business and private sector organisations.

53. Balanced regional development will be achieved through focusing on reducing imbalances in education, strengthening the economic bases of districts, improving access to infrastructure for relatively disadvantaged areas, allocating central government resources to districts based on population, land area, level of development and specific locational problems.

54. To promote balanced regional development, strategies are presented for strengthening the civil service locally, and for improving the immigration service and national archives.

55. Strategies for a fuller use of rural labour are outlined. These include improving the functioning of the labour market through employment exchanges, business consultation forums and the use of the media. A labour market database will be established, and manpower planning introduced.

HUMAN DEVELOPMENT: EDUCATION AND HEALTH

56. Human development priorities for both education and health are concerned with short-term reconstruction and long-term sustainable development. These represent two phases of program activities, which the Plan has endeavored to address as among the most important national goals of East Timor.

57. In the short-term over a two to three year period, education strategies will aim to consolidate the efforts and achievements of reconstruction. This will be done through rationalizing educational provision in relation to the needs of different areas of the country, and by developing human resources within the educational sector as a whole. Institutional capacity will be strengthened within the ministry, to promote reforms and to plan and develop educational programs.

58. In the longer term, education strategies will aim to promote reforms in key areas of the sector, as well as developing measures for institutional strengthening to achieve the provision of universal primary school education. Curricula will be designed and implemented, promoting high quality teaching. Institutional capacity will be strengthened with the aim of an efficient management of the educational system.

59. The education programs proposed in the Plan reflect a priority need to recruit and train competent teachers at all levels, but essentially for primary schools where the next generation of children can emerge as literate individuals with realistic opportunities to pursue higher education, meaningful jobs and careers. In line with teaching needs, programs focus on development of school facilities and educational materials, systematically improving teacher-student ratios, access to texts, support for school sports, and cultural development.

60. East Timor has one of the lowest literacy rates in the world. The Plan presents programs and projects for designing literacy manuals, and implementing campaigns to improve adult literacy, with a particular emphasis on women

61. Health priorities are among the most crucial in the Plan. Development strategies have been devised to emphasize the importance of providing adequate access to primary health care, focusing on prevention and clinical support in underserved areas. Health planners will develop a

system of primary health care, universally accessible to individuals and families in the community through household participation, and at a cost that the community and country can afford to maintain at each stage of its development.

62. Longer term health sector priorities are to ensure that health providers and clinical specialists can sufficiently meet the needs of the country's health system within the framework of overall social and economic development. In order to accomplish this, short-term activities include recruitment and staff training activities, a national plan for regional and rural health services, and an epidemiological approach to preventive medicine, inoculations, public health information, and improved hygiene.

63. A major concern is to solve the situation of women disadvantaged particularly by the mass displacement during the Indonesian period, but also suffering from domestic violence. Currently there are no laws either ensuring the protection of women's fundamental rights or addressing the social and cultural obstacles favoring men's access to opportunities.

64. The goal of promoting gender equality and empowering women must entail changes in attitudes, government social institutions and private sector practices. The overall strategy in the Plan is focused on mainstreaming gender equality in all areas and at all levels of education and health, thus ensuring that policies and programs respond to the needs and interests of women as well as men, and distribute benefits equitably.

65. Gender objectives in education and health emphasize the need for gender awareness campaigns at all levels, to remove obstacles to a full participation of girls in the educational process, and to ensure women's rights to health. This is particularly focused on reproductive health and on the prevention of health hazards.

AGRICULTURE, FISHERIES AND FORESTRY

66. The agricultural sector is pre-eminent, with the majority of the population deriving their livelihood from agricultural activities. The key position of agriculture in the economy means that there remains a strong imperative to ensure food security, rebuild to provide employment and income generating opportunities, and to expand opportunities for exports.

67. Agriculture in 2001 was the main source of income in 94 percent of sucos. Forty one percent of East Timor's population suffers from poverty, with those in rural areas more likely to be experiencing it. Agricultural policy and strategies, therefore, need to recognize the likelihood of seasonal food shortages and accord suitable priority to programs to overcome those shortages. Unfortunately, East Timor has little or no comparative advantage in agricultural commodities, and current wage levels coupled with the US dollar as the medium of exchange will constrain efforts to become internationally competitive.

68. The Plan presents strategies to efficiently deliver services to agricultural, fishing and forestry communities that improve their productivity and income-earning potential. These will also improve social welfare in rural areas and enhance human capital. Export development will be an uphill struggle, yet the Plan identifies a broad range of initiatives that provide funding and assistance opportunities to alleviate poverty as a first priority, and systematically enhance domestic livelihoods.

69. Agriculture and rural development continue to receive support under emergency rehabilitation funding arrangements, through TFET, bilateral donors and multilateral agencies.

They are substantial, yet as the Plan illustrates, they are not sufficient to meet East Timor's pressing needs.

NATURAL RESOURCES AND ENVIRONMENT

70. East Timor is relatively poorly endowed with natural resources apart from the oil and gas reserves of the Timor Sea. Fishery stocks are poorly understood, but might also comprise an important economic resource. Strategies proposed in the Plan recognize these limitations, but seek to develop sustainable domestic capabilities that optimize natural resources while also protecting the natural environment.

71. Natural resource development, environmental interventions, and the primary goals of poverty reduction and economic growth are inextricably linked. These are addressed within the sector plans that include: (1) improvement in people's health due to poor access to resources; (2) enhancement of the livelihoods of poor people, particularly in rural areas where they depend on land, water, forests and biodiversity; and (3) reduction of vulnerability to natural disasters such as violent storms, floods and fires.

72. The Department of Natural and Mineral Resources is not an implementing agency, but it is the administrative authority for pursuing legislation relating to minerals, energy and extractive industries, and thereby regulating development to utilize the nation's resources efficiently, whilst preserving its environment.

73. Programs within the Plan reflect environmental and resource priorities, and the need to encourage private development without exploitation. This responsibility requires inter-ministry cooperation, particularly concerning oil and gas resources and the related infrastructure that is essential to support national development.

INDUSTRY, TRADE AND THE PRIVATE SECTOR

74. The programmatic initiatives of the sector are divided into five divisions, each concerned with policy and regulatory priorities and capacity building that encourages private development of industry, investment, tourism and trade. Successful private sector development will be a key driver of economic growth and poverty reduction. In the near-term, the principal role of government will be to provide the best possible enabling environment for private sector development.

75. The transition to economic independence will be the main challenge confronting government during the next five years. This is particularly true as international spending may decline over the next few years, and revenues from oil and gas production in the Timor Sea may then subsequently increase. Both of these changes pose risks and opportunities to private sector development. The Government has committed itself to a market-based economy, but during the early years, this will be difficult to achieve without an open approach to foreign investment and foreign trade that will help build East Timor's international competitiveness.

76. During the UNTAET period, government policy has successfully fostered a rapid recovery of private investment and business activity, such that the supply of the vast majority of goods and services has been restored. Consequently, the first task of government in this sector is to continue this momentum and, in terms of early actions, provide positive signaling effects to the market.

77. The largest portion of East Timor's private sector is made up of its micro-enterprises and SMEs. Accordingly, their specific needs formed the backdrop of most of the policy options undertaken during the preparation of the Plan. Specific attention is given in the NDP to strategies that would most equitably distribute income and make available services to rural areas, thus addressing the priority goal of poverty reduction. These strategies are linked to the need to increase demand for domestic agricultural produce, and to improve domestic market linkages through consistency and quality of supply.

INFRASTRUCTURE

78. Infrastructure is an issue of overarching importance to society. It includes the physical capabilities and service systems that provide the population with the essentials of electric power, water, sanitation, postal services, telecommunications, roads, air and sea transport facilities, and various support services. Infrastructure has perhaps the strongest cross-sectoral implications for national development. Having an effective system of physical infrastructure and services is crucial for agricultural productivity and poverty reduction, but it is also a key determinant of business investment, is vital to human development, and the foundation for private sector development.

79. Although significant progress has been made to restore infrastructure, the quality and level of services remain woefully inadequate. The infrastructure sector plan emphasizes national priorities for economic development and a strong commitment to poverty reduction throughout its department activities, but the first priority is to restore or establish required physical capabilities and public services.

80. This focus will not detract from efforts to meet the needs and aspirations of those disadvantaged by poverty, remoteness and difficulty of access to infrastructure services. On the contrary, the ten divisions represented as the infrastructure sector in the Plan have systematically proposed programs that account for these needs.

81. The ultimate responsibility of each directorate is to provide a program of infrastructure development that ensures safe services, equitable prices, and maximum opportunities for economic development that improves human welfare. Most programs, however, are capital intensive and the Plan presents alternatives for development, including private sector investment, foreign investment, build-operate-transfer (BOT) options, and public service contracts. Sector strategies are heavily reliant on these alternatives and on subsequent assistance from the international donor community.

PART 1

VISION AND STRATEGIES

- Chapter 1. INTRODUCTION
- Chapter 2. VISION, GOALS, PRINCIPLES AND INDICATORS
- Chapter 3. THE DEVELOPMENT STRATEGY
- Chapter 4. POVERTY REDUCTION STRATEGY
- Chapter 5. CAPACITY BUILDING FOR PLAN
IMPLEMENTATION
- Chapter 6. MONITORING, EVALUATION AND REVIEW



1. INTRODUCTION

“The people of East Timor prepared the National Development Plan. It belongs to them and reflects their values, needs, ideas, aspirations and priorities.”

BACKGROUND

1.1 The release of the National Development Plan (the Plan) for the new nation of East Timor is a milestone in its history. It is the first time in more than 450 years that the East Timorese have participated as free people in formulating a twenty-year vision, identifying key development challenges, and evolving strategies and programs of action for the next five years (2002 – 2007) to take the nation forward economically, socially, and politically. The Plan is not the end of the planning and development process; it is only the beginning. The important work of preparation and implementation of annual action plans, including programs and projects, has begun and will proceed during the next five years.

THE PLANNING PROCESS

1.2 The process of formulation of the Plan began in earnest in September 2001, after the Second Transitional Government took office. A range of initiatives from the Government, civil society organizations and ordinary men and women fed into the planning process. These included activities within (a) the Poverty Assessment; (b) the Countrywide Consultation undertaken by the Consultative Commission for Civil Society on Development (CCCS); (c) intensive work over a period of three months by Government officials in eight sector working groups, each chaired by the relevant Ministers; and (d) discussions and feedback at, and following, a two-day stakeholder workshop on the Plan.

1.3 The Poverty Assessment (PA) comprised three components:

- c) a Suco Survey (SSTL) covering all the sucos (villages) in the country, which compiled an inventory of existing social and physical infrastructure, the economic characteristics of each suco, and the coverage of public services, based on information obtained from suco and aldeia (hamlet) chiefs, teachers and other local leaders;
- d) a Household Expenditure Survey (TLSS) which obtained information from the members of a sample of 1,800 households spread throughout the country, and collected data on household demographics, housing and assets, household expenditures, agriculture and the labour market, basic health and education, subjective perceptions of poverty, incomes and social capital; and
- e) a Participatory Potential Assessment (PPA) that assisted the communities in 48 aldeias in the 13 districts of the country to take stock of their assets, skills and strengths, identify the main challenges and priorities, and formulate strategies for tackling these within their communities.

- f) The Plan draws upon the results of the PA.¹ The SSTL Report was released in October 2001 whilst the reports on the PPA, the TLSS, and the composite PA (incorporating the findings from all three components), are expected to be published in mid-2002.

1.4 The Countrywide Consultation undertaken by the CCCS covered more than 38,000 East Timorese citizens – men, women, secondary school students and youth. The consultation captured the twenty-year vision (to the year 2020), as well as current priorities, initiatives the people can take, and how they think civil society and the Government can address their concerns. The results are incorporated in the vision, goals and strategies as well as in the sector interventions of the Plan. A popular version of the Plan entitled “East Timor 2020 - Our Nation, Our Future” outlining the vision, priorities and expectations of the population is being released simultaneously.

1.5 The eight working groups convened to work on the Plan involved more than 120 senior officials of the Government, including Ministers and Vice Ministers. They worked long days and weekends to formulate a homegrown Plan that takes into account the aspirations of the people, present realities and future prospects. Preparation of the *State of the Nation Report* has been the first major task accomplished by the working groups². It enabled the East Timorese to take stock of the position in which the nation finds itself prior to its independence, and provides the backdrop to the Plan. The working groups formulated a 20-year vision (to 2020), presenting the goals, guiding principles, strategies, policies, programs, projects and legislation necessary for the country to move ahead with its development over the next five years. There was a high degree of congruence between the vision and priorities identified by the people in the Countrywide Consultation and those formulated by the working groups. The working papers of the groups were presented by Ministers, and discussed at a two-day workshop for stakeholders, including NGOs, civil society organisations, interest groups, the Church, political parties and donors. The feedback from the workshop has been incorporated into the Plan.

1.6 The people of East Timor prepared the Plan. It belongs to them, and reflects their values, needs, ideas, aspirations and priorities. It is an amalgamation of inputs from the various stakeholders. The extent of citizen participation and the inclusive process adopted in preparing the Plan are unique, especially for an incipient country. Most importantly, this process has been crucial in building confidence and capacity among East Timorese Government officials, civil society organisations and communities.

ORGANIZATION OF THE DOCUMENT

1.7 The Plan provides a road map for the development of the country over the next five years within a twenty-year perspective. It is presented in three parts. Chapters 2 to 6 comprising Part I of the Plan provide an overview of the twenty-year vision, goals, strategies, and capacity development needs of East Timor, and monitoring, evaluation and review arrangements for the Plan. Part II presents a synopsis of the Macroeconomic Policy Framework and Medium-term Economic and Financing Outlook in Chapters 7 and 8, which are prepared by the Working Group on Macroeconomics and Public Finance. The remaining sector chapters prepared by the Working Groups on Political Development, Foreign Relations, Defence and Security (Chapter

¹ Only the preliminary results from the Household Expenditure Survey were available and fed into the Plan.

² Unless otherwise specified all the figures quoted in the Plan are from the State of the Nation Report.

9), Poverty Reduction, Rural and Regional Development (Chapter 10), Social and Human Development: Education and Health (Chapter 11), Agriculture, Fisheries and Forestry (Chapter 12), Minerals and Natural Resources and the Environment (Chapter 13), Industry, Trade and the Private Sector (Chapter 14), and Infrastructure (Chapter 15) form Part III of the Plan. The Plan organises and presents the outputs of the East Timorese as faithfully as possible.

2. VISION, GOALS, PRINCIPLES AND INDICATORS

“The formulation of the Development Vision for the country to the year 2020 was carried out in full consultation with the people, civil society organisations and government officials. The vision is an amalgamation of the inputs and tries to reflect accurately and fully the aspirations of all East Timorese”

THE LAND AND THE PEOPLE

2.1 East Timor is situated on the eastern part of the island of Timor, the easternmost of the Lesser Sunda Islands. It is bordered on the west by the Indonesian province of Nusa Tenggara Timur (or West Timor). The Savu Sea and the Strait of Wetar lie to the north of the island while Australia is to the south, about 500 kilometres across the Timor Sea. Also, the enclave of Oecussi in the western part of Timor Island is a part of the national territory of East Timor, as are the islands of Ataúro and Jaco.

2.2 The country has a land area of approximately 14,610 square kilometres (sq km), with a surprisingly varied topography and a diverse ecology. A core of rugged hills and mountains form a mountainous spine that divides the northern part of the country from the southern region. About 21% of the land is less than 500 metres above sea level, 41% between 500 and 1,000 metres and the rest (35%) more than 1,000 metres above sea level, with the last including Mount Tatamailau at approximately 3,000 metres. Around 44% of the territory has a slope of approximately 40% which, combined with heavy rainfall, contributes to soil erosion. The rainfall pattern is varied with the mountains receiving more rain than the coastal plains. The southern region receives more rainfall (2,000 millimetres or more) and has two harvests, while the northern part with less rain (between 500 to 1,000 millimetres) often has one harvest. The country is affected by the periodic El Niño-related weather anomalies.

2.3 The climate is hot, with an average temperature of 21°C, and a high humidity (about 80%). The dry months from May to October experience moderate winds and slightly milder temperatures – about 18°C on the coastline and 10°C or lower in the mountains. During the monsoon season (November to April), the rivers become torrents due to the extremely high rainfall in the mountains.

2.4 The country is organized into 13 districts, 67 postos (sub-districts), 498 sucos (villages) and 2,336 aldeias (hamlets). The districts have been grouped into three regions – the enclave district of Oecussi and the border districts of Bobonaro and Covalima forming the Western region, the districts of Aileu, Ainaro, Ermera, Liquica and Manufahi in the Central region, and the districts of Baucau, Lautem, Manatuto and Viqueque in the Eastern region – and the capital Dili. At present, the local government (administration) is organized at the district and sub-district levels although the traditional structures at the suco and aldeia levels continue via suco and aldeia chiefs. The districts have District Administrators with a small complement of staff and sub-district co-ordinators at the postos.



2.5 The last population census of East Timor Province was in 1990, and a population census of the new country has yet to be conducted. The 1990 Census placed the population at 747,557, which included 47,000 non-East Timorese (mainly Indonesians from other provinces of whom almost half were from West Timor). The rate of growth of population at about 2.5% per annum was high compared to that in the rest of Indonesia. The capital, Dili, had more than 14% of the population. The population density ranged from 48 persons per sq km in the Eastern region to 52 in the Central region with Dili at 271 persons per sq km. Estimates from the 2001 Suco Survey place the population at about 790,000 in mid-2001, with females accounting for 49.75% of the total. This figure does not include the approximately 120,000 East Timorese who were then still living in refugee camps in Indonesian Timor, following the aftermath of the 1999 paramilitary rampage. Since then, many of these refugees have returned to the country. In April 2002, some 60,000 refugees remained in the camps, but many are returning, with the approach of independence. The proportion of the population in Dili appears to have increased considerably in recent years, and unofficial estimates place it at more than 20% of the total. More than three-quarters of the population live in rural areas.

2.6 East Timor has a young population, with about 48.1% below the age of 17. This will place a considerable demand on education and health services, at least for the next decade. Also, the relatively high fertility rate implies a continued high population growth rate in the next decade or more, unless policies are introduced for family planning and health education. The labour force participation rate is about 74% overall with that for women estimated to be more than 50%. About three-quarters of those employed are in agriculture. Open unemployment, a recent phenomenon especially among youth, is in excess of 16%.

2.7 The ethno-linguistic diversity of the population is significant, with more than 30 languages or dialects in use. The major local languages include Tetun, Mambae and Macassae, each spoken by more than 10% of the population. The main language, Tetun, is understood by a large majority (about 80% according to some estimates) of the population, with about 40% able to understand and use Indonesian, approximately 5% able to understand Portuguese, and about 2% English. Indonesian was the working language for the government and the medium of instruction in schools during the more than 20 years of Indonesian rule. The new official languages are Portuguese and Tetun, with Indonesian and English accorded the status of working languages. This poses unique challenges of communication within the Government, between the Government and the people, and within the education system.

THE ECONOMY

2.8 The economy of East Timor was devastated by the 1999 violence. It has recovered somewhat in 2000, and further in 2001. The nominal gross domestic product or GDP, which is a measure of the value of all goods and services produced in the country at prevailing prices, was US\$321.2 million in 2000 (Boston Institute) and US\$380.0 million in 2001 (IMF)³. The GDP declined by 2.1% in 1998 and 34% in 1999; but grew by 15% in 2000 and 18% in 2001. The size of the real economy (i.e. GDP at constant prices or adjusted for price inflation) in 2001 was only about 88% of the 1997 level (IMF). Based on population data provided by the Government Statistics Office, nominal per capita non-oil GDP was estimated at US\$412 in 2000 and US\$452

³ The estimates of GDP and population vary between different sources and may not be strictly comparable. One set of estimates are available from the Boston Institute for Economic Studies (USA) and another from the International Monetary Fund (IMF).

in 2001 (IMF).⁴ This places East Timor in the low-income country category by international standards.

2.9 In 2001, the output of the agricultural sector accounted for 26.5% of non-oil GDP, with manufacturing industry at 2.5%, construction 13.3%, trade, hotels and restaurants 8.3%, transport and communications 7.4%, finance, rents and business services 6.3%, and Government services 33.5%. Almost three-quarters of the labour force (73.8%) were employed in agriculture and 16.8% were openly unemployed. All other sectors combined employed less than 10% of the labor force. Private consumption has been very high, reaching 100% of GDP in 2000, and private investment has been low. The large net external inflows (aid) played a significant part in the financing of domestic consumption and investment in the two years.

2.10 Inflation was very high in 1998 (80%) and 1999 (140%), but decelerated in 2000 (20%), reaching a low 3% in 2001. Data on recent private sector wages is poor. However, evidence from the 2001 Suco Survey indicates that wages for the unskilled in the coffee industry may have tripled since 1999 from around US\$1 a day to more than US\$3 a day. Anecdotal evidence suggests that these increases may have fed through into wage increases elsewhere in the private sector, especially in skilled areas. Allowing for inflation, real wages probably have remained the same since 1999.

THE DEVELOPMENT VISION

2.11 The formulation of the development vision for the country to the year 2020 was carried out in full consultation with the people, civil society organizations and government officials. The vision presented below is an amalgamation of their different inputs, and tries to reflect accurately and fully the aspirations of all East Timorese:

2.12 For the next generation, in the year 2020:

- a) East Timor will be a democratic country with a vibrant traditional culture and a sustainable environment;
- b) It will be a prosperous society with adequate food, shelter and clothing for all people;
- c) Communities will live in safety, with no discrimination;
- d) People will be literate, knowledgeable and skilled. They will be healthy, and live a long, productive life. They will actively participate in economic, social and political development, promoting social equality and national unity;
- e) People will no longer be isolated, because there will be good roads, transport, electricity, and communications in the towns and villages, in all regions of the country;
- f) Production and employment will increase in all sectors – agriculture, fisheries and forestry;
- g) Living standards and services will improve for all East Timorese, and income will be fairly distributed;

⁴ The GDP from oil and gas was estimated to be US\$71.4 million in 2000 and US\$63.9 million in 2001.

- h) Prices will be stable, and food supplies secure, based on sound management and sustainable utilization of natural resources;
- i) The economy and finances of the state will be managed efficiently, transparently, and will be free from corruption; and
- j) The state will be based on the rule of law. Government, private sector, civil society and community leaders will be fully responsible to those by whom they were chosen or elected.

DEVELOPMENT GOALS

2.13 This vision is to be realized through the achievement of goals and development targets (quantitative and qualitative indicators). The Countrywide Consultation undertaken by the CCCS identified education, health and agriculture as the population's main priorities for the development of the country. Responding to the wishes of the people, the Government also accords high priority to these sectors. The main goals include the following:

- a) Improve the education, health and nutritional status of the people of East Timor; promote gender equality and the empowerment of women; improve the economic, social and cultural well being of individuals, families and communities in East Timor; create human resources that are skilled and professional in accordance with the interests and talents in each field; and ensure equal opportunities to obtain work and effective utilization of labour.
- b) Transform the subsistence economy into a market economy; achieve food security; and protect the environment.
- c) Achieve and sustain rapid economic growth, utilizing to the optimum the country's human, financial and natural resources; with low inflation and increased employment adequate to cater to the growing labour force; a stronger banking and finance sector; maintain a competitive real exchange rate with more exports and less imports; create equitable business opportunities and increase incomes, especially in rural areas.
- d) Reduce poverty among women and men; establish a social safety net to reduce the burden on those in society who are unable to work/help themselves.
- e) Promote private initiatives, innovation and investments by creating enabling and supportive environments - including policies, legislation and regulations, reliable supplies of electricity, water, roads and transport, marketing and banking systems, and a competent, productive and disciplined labour force.
- f) Secure and maintain the unity, territorial integrity and sovereignty of the nation; create and maintain durable internal peace, security and stability; prevent crime and involve the community in the reduction of crime; and make the country attractive and safe to citizens and visitors.
- g) Promote integrated rural development to generate remunerative employment and sustainable livelihoods, increase rural incomes, reduce poverty, accelerate economic growth and reduce the gap between rural and urban areas.

- h) Promote an orderly development of cities and towns that are pleasant (e.g. with parks and playgrounds), not crowded, affordable and friendly to the environment.
- i) Achieve balanced regional development to reduce poverty, improve the lives of East Timorese in all regions, enhance and exploit complementarities between regions and agro-ecological areas, accelerate economic growth, and reduce regional disparities.
- j) Achieve growth in government (budget) revenues to improve financial independence; effectively manage oil and gas revenues and savings to benefit present and future generations; and ensure responsible, efficient and productive management of government (budget) expenditures to promote poverty reduction and growth.
- k) Develop and administer an effective, accessible and impartial system of justice, which is prompt and transparent, and in conformity with the positive values and cultural heritage of East Timor; create an effective and independent system to oversee, monitor and remedy the potential excesses of the government and its functionaries.
- l) Strengthen an already robust civil society, and create opportunities for its constructive engagement and participation in national life, and enhance the participation of citizens in public and national affairs.
- m) Foster a culture of respect for human rights (particularly for women, children and other vulnerable groups, including the poor) and the rule of law; create public trust in a fair and just public administration; establish control mechanisms to monitor levels of responsibility amongst government officials and public authorities.
- n) Promote good governance through popular participation; a responsible and responsive government including a lean, efficient, effective, accountable and transparent civil service and effective, professional, non-political defence and police forces; a decentralized administration with simple and transparent norms, so that governance and public administration is closer to the people; a socially responsible private sector; transparent and accountable civil society organizations; and a responsible, independent and effective media.
- o) Foster a robust multiparty democratic system; establish and sustain a system of checks and balances between the judiciary, the legislature and the executive (i.e. the Courts, the Parliament, the Council of Ministers and the President).
- p) Build and strengthen regional and international political, economic, scientific and cultural cooperation.

GUIDING PRINCIPLES

2.14 A number of principles have been identified to guide actions and progress in achieving these goals. The important guiding principles adopted by the East Timorese are listed in the following. As can be expected in such exercises, there is some overlap between the goals and the guiding principles.

- a) Participation of all citizens in economic, social and political processes and activities.

- b) Gender equality between women (girls) and men (boys) in access to opportunities, services, goods and privileges.
- c) Equitable development between population groups (e.g. able-bodied and disabled, young and old, rich and poor and different ethnic groups) and areas (e.g. rural and urban, accessible and remote).
- d) Equality and non-discrimination in access to jobs, other opportunities, goods, services and privileges, for diverse population groups in different areas.
- e) Honesty, impartiality, professionalism, integrity, hard work, efficiency, transparency and accountability in public service.
- f) Respect for, and preservation of, the values and culture of the various groups comprising East Timorese society.
- g) Integrated development, ensuring synergies between different interventions to generate benefits that are larger than the sum of the benefits of each intervention.
- h) Cultural, religious and gender sensitivity.
- i) Environmental, economic, social and political sustainability.
- j) Democracy, sovereignty, respect for human rights and the rule of law, and equality before the law.
- k) Self-reliance, social solidarity, peace and national unity.
- l) Creativity, innovation and quality.

2.15 A number of additional principles are to be adopted in the management of the economy, and for the overall development of the country. They are:

- a) A market economic system with strategic and regulatory roles for Government, including the provision of social safety nets.
- b) A strong role for the private sector in development.
- c) A role for government to ensure that physical and social infrastructure and services are provided, and to provide a growth enabling policy and legal environment, including the maintenance of monetary and fiscal stability.
- d) Effective, transparent and corruption free management of the economy and public finances.
- e) Pursuing a fair and equitable economy and society with equal opportunities and improved living standards for all.
- f) Developing in ways that preserve the beautiful environment, traditions and customs of East Timor.

KEY DEVELOPMENT INDICATORS

2.16 The key development indicators have been identified by the East Timorese population. They include economic indicators, such as growth in income (aggregate and per capita GDP), inequality in income distribution, labour force participation and employment, and poverty incidence; social indicators including food availability, access to and use of education, health, water and sanitation services; indicators of security including personal and food security as well as security from shocks and disasters; empowerment indicators such as the number of voluntary people's associations and voting in elections; and indicators of gender equity and empowerment of women. A detailed list of the indicators is provided in Annex 2.1.

2.17 The indicators for East Timor draw upon those presented in the global Millennium Development Goals (MDGs) adopted by more than 175 countries at the United Nations Millennium Assembly in September 2000 (see Annex 2.2). The MDGs use 1990 as the base year, and build upon the targets adopted at previous UN Conferences including those on Children, Environment, Food, Population, Social Development and Women. The Goals to be achieved by the year 2015 include:

- a) reduction of poverty and hunger by half,
- b) achievement of universal primary education with gender equality at all levels (i.e. primary, secondary and tertiary),
- c) reduction of mortality of children under five years old by two-thirds, reduction of maternal mortality by three-quarters, and the halting and reversal of the incidence and spread of HIV/AIDS, malaria and other major diseases,
- d) ensuring environmental sustainability,
- e) reducing by half the proportion of people without access to safe drinking water,
- f) improving significantly the lives of urban slum dwellers,
- g) developing global partnerships for development,
- h) developing and implementing strategies for decent and productive work for youth,
- i) making available new technologies, especially information and communication technologies, in cooperation with the private sector, and
- j) addressing the special needs of the Least Developed Countries (LDCs) and small island states.

3. THE DEVELOPMENT STRATEGY

“....the overriding goals for the development of the country (East Timor) are to reduce poverty.....and to promote rapid, equitable and sustainable economic growth.....”

INTRODUCTION

3.1 As an independent nation emerging from war and transition from the UN administration, East Timor faces many challenges and opportunities. It needs virtually everything. In the process of formulating the Plan, the Government has taken stock of the situation and identified nine key challenges confronting the country in the *State of the Nation Report*.⁵ These key challenges are:

- a) Helping the sizeable number of poor Timorese to help themselves, and to reduce poverty;
- b) Improving the position of women to achieve gender parity;
- c) Improving human resource capacities in the Government, private sector and civil society to manage and administer a nation state in the Twenty-first Century;
- d) Sorting through the multitude of local languages in use and resultant communication problems, and facilitating an orderly and cost-effective transition to the new official languages of Portuguese and Tetun;
- e) Transforming the agrarian subsistence production to a market-based economy;
- f) Improving productivity in all sectors through the introduction of appropriate technologies and practices, reducing risk and modernising production processes;
- g) Creating an enabling environment for the private sector (including farmers, fishermen, small, medium and large investors and entrepreneurs, traders and others) to generate the jobs and economic growth necessary to improve the welfare of the people;
- h) Managing public finances in an efficient and pragmatic way to enhance good governance and attract adequate budgetary support from donor partners, to provide essential services during the next three to five years, until significant revenue flows from the exploitation of oil and gas reserves begin to materialise; and
- i) Sound administration and sustainable utilisation of the oil and gas revenues to benefit present and future generations of East Timorese.

3.2 The above challenges are in tune with the priority constraints identified by the people in the PA during 2001 and the Countrywide Consultation undertaken by the CCCS in early 2002. These challenges underpin the strategy for national development during the next five years (2002/03 to 2006/07), which is seen as the first step towards achieving the twenty-year development vision of the people of East Timor.

⁵ Planning Commission, *The State of the Nation Report*, Dili, East Timor, April 2002.

THE DEVELOPMENT STRATEGY

3.3 Through a participatory planning process, the people of East Timor determined that the overriding goals for the development of their country are to reduce poverty in all sectors and regions, and to promote rapid, equitable and sustainable economic growth that reduces poverty and improves the well being of all the people.

3.4 Whilst these goals are clear, the question remains, “*How to get there – how to achieve the goals and objectives?*” The development strategy tells us, in broad terms, what the general approach will be, and how the goals and objectives will be achieved. The strategy helps decision-makers to focus on the main approaches to, and outcomes of, national development. The development strategy for East Timor addresses the nine key challenges identified by the people. These challenges are to be met through the strategies outlined below. These strategies are elaborated in the relevant sector chapters.

Poverty Reduction

3.5 More than two-in-five East Timorese are living below the national poverty line of US\$0.55 per capita per day. This poverty line has been set to fulfil the food requirement of 2,100 kilocalories per day and other expenditures on education, health and housing, taking into account normal consumption patterns in the country. In addition to expenditure, the other dimensions of poverty as mirrored by social indicators reflect an equally austere picture. For example, literacy levels are low, access to and use of education services modest, and health services meagre, reflecting both supply and demand constraints. Considering the significant number of poor people and the central role of poverty reduction in the development strategy, a detailed presentation of the poverty reduction strategy is provided in the next chapter.

Gender Mainstreaming and Empowerment of Women

3.6 Women constitute almost half the population of East Timor (49.75% according to the 2001 Suco Survey). Women are key economic and social agents. They are also important actors in caring for the young and the old, managing the household, and moulding the values and behaviour of children who are the future leaders. The active participation of women in national development as equal partners with men is crucial for the overall improvement of the welfare of the people.

3.7 Many East Timorese do not yet seem to fully appreciate women's rights or to embrace gender equality. Women (including girls) continue to be discriminated against in the ownership of assets, access to social and economic services, and participation in making decisions affecting their lives. The prevalence of a multitude of traditional practices and the absence of statutory laws make the identification and enforcement of women's rights difficult. The ingrained orientation of men towards the traditional roles of women in East Timorese society needs to be changed through education and sensitisation. A campaign of education and awareness raising on gender is essential, throughout the country and particularly in rural areas. Gender awareness and equity should be incorporated in school curricula. The print and audio-visual media should be mobilised to get the message across to all areas of the country.

3.8 East Timor has made a good start in recognising and promoting the role of women. For example, women constitute about 25% of the members of the Constituent Assembly (legislative

body).⁶ Drawing upon the recommendations of the Women's Congress in 2000, the Second Transitional Government of East Timor has included in the draft Civil Service Law a target of at least 30% representation of women in the civil service and has already achieved 25%. Many women are active in civil society organizations including non-government organisations (NGOs). However, there is a traditional division of gender roles that does not always work to the promotion of gender equality. Many activities in and outside the household are divided by gender including in farming. Women's participation in petty trade has been traditionally an important means to augment family income.

3.9 Gender parity appears to have been achieved in primary school enrolment. Yet the female participation rate in education at secondary and tertiary (including university) levels is low, and the gender gap wide. Successful experiences from other developing countries could be drawn upon and adapted to suit the conditions in East Timor, to bridge this gap. Health facilities that serve the specific needs of women need considerable improvement. Maternal health services are critical not only for mothers but also for children. Resource allocation to these services is inadequate, and should be augmented. Women are at greater risk than men from HIV/AIDS because of their subordinate position within the household. The campaign to halt the spread of HIV/AIDS should pay particular attention to the vulnerable situation of women, their reproductive role in transmission of the virus to children, and to their special needs.

3.10 Recognising the importance of gender dimensions, the Second Transitional Government set up an Office for the Promotion of Equality, and appointed a Gender Adviser reporting directly to the Chief Minister. This has facilitated significant sensitisation and inputs into the gender dimensions of the Plan formulation process. Additionally, the Countrywide Consultation undertaken by the CCCS provided for consultation jointly, with women and men, and separately with women and with women's groups, in order to capture fully women's vision for their country, and their national priorities.⁷

3.11 Programs proposed in the Plan also include those on women's economic empowerment. Gender dimensions are also incorporated in the Plan's education and health programs. The recently adopted Constitution has several provisions protecting the rights of women and promoting gender equality. Formulation, adoption and enforcement of necessary statutory laws prohibiting discrimination and violence against women and girls are planned. Civic and political leaders and opinion makers can set role model examples in their personal behaviour, promoting gender equity. After independence, the Government intends to ratify a series of international conventions including the Convention on Elimination of Discrimination of All Types Against Women (CEDAW). Gender inequality is the surest way to transmit poverty to future generations of men and women. Therefore, reducing gender inequality and enhancing women's productivity will be integral elements of the country's development and poverty reduction strategies.

Human Resources Development

3.12 East Timor has human capacities, informal and formal institutions, and social and exchange arrangements, which have evolved over many years, and withstood the onslaught of colonialism and occupation. While these are well suited to the past circumstances, many are

⁶ In August 2001, 24 women were elected to the 88-member Constituent Assembly accounting for about 27% of the total. However, two women members resigned since bringing down the proportion to 25%.

⁷ There is substantial agreement between women and men on the relative importance of education, health and agriculture – the top three priorities mentioned by the largest proportion of people consulted. However, there are significant differences on the other aspects. For example, women often mentioned "helping vulnerable groups" as the next priority while men ranked "roads and bridges".

inadequate for managing and developing a modern nation state in the Twenty-first Century. The modest capacity in the country is insufficient to meet its myriad needs. East Timorese in the government, private sector and civil society will need to acquire new knowledge and develop new skills to administer a modern nation state and build a more diverse and developed economy. Yet it will be difficult to build the capacity to meet all these needs during the next decade. Consequently, prioritising needs for capacity building is essential for planning and plan implementation, as is the sequencing of the introduction of activities designed to provide these needs.

3.13 The Plan presents the main areas for capacity building and training in different sectors. Human resource development strategies focus on capacity building within the Government, private sector and civil society organizations, in such areas as management, supervisory skills, office management and administration, gender awareness and equity, human rights, information technology, Portuguese language and translation. Training programs for district and village staff are also envisaged. Entrepreneurial, technical, and vocational skills are in short supply, and are to be augmented through training programs and projects, including technical and vocational training.

3.14 During the past two decades, a sizeable number of the youth have joined the struggle for independence and missed the opportunity to attend school. The Plan visualises training programs for these veterans and other youth to impart productive skills for wage or self-employment.

3.15 Training and capacity development through formal education programs in primary and secondary schools and tertiary institutions are proposed to be expanded with particular attention to increasing the participation of the poor and girls. Simultaneously, campaigns to improve adult literacy and numeracy are envisaged, since these are crucial for productive employment and economic growth. In the health sector, capacity building is likely to be time consuming, costly and difficult, and the focus necessarily will be on the provision and delivery of services to meet basic health care needs. Similar efforts on strengthening capacity are visualised in other sectors. Capacity building efforts should go hand in hand with an efficient and effective utilization of scarce human resources. (See Chapter 5 for more details on capacity building.)

Language and Communication

3.16 There are at least 30 local languages or dialects being used in different parts of the country. Almost 80% of the people of East Timor can speak or understand Tetun, with more than 40% able to use Indonesian. Portuguese is understood by about 5% and only 2% can operate in English. The Constitution formalised the adoption of Portuguese and Tetun as the official languages with Indonesian and English to be used as working languages as long as needed. The strategies for improving proficiency in Portuguese include the introduction of the language as the medium of instruction in grades 1 to 3 and as a second language in grades 3 and above. This is to allow time for training of teachers and development of the curriculum and textbooks in Portuguese language. The process of introduction of the Portuguese language as the medium of instruction in grades 4 onwards will be gradual and flexible to allow for a smooth transition. Also, language training in Portuguese is to be provided to civil servants and promoted in the private sector and in civil society. Simultaneously, development of Tetun as a written language for daily use, and for judicial and technical purposes is being pursued. This is a pragmatic approach to tackling a difficult challenge.

Transforming Subsistence Production into a Market-based Economy

3.17 East Timor is an agrarian society with a largely subsistence economy in which much of the production is consumed by producers (home consumption). About 76% of the people live in rural areas, and the poor among them account for 85% of the nation's poor. Most of the rural residents depend on agriculture, and productivity in the sector is low. However, there is potential to increase productivity and production, promote specialisation in niche commodities to take full advantage of the agro-ecological diversity, to enhance market exchange and expand exports. In the short and medium term, the sector is not only an important driver of economic growth, but is also a key vehicle for poverty reduction in the rural areas. Recognising this, the Plan provides for introduction of improved technologies and practices, enlarged support services, and better functioning markets. There is a wealth of successful experiences in the Asia-Pacific region, showing how the agriculture sector could be mobilized to accelerate economic growth in the initial stages of economic development, and transformed from a subsistence to a market-based system. Additionally, integrated rural development is seen as a vehicle to supplement and augment initiatives in the agriculture sector to transform the rural economy.

Improving Productivity and Modernising Production

3.18 Low-input low-output technologies and processes typify production in virtually every sector of the economy. They rely on locally available and often home-produced inputs. Emphasis on risk minimisation is the norm for much of the production intended for home consumption, with only a small portion passing through market channels (see paragraph 3.17). Introduction of productivity enhancing technologies and processes is to be promoted through public support services (e.g. in agriculture) as well as through private and civil society initiatives (e.g. domestic and foreign direct investment and the promotion of micro, small and medium enterprises in informal and formal production, and in the service sectors). East Timor is fortunate to have access to modern off-the-shelf technologies in many sectors, ranging from agriculture to information technology. The initiatives put forward in the Plan visualise the adaptation and propagation of technologies to suit the ecological, economic, social and cultural conditions of East Timorese society.

3.19 Modernisation of production requires markets both for the supply of inputs and for the sale of products and services. Strengthening existing markets and developing new markets is feasible through improved infrastructure, reduction of transaction costs, improved access to information, and the promotion of competition. The important role of good infrastructure including roads and bridges, ports and airports, electricity and water supply, transport, telecommunications including radio, TV, telephone and internet and post are recognised. The Plan provides for rehabilitation, improvement and construction of improved infrastructure to promote the modernisation of the economy and better serve the needs of the people.

Creating an Enabling Environment for the Private Sector to Flourish

3.20 The private sector in East Timor comprises among others farmers, fishermen, and micro, small and medium size entrepreneurs. It is in a nascent stage of development and needs a nurturing environment to develop. Much of it has been geared to fulfil domestic consumption needs, and to serving the demands of the government during the past quarter century. The principal role of the Government is shifting from driving the economy to create an enabling environment - including laws, regulations, and enforcement mechanisms (e.g. police, courts and other institutions) and arranging for the delivery of essential support services for the private sector to gain confidence and strength, and to become the engine of economic growth. The Plan incorporates measures to introduce enabling policies, laws, regulations and enforcement

mechanisms in such areas as land ownership, occupancy and lease/rental (tenancy), corporate and bankruptcy laws, banking and insurance, and appropriate security and enforcement mechanisms including well functioning civil and criminal courts and efficient police and security services. Initiatives to strengthen the capacity of the private sector, especially that of small entrepreneurs, is visualized through pilot testing and the adoption of successful approaches in other countries (e.g. in micro finance, small and medium industries development and tourism services).

3.21 The Government intends to strengthen the provision of essential infrastructure including reliable electricity and water supply, telecommunications and transport through a combination of public, private, civil society organisations and community partnerships. Already, the private sector is the major actor in the provision of such services as transport, communications, agro-processing and manufacturing, tourism and hospitality services (e.g. hotels and restaurants), and marketing, including the supply of inputs and sale of output. As it gains strength and matures, the private sector will play an increasingly important role in the provision of infrastructure, education and health services, side by side with the Government and civil society organisations including the Church and NGOs. The Government will focus on its core functions, and will avoid involvement in commercial activities unless there is clear evidence that the private sector is unable to provide essential goods and services (market failure), and that such non-provision impedes poverty reduction and economic growth.

Managing Public Finances

3.22 While the size of the Government will be smaller than in previous years, it will still have a critical role to play in managing public finances, ensuring the rule of law and good governance, and in implementing development priorities. In the short and medium-term, East Timor is confronted with the twin problems of a limited capacity to raise domestic revenues and a relative lack of skilled human resources. Since the mid-1970s, many of the resources required for government operations in the territory were provided by the central government in Jakarta and more recently by the UN and other donors. The Government will have to tackle the dual problems of a lean civil service⁸ that is not yet fully competent in government, and inadequate resources to fund all its priority programs. Effective management of the limited staff, and careful and efficient use of the scarce financial resources must take centre stage in governance during the next few years.

3.23 Efforts to prioritise programs and spending during 2002/03 are already under way. The exercise emphasises prioritisation and sequencing of expenditures and investments, and ensuring complementarities and synergies between programs to generate benefits that exceed the sum of those resulting from individual programs. A cross-sectoral approach should ensure efficient resource use, and generate commensurate benefits. At the same time the continual updating of strategies within sectors and agencies will be important. Also, a three-year medium term fiscal framework (MTFF) incorporating a results-based management approach is being developed for adoption.

3.24 By mid-2002, the departure of the bulk (about 70%) of the foreign personnel and the local counterparts engaged by UNTAET will leave a major gap in the capacity of the

⁸ The civil service strength (excluding the military and security forces and the police) is expected to reach about 12,000 by the end of 2002, which is less than half of the approximately 28,000 under the Indonesian rule. The former is considered to be adequate (if fully competent and equipped) to perform government functions and is barely affordable by the country, given its present circumstances.

Government. To facilitate a more orderly transition, this gap is planned to be filled at least temporarily by about 300 foreign personnel with expertise in finance, management, development administration and other technical fields. They are to be deployed in various line ministries (including the Ministry of Finance) and departments at the centre in Dili, and in the districts. This should ease the situation and allow time for building the capacity of the civil service in the next twelve to eighteen months. The financial crunch on budget resources is expected to ease somewhat, once significant revenues from oil and gas begin to materialise.

Administration of Oil and Gas Revenues

3.25 The projected flow of significant oil and gas revenues currently expected to begin in 2004/05 or shortly thereafter, is a blessing to the people of East Timor. It will allow them to more fully address their development needs and priorities, further strengthen their human resources, consolidate the gains achieved so far, accelerate and sustain economic growth, reduce poverty and improve the welfare of all East Timorese. According to present indications, the flow of significant oil and gas revenues is expected to be of limited duration – between 20 to 30 years – depending on the types of petroleum products extracted, world prices and new discoveries. Prudent management, saving, investment and utilization of the windfall in oil and gas revenues provides a valuable opportunity for East Timor to build its human, physical and economic capacities, and graduate to a middle-income country. The thrust will be to utilise the resources for the benefit of present and future generations of East Timorese, and curb the temptation to squander the windfall in ostentatious consumption. The Government is already benefiting from the advice and assistance of Norway on the latter's experience in managing petroleum revenues in a sustainable way.

GOVERNANCE AND MACROECONOMIC MANAGEMENT

Governance

3.26 East Timor is fortunate in having a vibrant civil society and an enthusiastic people that are eager to move on with nation building. However, development in East Timor is constrained by a lack of appropriate legislation, regulations, institutions and other elements of a national governance structure. As indicated in the foregoing, the Development Strategy includes a focus on developing, as soon as possible, priority legal, institutional and governance structures that support poverty reduction, gender mainstreaming, human resources development, private sector development and overall economic growth.

3.27 The strategy considers and incorporates the social and cultural values and norms underpinning society. These include areas such as religion and the role of the Church, the cultural and social context in which productive, social and community activities occur, and the impact of development on the natural environment. Emphasis will be accorded to strengthening and maintaining an environment of peace and security. The development strategy will build upon the extensive participation of the people in formulating their national vision and development priorities. It will promote continued participation of the people in translating the Plan into action (implementation), monitoring and evaluation while seeking accountability from public institutions and functionaries, the private sector, civil society organisations and the media.⁹

⁹ The baton of government will pass from UNTAET to the Government on 20 May 2002. Use of the future tense in this and other paragraphs should be seen in this light.

Macroeconomic Management

3.28 Appropriate macroeconomic policies will underpin the development strategy. These policies will be designed and managed to be pro-poor. Examples of pro-poor policies include:¹⁰

- a) equitable tax and revenue policies,
- b) priority to public spending on services that are most used by the poor (e.g. primary education, basic health care, rural water supply, and urban slum upgrading),
- c) reducing rural urban gaps in access to, and affordability of, basic social services (e.g. education and health care) and essential economic services (e.g. extension, technology, training, credit and markets),
- d) curbing price rises (low inflation),
- e) ensuring banking, credit and microfinance services are available to all, including the poor and women, and
- f) implementing trade and investment policies that promote growth of production and employment to benefit the poor.

3.29 All the macroeconomic policies (including fiscal policy, monetary policy, exchange rate policy, trade policy, investment policy and wages policy) will be framed as a consistent package that will promote growth and poverty reduction. The package will be designed to establish and strengthen the international competitiveness of East Timor. The economy will be open to trade and investment, with adequate safeguards to nurture and develop domestic industries that are competitive. The macroeconomic and sector policies will aim to promote the development of a strong and dynamic private sector, leading the growth process. Foreign investment will be encouraged, especially in sectors that contribute to strengthening East Timor's economic infrastructure and human skills and facilitate the transfer of technology.

3.30 In the initial stages, growth is likely to be led by labour-intensive activities and businesses employing unskilled and semi-skilled labour, particularly in the transformation of agriculture. Macroeconomic policies will be conducive to moving to more mature stages of growth, including high technology and high skills businesses, as investment demand and relevant skills emerge. The policies will be conducive to maintaining the competitiveness of East Timor with its neighbours and in international markets. Higher domestic saving and investment will be encouraged. The banking and financial sectors will be developed to provide adequate services to all the people, and especially to rural residents, following prudent principles and practices.

¹⁰The details on the macroeconomic policies are presented in the chapter on the Macroeconomic Framework.

4. POVERTY REDUCTION STRATEGY

“.....poverty reduction in East Timor should be seen primarily as a means to accelerate and sustain economic growth.”

INTRODUCTION

4.1 Poverty is multidimensional and manifests itself in different forms. It is more than a problem of inadequate income. It includes a lack of access to basic social and essential economic services and life choices, including opportunities to participate in economic, social and political processes. The many characteristics of poverty include malnutrition and illness, shortened lives, illiteracy, social exclusion and the lack of appropriate means to improve one's situation. These dimensions may be experienced in different combinations. For example, men and women view and experience poverty differently. Often, women have less access to, and control over, assets such as land and economic (e.g. credit and extension) and social services (e.g. education and healthcare), and limited participation in decision-making in and outside the household.¹¹ Thus, gender inequality is considered to be one of the most important causes of poverty among women.

4.2 On a more general level, inequality can manifest itself in the ownership of land, in the distribution of wealth and income, in access to economic and social goods and services as well as to remunerative jobs, in participation in social and political processes, and in other life choices. Virtually all such inequalities are present in different combinations across regions and over time. They contribute to poverty and to the unequal distribution of income and the benefits of development.

4.3 Consequently, poverty can be defined in both money (expenditure or income) and human terms. However, many of the quantitative measures in use are based on poverty lines defined in expenditure (income) terms, supplemented by other indicators on aspects such as access to and use of education (including literacy), health, water, sanitation and housing. Gender dimensions are also incorporated in poverty measurement. National poverty lines are constructed based on data generated from household expenditure surveys covering a sample of the households in the country. The head-count ratio of poverty measuring the proportion of people below the poverty line in the total population is the most commonly used index. A poverty gap measure (the ratio or percentage of the amount required to bring the expenditures of the poor to the poverty line, relative to the total expenditures of the poor at the poverty line) is used to measure the intensity of poverty.¹²

¹¹ The ranking of development priorities may differ between men and women. For example, while the results of the Countrywide Consultation show almost complete agreement between men and women on the top three development priorities (education, health and agriculture), significant differences emerge on ranking the other priorities. Also, the differences in ranking between men and women vary by district. For example, in Aileu which is one of the poorest districts, women ranked “helping vulnerable groups” while men indicated “roads and bridges” as the fourth priority.

¹² For example, the poverty line in East Timor is US\$0.55 per person per day and about 341,000 East Timorese are below the poverty line. Preliminary results from TLSS indicate the average expenditure of the poor to be \$0.48 per person per day. Based on the above, the poverty gap is estimated to be about 13% $[(0.55 - 0.48) \times 341,000 + (0.55 \times 341,000)]$.

4.4 Understanding the causes and consequences of poverty are important to design appropriate means to address it. The poor are not a single homogenous group. People view and experience poverty in different ways. The perceptions of the poor, their neighbours, community leaders and local officials on poverty, the constraints faced by the poor, and the potential that exists are valuable in understanding the situation on the ground. Often, these perspectives are captured through consultations, participatory appraisals, surveys and/or focus group discussions with these groups, through participatory poverty (potential) assessments (PPAs).

POVERTY IN EAST TIMOR

4.5 The people of East Timor have survived harsh and difficult conditions and successfully overcome both colonial and occupation regimes. Their rich experience in the political liberation of their country has been widely recognised. However, the stark reality is that the country is one of the poorest in the region, with not only low income, but also poor performance on social indicators such as, education, literacy and health. Thus, there is an urgent need for economic, social and cultural liberation to empower the people to exercise and enjoy fully their newfound political freedoms and rights.

4.6 Recognising the imperative of poverty reduction, the East Timor Transitional Administration (ETTA) in partnership with four donors¹³ undertook a poverty assessment during 2001-02. The assessment comprised a survey of all the sucos (villages) in the country, a living standards measurement (or household expenditure) survey, and a PPA. Based on the preliminary results from the household expenditure survey undertaken in September 2001, a national poverty line at the equivalent of \$0.55 per person per day was formulated. Around two-thirds of this was allocated to food, sufficient to provide 2,100 kilocalories per day, and the rest to non-food items including education, health, clothing and housing. Using this benchmark, it was estimated that about 41% of the population fell below the poverty line, with the incidence higher in the rural areas (46%) than in the urban centres (26%). The lowest poverty rate is in the urban centres of Dili and Baucau (14%).

4.7 The vast majority of the poor (85%) live in the rural areas. Of these, the poorest groups are in households that have small landholdings or are headed by fishermen. Additionally, households with many children, or those with a large number of elderly or other dependent relatives are most likely to be poor. Poverty incidence is higher among households headed by those with no schooling, and it declines with a rise in the educational achievement (level) of the household head.

4.8 Poverty in East Timor is also related to inequality in income distribution. The generally used measure of inequality is the Gini-coefficient, which varies between 0 (absolute equality) and 1 (one person receives all the income). In 1995, the Gini-coefficient in East Timor was at 0.363, which was higher than in some of the other poor provinces of Indonesia (see Table 1). This can be explained in part by the low productivity of agriculture, which reduced rural incomes. Although three quarters (73%) of workers were employed in agriculture, they generated less than one-third (around 30%) of the gross domestic product (GDP). Agricultural output per worker in East Timor during the mid-1990s was less than half that in most other provinces during the Indonesian administration.

¹³ These are the Asian Development Bank, the World Bank, the United Nations Development Programme and the Japan International Cooperation Agency.

4.9 The majority of the urban workers were either employed by the government or other service providers and probably had earnings similar to those elsewhere in urban Indonesia. Thus, in the mid-1990s the per capita income in Dili was 73% higher than that for East Timor as a whole while that for the poorest district, Lautem, was 42% lower than the national average. In other words, the per capita income in Dili was about three times that in Lautem. The departure of Indonesian officials in 1999 was followed by an influx of foreign experts under UNTAET and other donor and NGO programs. As a result, the Gini-coefficient increased marginally to 0.37 in 2001.¹⁴ This effect may be moderated somewhat after the scaling down of UNTAET operations after independence on 20 May 2002.

Table 4.1. Inequality and Agricultural Productivity, 1995¹⁵

	Gini-coefficient	Agricultural output per worker (Rp. Millions)
East Timor	0.363	0.847
W. Nusa Tenggara	0.286	1.706
E. Nusa Tenggara	0.296	0.961
Maluku	0.269	2.026
Irian Jaya	0.386	2.007

4.10 An additional frequently used measure of inequality is the ratio of the proportion of income captured by the richest 20% of the population to that accruing to the poorest 20%. In 1998, this ratio for East Timor was estimated to be about 3 by the Boston Institute for Developing Economies (USA). The inequality in income distribution in East Timor is considered to be low to moderate as compared with that in other countries at a similar stage of development.

CAUSES OF POVERTY

4.11 The more apparent causes of poverty in East Timor include the following:

- a) rapid population growth (estimated to be around 2.5% per annum),
- b) lack of ownership and/or access to adequate productive assets, including land (for example, 24% of the families owned less than 0.5 ha of agricultural land and 60% between 0.5 and 2.0 ha),
- c) lack of productive skills (including literacy),
- d) lack of remunerative employment or jobs (the open unemployment is more than 16% and especially high among the youth, and there may be significant underemployment in the agriculture sector),

¹⁴ Preliminary estimate from the 2001 TLSS.

¹⁵ Reproduced from Booth, A. (2001), "Poverty, Equity and Living Standards in East Timor: Challenges for the New Nation," in Hill, H. and J. Saldanha, East Timor: Development Challenges for the World's Newest Nation, Institute of Southeast Asian Studies, Singapore, p. 244.

- e) lack of or inadequate access to social and economic services (e.g. access to schooling is low especially in the poorer districts, and the rural residents have to walk on average 70 minutes to reach the nearest health facility; and access to extension services low and markets difficult),
- f) lack of information about the rights and obligations of citizens (this has been improving in the last two years),
- g) political, social and economic turmoil, resulting particularly from the violence of 1999,
- h) discrimination, particularly against women, in the economic, social, political and legal arenas,
- i) natural shocks including drought, flood and fire,
- j) unexpected death and illness, including Malaria, TB, and STD and HIV/AIDS,
- k) manmade shocks such as revenge killings and violence, displacement and fear/insecurity,
- l) social breakdown, including breakdown of marriage, family and social support systems, and
- m) increase in the prices of basic necessities (e.g. food, clothing and fuel) and services particularly during 1999-2000, partly resulting from introduction of the US dollar.

4.12 Some of these causes may be accentuated by poverty thereby creating a vicious circle.

CONSEQUENCES OF POVERTY

4.13 The effects of poverty on the poor are degrading and devastating, especially for women and children. The consequences of poverty are also detrimental to society. These include the following:

- a) the meagre resources of the poor are not adequate to subsist, let alone to save and invest,
- b) the poor are forced to over-exploit renewable and non-renewable resources (e.g. forests including mangroves) for sheer survival, thereby contributing to environmental degradation,
- c) the sub-optimal development of the productive potential of the poor, women and other vulnerable groups, results in a reduction or loss of their full contribution to economic growth and social development, and
- d) the poor may impose negative externalities such as crime, spread of diseases, social unrest, and political instability.¹⁶

¹⁶ Environmental degradation is another negative externality mentioned already.

4.14 Poverty reduction should be addressed through policies and programs that help redistribute the growing assets and opportunities, income, services and choices to the poor. Disaffection of the poor and the disadvantaged may lead to social unrest and political instability, in addition to economic disruption. Therefore, poverty reduction is not only sound economics but also good politics. East Timor can ill afford to ignore the potential and aspirations of its poor and women.

POVERTY REDUCTION STRATEGY

4.15 Economic growth and poverty reduction are the overall goals of the development of East Timor. The people – including farmers, fishermen, traders, labourers, workers, and micro, small and large investors – are the main actors that generate economic growth through their innovation, skills and work. The Government is primarily a facilitator in this process. The assets and efforts of the poor are necessary for the country to accelerate its economic growth, and to sustain development. This is all the more significant, since the poor constitute more than two-fifths of the population. The East and Southeast Asian countries mobilised the efforts of all their peoples – rich and poor, men and women, skilled and unskilled – in order to generate and sustain rapid economic growth and achieve the status of newly industrialised countries (NICs). They treated their people as their most valuable resource. This is an important lesson from which East Timor could benefit. Indeed, during the PPA in November – December 2001 and the Countrywide Consultation undertaken by the CCCS in January – February 2002, the people of East Timor wanted to convey the important message to the Government that they should be seen as an asset rather than a liability.

4.16 A large majority of the poor people in East Timor is capable of contributing to the country's economic growth and development.¹⁷ The challenge is to provide the enabling environment for them to participate in, and partake of the benefits of development, while assisting the few that cannot help themselves. Thus, poverty reduction in East Timor should be seen primarily as a means to accelerate and sustain economic growth. The Poverty Reduction Strategy of the country is formulated on the basis of this approach. It is understood that rapid economic growth is a prerequisite for sustained poverty reduction in East Timor. The main elements of the Poverty Reduction Strategy comprise the following:

- a) Create an enabling environment to generate opportunities for the economic participation of the poor, improving their productivity and enhancing their incomes;
- b) Provide and/or encourage and help others to provide basic social services to the poor on affordable terms;
- c) Provide or help to provide security of person and property, and protection from unforeseen shocks and disasters (vulnerability), including food security at both the household and national levels; and
- d) Empower the poor and other vulnerable groups through popular participation in deciding upon and managing development in their aldeias, sucos, postos, districts and the country.

¹⁷ Only a small minority (including orphans, the disabled, widows, and other vulnerable groups) require either temporarily or on a continuing basis direct transfers of income or other help to lead a reasonable life by the standards of the East Timorese society.

4.17 Elaboration of these four elements of the strategy and their links with activities undertaken in the various planning sectors are illustrated in the following sections:

Opportunities for Economic Participation

4.18 The experiences of the Asian NICs show that the initial thrust for rapid economic growth emanated from the agricultural sector, especially from productivity improvements in small-scale agriculture. About three-quarters of the labour force in East Timor is dependent on small-scale agriculture, and improving their productivity is critical for accelerating the country's economic growth. Almost half of this labour force is poor, and a majority of the poor are women.

4.19 The poor in East Timor are engaged primarily in agriculture – in cultivating crops, animal husbandry, fisheries and forestry. Improving productivity in the sector is recognized as a high priority. Traditionally, East Timorese farming families have attempted to minimize risks from crop failure due to adverse weather or other unforeseen events through the practice of intercropping and low seeding rates.¹⁸ Other approaches to risk minimisation such as the use of drought resistant varieties, improved water use including irrigation management, and high yielding crop varieties are feasible. Proposed initiatives for this within the Plan include rehabilitation and construction of irrigation systems and their improved operation, introduction of water harvesting techniques, wider distribution of improved seeds of crops, fruits and vegetables, protection of livestock, improved fishing and sustainable management of forest and other natural resources, through community participation. Improvements in marketing and infrastructure are also planned. Provision of support services is expected to materialize through public and private initiatives in agriculture, and in other sectors.

4.20 The informal sector has been an important contributor to growth in the Asian NICs. Alongside agriculture, a large proportion of the employed in East Timor are dependent on the informal sector, in both the urban and rural areas,¹⁹ and a majority of them may be poor. Consequently, increasing opportunities and improving productivity in this sector are crucial for enhancing the country's economic performance and reducing poverty. Initiatives proposed in the Plan include training, introduction of appropriate technologies, and other support services including the supply of micro credit.

4.21 A third important area is the formal private sector, in manufacturing, construction and real estate, trade, transport, tourism, and financial and other services. Priority policies and legislation are being drafted to improve the policy environment, and to encourage both domestic and foreign private investment in the country.

4.22 A fourth area is the provision of infrastructure – including roads and bridges, ports and airport(s), electricity, telecommunications and postal services. These are critical for the movement of people and goods, an orderly and efficient functioning of markets, and for a sustainable development of the country. A number of interventions are proposed to improve the country's infrastructure, drawing primarily upon aid resources.

¹⁸ For example, many small farmers grow three or more crops (e.g. sweet potato, maize and beans) on the same plot of land simultaneously.

¹⁹ For example, a 1993 survey by BPS, the Indonesian statistical agency, showed that about a third of the farm household income came from off-farm sources including wage income and self-employment in manufacturing, trade, transport, other transfers (e.g. pensions), etc. (Cited in Booth, A. (2001), "Poverty, Equity and Living Standards in East Timor: Challenges for the New Nation," in Hill, H. and J. Saldanha, East Timor: Development Challenges for the World's Newest Nation, Institute of Southeast Asian Studies, Singapore, p. 249.)

4.23 The final area relates to macroeconomic policies and the management of public finances, including public expenditure allocation. In this area, pro-poor macroeconomic and public expenditure policies will be implemented.²⁰

Basic Social Services

4.24 Enhanced access to and use of basic social services is an urgent need in East Timor. Almost half the adult population is illiterate, with women considerably disadvantaged relative to men. Whilst access to schooling improved considerably during the Indonesian period, when compared with the latter years of Portuguese rule, the quality of teaching and learning was low. Currently, about a third of children are not enrolled in primary school, and up to 20% of those reported as enrolled do not attend classes. Access to and use of public health services is minimal, due to the inadequate number of trained personnel, facilities, medicines and supplies (supply constraints), coupled with poor access and cost (demand constraints). For example, in the rural areas, reaching the nearest health facility requires - on average - a 70 minute walk. After reaching the facility, there is no guarantee that a doctor and/or nurse will be available. Additionally, each visit costs about two dollars (US\$2). Access to safe water and sanitation is also low, and the quality of much of the housing stock is inadequate.²¹

4.25 The provision and effective use of basic social services is an important means to break the poverty cycle. Education and literacy are prerequisites for introduction and adoption of modern productivity enhancing technologies. The Plan incorporates programs to improve school participation rates, especially for children from poor families, and to improve the quality of teaching and learning. Adult literacy programs are also proposed. Evidence from other countries shows that education of girls and women have multiple benefits, affecting their welfare, and that of their children, families and future generations. The delivery of basic health care is to be improved by addressing both the supply and demand constraints. These are key ingredients for improving not only the productivity of the population but also the welfare of the society.

4.26 Ensuring access to, and affordability of basic social services is an important task for the Government. This does not mean that the Government should deliver all the services. As in many countries in the region, NGOs and religious organizations in East Timor have been involved in the delivery of some of the basic social services. The Church is prominent in education, some NGOs have been involved in healthcare delivery (until mid-2001), and others are involved in supporting community water supply and sanitation. The private sector has also been active in the delivery of services to those who can pay in other countries. For example, almost half the health services in the Philippines are delivered by private clinics and hospitals.

4.27 Under present circumstances in East Timor, the delivery of quality primary, junior secondary and senior secondary schooling, and primary health care (including preventive care such as immunization and health, hygiene education and curative care) are given priority within the Plan. With regard to water supply and sanitation, the overall approach is to address the provision of the services in urban areas on a cost recovery basis, whilst community ownership and operation is the norm in rural areas. The challenge is to build partnerships and strengthen complementarities between public and private entities – in this case mainly with the Church and

20 The UN World Summit for Social Development (Copenhagen, March 1995) recommended the adoption of the 20/20 Compact for mobilisation of resources for financing basic social services. The basic social services include primary education and adult literacy, basic healthcare, safe water and sanitation. These services are considered essential for combating the worst manifestations of poverty and deprivation and improve human development. The Compact calls for devoting at least 20% of public expenditures (government budget) and 20% of ODA to providing basic social services.

21 The phenomenal destruction of property in the 1999 violence greatly reduced the modest stock of relatively better quality housing.

the NGOs – to deliver services to the population at large, and to the poor in particular, with gender equity.

Security

4.28 The third element of the Poverty Reduction Strategy, is concerned with ensuring the security of person and property (against violence, destruction and theft), food security, livelihood or job security, and protection against unforeseen calamities - including natural disasters such as floods and droughts, as well as economic shocks and political and social disturbances. Security of person and property has been a major concern for many East Timorese families during much of the 25 year occupation, and particularly in September 1999. The security situation has improved considerably since September 1999. Proposals are included in the Plan to consolidate, improve and sustain the current relatively stable and peaceful situation in the country, with the participation of its constituent communities. Interventions include precautionary measures (monitoring/intelligence), police and law enforcement activities, and efforts to promote reconciliation and reintegration of refugees and other groups at risk.

4.29 Food security is an important concern for the population in general, and for the poor in particular. The findings from the 2001 SSSL and the TLSS show severe stress in food availability during December and January – the lean months preceding the harvesting of maize and rice, the major food crops – with significant stress during November and February. Coping strategies mentioned by the people include reducing consumption (eating two meals a day instead of three), substituting maize for rice and cassava and sweet potato for food grains, selling livestock, and borrowing from relatives and friends. There have been some improvements in national food security in the last two years resulting from better harvests of rice and maize. However, food security is still a major concern at the household level.

4.30 Interventions outlined in the Plan for the agriculture sector will enable a consolidation and further improvement in overall food availability in the country. They will also contribute to improving food security at the household level. Further targeted interventions may be necessary to strengthen food security at the community and household levels, including strengthening traditional community structures such as caring and sharing arrangements. However, it is important to recognise that food scarcities may adversely affect all households in a poor community, and there may not be enough to share and alleviate the hunger. Often children and women are at greater risk. This takes on increased significance when viewed in the context of almost half the children in the country being underweight, and a quarter malnourished. Examples of interventions included in the Plan at the program level include school feeding and the distribution of milk and food supplements to pregnant and lactating women. Continuation of the current practice of augmenting food availability through imports in the short and medium-term, and timely distribution to vulnerable groups is also envisaged.

4.31 Insecurity of livelihood or employment is pervasive in the traditional, informal and formal sectors.²² This can arise from lack of recognition of ownership and tenancy of agricultural land, from traditional access to such resources as forests, or other public lands for collection of food, fodder and other products, and from delineation and lease or sale of common property resources (e.g. fishing grounds and pastures). In most cases, it is the poor and vulnerable that are at risk. The proposed legal frameworks and policies on agricultural land, fisheries and forestry should minimize such risks. Additionally, employment arrangements in the informal and formal

²² Also, open unemployment is in excess of 16% of the labour force with a much higher rate among youth and veterans who participated in the struggle for independence. A significant proportion of the labour in rural areas may be underemployed.

sectors for unskilled (and often poor) labourers may be insecure, due to economic or market developments (e.g. cheap imports) or other events, with unscrupulous employers exploiting workers for long hours of menial work with low wages. Some protection of the workforce in terms of fair wages and working conditions is envisaged, without these creating disincentives for employment.

4.32 Security from natural and man-made disasters is a further dimension that needs to be addressed. There is a wealth of experience on these aspects in other countries in the region, and in other regions of the world. It includes disaster forecasting, preparedness, prevention and mitigation. Employment in public works, including community maintenance of roads, is already being implemented in East Timor. Other initiatives in this direction are proposed in the Plan. They stress the importance of community involvement and the strengthening of community resilience, in addition to material help from the Government, donors and NGOs. These interventions and arrangements may be refined, based on experience during the first two to three years of plan implementation.

4.33 Security from economic shocks is an area that also needs attention. One of the more significant, imminent economic shocks is the scaling down of UNTAET operations, and the departure of a large number of foreign staff. This will be felt not only in the urban areas of Dili and other district towns, but also in the hinterlands that provided goods and services to foreigners. Some short-term and medium-term training and employment measures are contemplated to cushion the adverse impacts of the UNTAET contraction.

Empowerment

4.34 The fourth dimension, empowerment, embraces the provision of “voice”, and the participation of the poor in making decisions about their future and the future of their communities, on economic, social, cultural and political issues.

4.35 As the experiences in the formulation of the Plan demonstrate, popular participation is a widely accepted norm in present day East Timor. Many initiatives proposed in the Plan intend to consolidate and build upon this enthusiasm. Examples include community decision-making and management of water supply, infrastructure and natural resources. Successful examples of community management of schools and health facilities in other countries should be drawn upon in piloting and testing similar approaches in East Timor.

4.36 Decentralisation is an important means to ensure the sustained participation of the people in general, and the poor and women in particular, in local affairs. The degree of decentralisation can be at three levels: deconcentration, delegation and devolution.²³ For example, prior to 1999, “deconcentration” was the rule, with the central government delegating responsibility for implementation of policies and programs decided by Jakarta to administrators at the local level. It was a top-down system with little room for decision making at the local level or the flow of information from the bottom up, let alone people’s participation. Delegation involves the transfer of some decisions and functions to local organisations including those at the village level. For example, the ongoing Community Empowerment Project (CEP) delegates responsibility for a number of decisions and functions to elected Village Development Councils. The Plan aims to build upon the experiences and lessons learned in the CEP, and to expand and replicate the more successful approaches in other areas. Devolution is the next level of decentralisation, and involves the transfer of significant authority for decision-making, finance

²³ UNDP, *East Timor Human Development Report 2002*, second draft, Dili, April 2002.

and management to elected local governments, often with the power to impose taxes and raise revenues. Significant capacity building at the local level is a prerequisite for the introduction of devolution. This is a gradual process, which the Government intends to pursue.

4.37 Informed participation of the people requires civic education and improvements in education and communication. The recent highly successful experience of voter education resulting in high levels of participation in the Presidential election - with a turnout of more than 86% of eligible voters - is an excellent example of civic education, which can be replicated in other areas. Civil society organisations, including the Church, have been important facilitators in the voter education process. School curriculum development is expected to incorporate civic education. Also, separate programs on civic education are to be promoted through the mass media, in partnership with civil society organisations.

4.38 The challenge of formulating and implementing an information, education and communication (IEC) strategy focusing on all the people is recognised. This is critical for informing and educating the people on the roles, functions and activities of the different organs of the Government, donors, NGOs and other civil society organisations. At the same time, viable channels need to be evolved to facilitate the flow of information from the people on the ground to policy makers, other Government functionaries and other stakeholders. This is especially important for the poor, women and other vulnerable groups. In this regard, the institutionalisation of the recent successful political and popular participation and consultation approaches may be appropriate. The Plan incorporates initiatives that go some distance in this direction (e.g. information and education on the role and activities of the Parliament, organisation of communities and provision of audio visual equipment). It is necessary to examine the initial experiences in the different sectors in formulating the IEC strategy and in designing appropriate coordination mechanisms.

CONCLUSIONS

4.39 The implication of the preceding analysis is that improving the productivity of the poor is essential for East Timor's economic growth. It should be an integral part of the interventions in all the sectors of the economy to achieve and sustain rapid economic growth and improvements in the welfare of all Timorese. Creating an enabling environment for catalysing and sustaining the contribution of the poor to national development is an important task for the Government. It will entail both providing, and helping others provide basic social and essential economic services to the poor, nurturing and promoting the entrepreneurial initiatives of the poor, and prohibiting discrimination based on gender, ethnic origin, language, or geographic location.

4.40 Enforcing the rule of law, creating a secure environment, and a sound management of fiscal and monetary affairs are important ingredients for economic growth and overall development. Discretionary decision-making must give way to rule-based procedures, with reduced opportunities for corruption and favouritism. The role of Government should be limited to providing those essential services that the private sector and civil society organizations are not in a position to deliver. These are important ingredients for poverty eradication, gender equity and economic advancement of the country.

4.41 In particular, there is a need to link closely governance and poverty reduction, to enable the people to seek solutions to their development problems, and to exploit all available opportunities. East Timor must create a conducive political, social, economic and legal environment for the poor to mobilise their resources, to realise their potential, and to build sustainable livelihoods.

5. CAPACITY BUILDING FOR PLAN IMPLEMENTATION

"East Timorese in the government, private sector and civil society will need to acquire new knowledge and develop new skills to administer a modern nation state, and to build a more diverse, developed economy."

INTRODUCTION

5.1 Promoting economic growth to reduce poverty will require the Government to facilitate the delivery of basic social and economic services. This delivery will itself require enabling laws and regulations, and the empowerment of the population through community management and participation.

5.2 To build capacity to meet East Timor's significant needs in infrastructure, technology, training, capital and access to markets during the next five years is clearly impossible. Consequently, prioritizing needs for capacity building is essential for planning and plan implementation, as is the sequencing of the introduction of activities designed to provide these needs. East Timorese in the government, private sector and civil society, will need to acquire new knowledge and develop new skills to administer a modern nation state, and to build a more diverse, developed economy.

5.3 In this process, criteria for prioritization should centre on the importance of capacity building for essential, sustainable, and affordable service delivery. It is vital that the most crucial areas for capacity building be agreed at the earliest stage of plan implementation. The Plan presents the main areas for capacity building and training, in several of its programs, in different sectors. These programs address both short-term implementation needs, and capacity requirements for the medium term at the central, district and local levels. They recognize a crucial point: that capacity building will have to be based extensively on government partnerships with civil society organizations, the church, NGOs and the private sector. Additionally, capacity building must take into account the roles performed by existing traditional institutions, informal networks, and mutual-help groups, particularly at the village level. These were critical in maintaining communities during the struggle for freedom, and will continue to play an important part in capacity building at the local level.

5.4 On the basis of these requirements, several areas are prioritized in the Plan. These can be summarized, as follows:

GOVERNMENT AND GOVERNANCE

5.5 Capacity building at the government level is crucial for East Timor. During the Indonesian period, limited indigenous expertise was developed in senior and middle management, supervisory level skills, and in office management and administration. Additionally, many of the East Timorese trained in these areas left the country during 1999, and have not returned. Consequently, as outlined in *The State of the Nation Report*, the vast majority of current civil

servants are neither adequately experienced, nor trained for the roles they will have to undertake. Yet East Timor will have to depend heavily on its civil service to manage the transition to an independent, democratic, and economically viable society. To address this problem, the former Cabinet endorsed a comprehensive ten-year program for Governance and Public Sector Management developed by the National Planning and Development Agency in 2001, with support from the UNDP. This program was well received by donor countries. The Plan builds on, and develops this program, by stressing the need to develop organizational and managerial values within a framework that respects East Timorese cultural values, whilst concomitantly pursuing open, cost effective and accountable systems of government.

5.6 The Plan sets out strategies for developing and strengthening institutions for the post-transition period. It outlines how capacity can be built to enable the Government to assist in the development of a market-based economy. For each sector, the Plan also provides strategies for strengthening capacities in policy development, co-ordination, and the core skills required for management. It shows how the East Timorese Government can provide an enabling economic environment, deliver appropriate services, and establish relevant legal frameworks during the post-independence period. It stresses the need for transparency, and outlines how capacity can be built within the civil service for drafting legislation, developing policy and upgrading skills. In this, it cites as most crucial: the development of operational planning and budgeting; the development of organizational and supervisory skills at middle and supervisory levels; training in records management and document control, information technology, Portuguese language and translation; training programs for district and village staff; gender awareness and equity training, and human rights training. In meeting these aims, additional, basic skills need to be developed at a number of levels within public service. For example, at the senior and middle management level, there is a need to develop the ability to put together operational plans and budgets, to develop capacity in advising ministers on legislation and regulations, to create operational programs from policies, and to link government with the private sector, NGOs, and civil society organizations. Similarly, at the office management and administrative levels, skills need to be developed in areas such as records management, drafting documents, and communication. Only through developing skills such as those outlined above, will East Timorese be able to genuinely own their administration, and begin to build capacity themselves.

5.7 The Capacity Development for Governance and Public Sector Management Programme, outlined above, suggested 75 areas of development, implementation of which was regarded as important for institutional and human resource development in East Timor. Some of the more crucial of these have already been specified, notably for improving capacity for service delivery in the Civil Service Academy, improving human resource skills and capacity for the development of policies, legal and regulatory frameworks for civil service personnel management, and for servicing the government with cost-effective, efficient human resources systems. Donor support for these, and for other areas such as records management, policy, guideline and procedure development, legislative review, planning and budgeting, the operation, maintenance and management of Information Technology will be important in strengthening governance and public sector management capacities. The aim of such support, and one of the essential goals for building capacity for plan implementation is to develop a professional, efficient and effective civil service, capable of monitoring and guiding long-term development. This is linked directly to poverty reduction, to optimising the delivery of services to the public, and to enabling the development of a vibrant private sector.

DECENTRALISATION

5.8 The need for political decentralisation is stressed in East Timor's Constitution. Decentralisation aims to provide more efficient delivery of services and decision making, with priority given to communities who understand their local needs and circumstances. The Plan proposes that capacity be built for this, through the provision of training for the administration of five regional offices for several ministries, backed up by regional coordinating bodies with representatives from government, community groups, NGOs and civil society organizations. To further these proposals, training is required to improve the management skills of district and deputy district administrators, local development officers, and sub-district coordinators. Such training could be developed and provided through the Office of District Affairs. Sector managers working at the district level also require relevant training, to implement, monitor and evaluate plan activities in their respective areas. Additionally, at the suco level, there is a need to develop programs to increase village capacity for plan implementation, and to provide support for developing capacity in local training institutions to provide sustainable assistance to local administrators. NGOs, church organizations and civil society groups can assist in this process, as well as developing civic education programs to facilitate local communities to monitor plan outcomes, in relation to their original "vision" statements in the Countrywide Consultation.

EMPLOYMENT

5.9 Entrepreneurial, technical, and vocational skills are lacking in every sector of the East Timorese economy. The Plan stresses that one of the most important challenges for East Timor, both currently and in the foreseeable future, is to create an adequate number of both formal and informal employment opportunities to meet the needs of the country's youth. Some 15-20,000 young East Timorese enter the working age population each year, far more than the anticipated number of jobs in the public sector. To meet their needs, the Plan argues for an extension of the current on-the-job training undertaken in informal economy workshops throughout the country, the design and implementation of basic training programs by employers in the formal sector, and a further development of existing donor and church programs in vocational training. To facilitate the development of technical and vocational training, the Plan proposes that the Government establish a unit responsible for Technical and Vocational Education and Training. The Labour Code passed by the Constituent assembly, due to be enacted on May 1st, 2002, requires that the Department of Labour and Solidarity establish a Division of Vocational Training and Employment, comprising three units – for skills development and upgrading, employment services, and labour market assessment. Additionally, community-based training centres are to be set up in the countryside, to train people in the skills needed in the local informal economy, and to provide advice on employment. These centres will also develop a basic skills-employment matching service.

EDUCATION AND LITERACY

5.10 Currently, standards of education in East Timor are among some of the lowest in the world. Illiteracy prevents approximately 50% of the population from participating fully, socially and politically. It also restricts the attainment of improved health standards. Most importantly, however, it limits national development, since literacy and numeracy are crucial for productive employment and economic growth. Consequently, the Plan focuses on capacity building for reconstructing and developing the education system – through prioritizing strategies for teacher training, increasing primary school enrolment, improving retention rates, modernizing the curriculum, and enhancing community involvement in the management of schools. One of the

most difficult tasks for schools in the years ahead will be to extend both the use of Portuguese language and the standardization of Tetun for use in schools –as required in the country’s Constitution. Again, the plan offers programs and projects through which this can be achieved – through language training for teachers and administrators, and the production of texts in the two languages. Most importantly, the Plan also details programs and projects to design a literacy manual, to extend existing donor literacy campaigns, and to develop new campaigns for implementation by the Ministry of Education.

HEALTH

5.11 Standards of health in East Timor are poor, and existing health provision is weak. Life expectancy ranges from 50-58, and is combined with high infant mortality rates of 78-149 per 1,000 live births, and under-5 years mortality rates of 124-201 per 1,000 live births. Women bear an unacceptable burden of maternal mortality and morbidity, with maternal mortality rates at 350-800 per 100,000 live births. Only 30% of births have any skilled birth attendance. Approximately 3-4% of children aged 6 months to 5 years are acutely malnourished, whilst 1 in 5 are chronically malnourished. About 45% of children under 5 are underweight. Almost all health facilities were destroyed in 1999, and there are acute shortages of doctors, nurses and midwives. To build capacity in this area will be extremely difficult, and the focus necessarily will be on the provision and delivery of services to meet basic needs. The Plan presents policies, and short and longer-term strategies for this. It prioritises ongoing, long-term programs in child, maternal and reproductive health. Crucially, it also focuses on current needs to build capacity for the provision of support services and management systems for the delivery of these programs.

INFRASTRUCTURE

5.12 As detailed in the *State of the Nation Report*, infrastructure is in a poor state, and capacity in this sector is extremely weak. This is an issue of overarching importance for all sectors of the economy and society, since infrastructure is a key determinant of agricultural productivity, poverty reduction, investment, human development and government capacity to deliver services. The Plan specifies detailed programs for building capacity in the key areas of water supply and sanitation, road reconstruction, and the restoration of basic transport and communication facilities. For the longer term, it specifies programs for the development of a sustainable power infrastructure, with an accompanying institutional framework. The substantial expenditures required for these programs highlight the crucial issue of financial constraints on infrastructure development. Here - perhaps more than in other sectors - there is a pressing need for prioritization and sequencing. Many of the programs suggested to the Planning Commission for funding may be necessary when viewed in the context of the developmental needs of the country over the next twenty years, but the key questions for the sector are, which programs are needed currently, which in five, and which in ten or twenty years from now. On this basis, a series of programs have been selected and designed in the Plan, focusing specifically on infrastructure needs in both the short and longer term.

THE JUDICIARY

5.13 A crucial area for East Timor’s development is an effective judicial system. Building capacity for this currently is a major problem. As outlined in the *State of the Nation Report*, one of the most pressing problems is a shortage of legal personnel. There are very few trained East Timorese judges, prosecutors and public defenders, and the courts have few resources. Developing the judiciary will require rapid capacity building in three areas: i) simplification of

legal procedures in both civil and criminal law to replace the current overlapping system with its heavy emphasis on procedure; ii) the creation of an independent, skilled judiciary, possibly through the formation of a judicial council to train and supervise judges; and iii) the development of a legal association to certify and train lawyers, establishing admissions criteria, and regulating legal conduct.

CONCLUSION

5.15 In most of the areas for capacity building outlined above, during the coming years, East Timor will need continuing international support. At least in the short term, to further capacity building and human resource development, there are positions which need to be filled by international advisers, working closely with local staff. Particularly crucial are positions with a high technical content, such as financial management, engineering, legal and judicial expertise. It is vital that this mentoring continue, particularly for the next five years, whilst East Timorese are in tertiary education, on leave of absence to learn requisite skills. For implementation of the Plan, it is crucial that the knowledge and skills appropriate for the attainment of economic growth, poverty reduction and human development be transferred and developed in an East Timorese context.

6. MONITORING, EVALUATION, AND REVIEW

"A comprehensive planning process with effective monitoring and evaluation will take into account what decision-makers need to know to make timely corrections..... the process must be participative, not one of unilateral decision-making by a small cadre of Ministers."

"This is East Timor's first Plan,....., it is important that it is reviewed at certain times to see if the overall strategic direction remains valid or if changes should be made."

INTRODUCTION

6.1 Planning for the future is an ongoing concern, and the National Development Plan is only the beginning of a structured planning process. The heart of the Plan is the national vision that reflects the hopes and aspirations of East Timor's people. It is a statement to indicate long-term commitment to human principles and constitutional concepts that provide leaders with a philosophical framework for development. However, the vision does not, in itself, provide insights about how to plan, to grow, to address poverty, or to adapt to an ever-changing world. East Timor faces all these challenges and many more, not least of all how to manage its financial resources during a very critical time of transition.

6.2 The Plan is, however, an initial framework that will grow, change, mature, and become systematically better with time and attention. This section of the Plan includes a description of a process that can ensure an effective monitoring and evaluation process, provide timely information to senior ministers who must decide the nation's goals and strategies, and establish administrative control of planning activities. The process will reduce the risk of the nation becoming entrapped by unexpected circumstances or untimely events. It will allow the nation's leaders to recognise unexpected opportunities or to act upon favourable circumstances. The ultimate aim is to nurture the nation's vision, bringing the nation and its people consistently closer to their aspirations for health, peace, equality, and prosperity.

6.3 Preparation of the Plan also involved policy development and the formulation of programs and projects. Experience from elsewhere shows, however, that the focus of planning has been largely on formulation, design and appraisal of programs and projects, without placing equal importance on monitoring and evaluating development plans and the implementation of their policies, legislative initiatives, programs and projects. That experience shows also that the lack of emphasis on monitoring and evaluation has led to major delays in implementation, underperformance of programs and projects, and a failure to learn from the lessons of past activities.

6.4 Monitoring and evaluation are critical components of successful national development planning exercises. Ensuring that policy objectives are met – through program and project activities – requires adherence to a sound process of monitoring and evaluation. Additionally, such a process meets the requirements of



Government, donors and other stakeholders for transparency and accountability. The main outcomes of strengthened monitoring and evaluation capabilities are improvements in program and project implementation and management.

6.5 Consequently, an institutional planning process is essential, one that empowers the nation's leaders with responsibility for strategic planning. The process itself must ensure continuity of monitoring and evaluation that will result in a living development plan, one that grows with the nation itself. First, it will provide timely feedback on actual performance by every agency within the Government's authority. Second, it will provide realistic projections and analyses of what the nation faces in the coming year, the next few years, and perhaps the long term. And third, the planning process will permit adaptation of the existing plan, its goals, objectives, and strategies. The key agency responsible for the various planning activities, including monitoring and evaluation, is characterised generically here as a 'Planning Commission', although it might be a quite different body to the currently existing Planning Commission.

6.6 The Plan, as noted above, is simply the beginning of the planning process. Planning responsibilities will now fall to a senior person in each 'sector' (Ministry, agency, or office of Director-General). Actual planning will continue on the model developed through the first national planning process, but include specific one-year action plans devised at department and division levels to implement the comprehensive long-term plan. This might consist of working groups and key managers at division level, with at least quarterly planning duties, and comprehensive long-range planning on an annual basis (these points are addressed below). No new staffing would be required. Indeed, the planning function is an appropriate responsibility for managers in these positions, although the planning activities should be highly participative.

MONITORING PERFORMANCE AND OBJECTIVES

6.7 Monitoring and evaluation are complementary yet different activities. Monitoring is the tracking and information gathering process that provides the data, insights, or descriptions of results in a systematic manner throughout a plan's life. This is a communication and reporting procedure, which is proposed here on the basis of quarterly 'feedback' and annual 'consolidation.' In contrast, evaluation is the process of analysing the information obtained through monitoring to determine what progress is being made, what problems exist, what successes have been achieved, and how task-related activities compare against planned outcomes. In this section, 'monitoring' is addressed separately from 'evaluation,' which follows in the subsequent section.

6.8 Monitoring involves the continuous assessment of program and project activities in the context of implementation schedules, and the use of program/project inputs by targeted populations in the context of design expectations. It is an internal program/project activity, an essential part of good management practice, and an integral part of day-to-day management.

6.9 Monitoring, therefore, is an important management tool, one that provides the basis for corrective actions to improve plan, policy, program and project design and implementation, along with the quality of results. It is a continuous assessment of the progress of policies, legislative initiatives, programs and projects with the aim of ensuring they achieve their policy objectives. Monitoring assists organisations – the Government and its Ministries and other agencies in this instance – to assess:

- a) the relevance of policy, program and project goals and objectives, along with legislative initiatives and reforms, on a continuing basis;
- b) efficiency in the delivery of inputs;
- c) effectiveness in the production of planned outputs and in fulfilling immediate objectives of policies, programs and projects;
- d) timeliness of policy, program and project activities and the adherence to the implementation schedules that have been developed; and
- e) problems encountered in the development process and possible remedial actions.

6.10 Consequently, a consistent and reliable monitoring process that addresses task-level performance indicators is essential. This will be achieved on several levels, including national, sector (Ministry or agency level), program, project and activity level. Monitoring (and evaluation) therefore requires a regular routine of preparing progress reports. The following reports and activities will comprise the 'backbone' of monitoring and evaluation in East Timor:

- a) quarterly policy, program and project performance reports;
- b) six-monthly or semi-annual policy, program and project performance reports;
- c) program/project site visits;
- d) annual review reports for sector-level activities;
- e) progress performance reports of large donor-funded programs and projects, as well as policies and legislative initiatives; and
- f) progress performance reports on policies, legislative initiatives, programs and projects.

6.11 Pro-formas need to be developed for each report to simplify the process of monitoring (and evaluation) and to ensure consistency in report preparation.

Monitoring at the National Level

6.12 The present Plan combines the outcomes of two separate but closely related visioning exercises – the Countrywide Consultation and the Ministry-level work of the Working Groups. Follow-up planning exercises could usefully follow the same format, with some activities being conducted on a nationwide basis and others being performed at Ministry level.

6.13 Some activities at national level will have a monitoring function. The TLSS, for example, provided a very detailed snapshot of living and working conditions in all regions and for all social and economic segments of the population. The Countrywide Consultation provided qualitative insights on the concerns and aspirations of a broad cross-section of society. Follow-up exercises at regular intervals, perhaps every 3-5 years, would be useful in measuring the progress being made in different areas and across a broad spectrum of indicators.

6.14 There is also a need for regular and close monitoring of macroeconomic indicators as these provide guidance on the general health of and changes in the economy. Such monitoring must be supported by monitoring policy development and implementation of policies. A Macroeconomic Policy Unit is proposed for the Ministry of Finance (MoF) for this purpose,

while such a Unit would also take responsibility for coordination with other key financial institutions such as the central bank (currently the Banking and Payments Authority – BPA). Macroeconomic skills are, however, in short supply, and capacity building and support in this area will be needed in support of national development.

Sector-level Monitoring

6.15 Each Ministry or agency, through the Working Group process, established development goals and long-term policies within a framework of guiding principles that reflect priorities of the sector under the national vision. In many instances, they extended a sector-specific vision to reinforce their commitment to national development. Because development goals and policies are long term and therefore do not change significantly over time, the reporting Ministry or agency should make a thorough review of its achievements with recommendations for changes at least annually. Interim reviews on a quarterly basis would be ideal but require additional resources.

Program-level Monitoring

6.16 Not all agencies or divisions within departments have formal programs to monitor. The offices of the Directors-General, for example, have activity responsibilities and priorities that they would pursue as part of their administrative roles. The Plan lists many of these as ‘programs’ with descriptive titles. Monitoring at this level will entail descriptive progress reports without specific performance benchmarks. For activity-specific programs that exist in line divisions, there are performance indicators or descriptive benchmarks associated with each relevant objective. Program managers should, therefore, be accountable for reporting quarterly on performance results or describing progress with respect to each objective for which they are responsible.

Project-level Monitoring

6.17 A ‘project’ is distinct from a ‘program’, comprising a well-defined set of tasks to be accomplished within a specific time frame and with a specific budget. In contrast, programs are commonly considered ongoing activities with a sense of permanence, such as a ‘trade promotion program.’ A project under trade promotion may be to establish trade legations with primary trading partners within one year. Therefore, all projects should have clearly defined and measurable performance objectives. There should be no ambiguity about whether a project is making progress, falling short, or has succeeded.

6.18 There are three categories of projects for East Timor. The first concerns projects that are budgeted and implemented entirely within the capabilities of the Government. The second comprises projects funded and implemented through the donor community. The third includes ‘all others,’ which may be the result of one-off bilateral agreements with a specific country, a contract with an international company for a turnkey project, or projects with allocations under trust funds or joint-development programs. In each instance, however, the projects will have well-articulated objectives and performance indicators that should be tracked quarterly and reported. Donors and bilateral participants not subject to direct reporting to government should make their progress reports available to the Planning Commission to ensure transparency and effective planning.

EVALUATION OF PERFORMANCE RESULTS

6.19 Evaluation may be defined as an assessment, which is as systematic and objective as possible, of an ongoing or completed program, project or policy, its design, implementation and results. Normally, evaluation occurs at the completion of a program or project, or at the completion of a particular stage of such a program or project. Consequently, the purposes of evaluation are

- a) to provide an objective basis for assessing the performance of programs, projects, policies and activities;
- b) to improve programs and projects through feedback on the lessons learned; and
- c) to provide accountability, including provision of information to Government, donors and other stakeholders, including the general public.

6.20 A formal evaluation process must be developed in East Timor to provide the Council of Ministers with a consistent and accurate assessment of results throughout the government sectors. Donors invariably structure their projects with internal reporting and evaluation systems and, while all donors have their own methods of evaluation, their evaluation framework is similar. They will provide government planners with realistic summations of their activities and projects on a timely basis that will be sufficient for the CoM to fully comprehend how all programs and projects are progressing.

6.21 The challenge, therefore, is for East Timor to create a comparable system. This is not necessary to simply placate donors (yet donors will want periodic verification of how the recipient ministries and agencies are performing), but to provide East Timor's leaders with the most accurate diagnostics possible to help them steer their country toward its goals. Such a system cannot be driven by financial priorities – a plan that is forced into a budget is not a plan at all, but an 'allocation process.' The system must produce scenarios of both social and economic performance, and subsequently be judged in light of all development indicators. Budgets are vital, first of all, as 'tools' for tracking, keeping score, and quantifying results in universally understood terms. They are equally important for allocating resources, but only within a fundamental framework of an effective national development plan. Financial budgets become the standards for allocation and the mechanisms for assessing time-phased activities. An effective evaluation system must have the components of planned objectives articulated in measurable benchmarks, a method of analysis, and a correction process. These components are addressed below.

Planned Objectives

6.22 Objectives, as defined in the Plan, are the operational results to be achieved. They are typically described within programs or projects, or as role expectations for managers (such as directorates' responsibilities to draft bodies of regulations). Objectives also are typically defined within a time frame and are measurable. For example, an educational development plan or a program for reducing poverty, have individual time-phased objectives, but must also be orchestrated with all other governmental activities and, therefore, considered within a budgeted resource and finance framework.

Measurable Benchmarks

6.23 Performance indicators are the predominant benchmarks used in program and project management. These are both quantitative and qualitative results that not only define when objectives are met, but provide timely points of assessment to ensure that planned activities are being effectively implemented. Similar patterns of performance benchmarks, dealing with such matters as timeliness of implementation, cost and project results, are required for every program and project and, indeed, for any initiative that occurs through government for which the political leadership is responsible.

6.24 Benchmarks should be appropriate to measure the intended performance, sufficient to inform decision-makers as to the results (or to corrections needed to remain on-course), and feasible within the constraints and abilities of those accountable for results. Consider, for example, the national goal of 'reducing poverty' and one task-related objective to be 'to reduce the number of people living below the poverty line.' This objective may be further refined to a measurement such as 'reducing the number of people living below the poverty line by five percent within one year.' The appropriate benchmark would be to count the number of people currently living below the poverty line, and count that number again at the end of one year. This measurement may also be sufficient to inform decision-makers as to the results, but perhaps it may not. Decision-makers may also want to know where progress has been made (who was affected, who benefited from poverty reduction programs), how they achieved the added income to rise above the poverty line (by earned income, a currency manipulation that distorted results, or a per-capita GDP measurement that averaged out national product when only a handful of the elite made windfall profits and most people remained poor). Consequently, an appropriate benchmark is one (or a set) of performance indicators that provide sufficient information to decision-makers about the real results of planned activities. Finally, the measurement must be feasible. That is to say, the objective must be attainable (five percent reduction in the number of people below the poverty line in one year may be unrealistic or perhaps even too modest), and the programs implemented to achieve this must have the human, material, and financial resources to succeed.

6.25 The role of budgets, as indicated earlier, is critical to all plans. However, there are different types of budgets used in planning, but budgets should not drive plans. A financial budget is essential to allocate scarce monetary resources, and it subsequently becomes a numerical measurement on which to track and analyse performance. The role of a budget office, however, is to carefully accumulate data and to address all aspects of transactions and financial data monitoring. Analysis may be delegated to a budget office or to another unit (as discussed in the next section). The point here is that a financial budget is only part of the evaluation equation. Operational budgets are also required, and often they are equally important to financial budgets. They include staff mobilisation plans and targets for staff resources (measured in person days per project, number of work hours, levels of effort, and many other criteria). They include material budgets and procurement levels, time budgets, and various measurements on social issues (such as access to or distances from health clinics). The important point is that almost all activities and resources can be budgeted in measurable terms such as money, time, numbers, percentages, or quality standards, among others. They still must be appropriate, sufficient, and feasible to qualify as useful performance indicators.

Methods of Analysis

6.26 Designing and implementing a monitoring and evaluation system is a significant project requiring experts in planning and monitoring systems, and specialists in developing analytical procedures. A budget office can be highly effective for tracking and evaluating financial budget

performance. The reason should be clear. Financial budgets comprise only a small part of the total planning and monitoring system. Human resource capabilities, asset management, regulatory performance, trade activities, foreign affairs, and many other issues make up a majority of the components within a national development plan. Each of these has its own set of tasks and objectives, and each must have performance indicators or means of describing whether they are being effectively implemented.

6.27 For most development programs and a majority of donor projects, the methods are similar. They will define the benchmarks and performance indicators, and establish a time-phased system of tasks required to accomplish their objectives. This system will be broken down into stages, such as quarterly increments of task activities, and the indicators will be prorated to each of these incremental stages. Therefore, reports will provide assessments of partial task results and compare these against 'budgeted' or expected results for each operational period. The techniques of evaluation will almost always take the form of variance analysis, and be reported in easy-to-understand statistics. Variances can be calculated as absolute numbers (so many dollars under or over-budget, so many under or over-utilised staff compared to staff schedules, and so on), or by percentages (a certain percentage under or over budget for purchased assets, number of people trained, and so on). More sophisticated economic models are often necessary for variances in monetary or fiscal performance, trends in income, trade, or investments, asset depreciation, technology development, industry capacity, and other macro factors.

6.28 A nation's development, however, cannot be entirely reduced to numbers and analyses. A great many objectives are concerned with social, cultural, and behavioural dimensions. Poverty, for example, may be reduced to a definition of per capita income, yet the form of that income may be meaningless; a depreciating monthly cash income, even if the nominal amount is rising rapidly, may translate to even more wretched conditions for the individuals caught up in these circumstances. Cash money, even if sufficient to a rural family that cannot access health care or schooling for children seems hollow. A fully employed economy – if such a thing could exist – may still be abhorrent if the population is ruttled in meaningless work and destitute conditions. Measurements of legislative endeavours, regulatory reforms, types of foreign investment, East Timor's presence in the region as a trading nation, political stability, cultural preservation, environmental protection, national security, and many other similar concerns require very creative methods of evaluation. These cannot be addressed fully in this report, yet they will be required for East Timor to have an effective and complete national planning, monitoring, and evaluation system.

Correction Process

6.29 The correction process completes the cycle, and it is where the CoM, with support and information from donors, from the budget office, and from the body set up to oversee planning implementation, will steer the ship of state. In order to meet their responsibilities, they must have ready access to crucial information that is accurate and reliable, and they must have that information when it is needed. The 'instrumentation' of monitoring and evaluation provides that assortment of information. The ultimate objective is to have informed and enlightened decision-makers capable of correcting the direction of the plan.

6.30 Corrections are essential to remain realistically on course but, most importantly, to avoid major and unforeseen disasters. Without regular feedback and appropriate analysis, they cannot make such decisions, and the timing of information can vary significantly. For example, feedback from a nationwide survey of the population's perceptions about social and economic development may be important, but it may not be critical enough to cause planning to be repeated more than every few years. In contrast, a program aimed at repatriating indigent

refugees may require monthly or even weekly monitoring. Those situations of higher risk than others require more deliberate monitoring intervention, and those that could have greater consequences than others require greater attention.

6.31 A comprehensive planning process with effective monitoring and evaluation will take into account what decision-makers need to know to make timely corrections. In addition, the process must be participative, not one of unilateral decision-making by a small cadre of Ministers. They will need to work with the planning specialists, donor representatives, and budget analysts to fully address each issue, then to communicate decisions with a consensus of agreement on changes or adaptations. Ministers will need to work closely with their department heads and directorates to share information and to involve them in the planning and evaluation system. This not only builds capacity systematically throughout government, but also progressively advances the plans and all task activities toward achieving the nation's development goals. In effect, each iteration of the monitoring and evaluation cycle improves the plan, improves operational performance, sharpens objectives and their related indicators, improves human resource capabilities, and moves the nation steadily toward fulfilling the vision for national development.

PLANNING REVIEW

6.32 'Review' and 'evaluation' are often used interchangeably. However, a distinction can be made between them, with that distinction relating mainly to the purpose, timing and level at which the activity occurs. As noted above, evaluation tends to be focused on assessing how well programs, projects or policies are performing, and it may occur at various stages during the lifetime of an activity. Review tends to occur at a higher level and may influence the overall strategic direction being taken by the organisation which, in this case, is the Government of East Timor. This is East Timor's first Plan and, consequently, it is important that it is reviewed at certain times to see if the overall strategic direction remains valid or if changes should be made. Two matters are important here:

- a) because the national budget is based on a three-year, medium-term fiscal framework, the national strategic plan needs to be reviewed each year so that it 'rolls forward' and remains consistent with the Budget; and
- b) because the Plan is East Timor's first, it should be subject to a full review after its first year of operation (meaning that the review would be due in July-August, 2003). The review should involve external support and personnel, along with domestic inputs and personnel in a team approach.

6.33 As the Plan's policies, programs and projects are implemented, user surveys and other means should be used to monitor the outcomes of the programs against the intended results, according to the performance indicators or benchmarks established in the Plan. Such evaluations should focus on the cost-effectiveness of spending, analysing and explaining reasons for any cost overruns or shortfalls in outcomes that may have occurred.

INSTITUTIONAL SETTING: MODEL OF PLANNING, MONITORING AND EVALUATION

6.34 On completion of the Plan, the Planning Commission will be disbanded. There is, however, a need for a Government body with responsibility for overseeing national development planning functions, particularly monitoring and evaluation. In many countries such a body is

located either in the Prime Minister's Office, in the Ministry of Planning, or - less frequently - in the MoF²⁴. In East Timor, there is a need to find a suitable institutional location for such a body. It should be located within an institution or office which can have an overview both of planning operations, and of the role of government, civil society and community organizations in plan implementation. For it to be credible, this organization must have a significant degree of autonomy, and be able to involve stakeholders in implementation, monitoring, and assessment. The location of the government body overseeing implementation of the Plan should be decided after independence, and should involve discussions with government ministers, civil society organizations and the main stakeholders already involved in the planning process. The body set up must ensure that adequate participatory processes are established to enable all stakeholders to be involved in the monitoring of plan implementation. Since the vision statements of the East Timorese population were crucial in designing and giving direction to the Plan, it is vital that groups representing their interests within the community and civil society are fully represented in monitoring and evaluation of plan implementation. Those monitoring the plan should be trained in participatory methods, and indicators devised for this monitoring should be based upon participatory approaches and techniques

6.35 Individual ministries will also require some planning capability, including the capacity to undertake monitoring. The use of pro-formas will allow individual officers to undertake regular monitoring. However, at least in the larger ministries, the establishment of an internal policy and planning unit could support project preparation, implementation, monitoring and evaluation, and review. Such a unit could also provide the link to the national-level monitoring body, outlined above, as well as a contact point for donors and other stakeholders.

6.36 The routine involvement of stakeholders, outlined above, and other partners, notably the donor community, will be instrumental in ensuring that planned future donor activities be based on an accurate knowledge of experience with current programs, and a regularly updated awareness of the Government's priorities. Regular joint sector missions by donors could be planned to take place shortly after quarterly updates become available. Such missions could be provided with the latest information, to avoid placing a supplementary reporting burden on the government.

CONCLUSIONS

6.37 Following independence, the Government should establish a new body with responsibility specifically for overseeing national development planning functions, particularly monitoring and evaluation. This should have a significant degree of autonomy, and should be located within an institution or office which can have an overview of planning operations, the role of government, agencies, and civil society and community organizations in plan implementation. This new body will have to draft a policy statement that captures its responsibilities, relationships with the budget office, donor coordination, and respective line ministries. A general framework for planning and reporting should be instituted so that a pervasive process can be implemented with consistent models of quarterly and annual reports that follow upward from project and program levels to ministries or agencies, and then to the new overseeing body.

²⁴ The monitoring and evaluation suggested here has a much broader focus, and is distinct from that which will be undertaken for the medium term fiscal framework (MTFF)

6.38 The reports submitted to the organisation overseeing plan implementation should be aggregated summaries, and they should include both the quantitative and qualitative analyses of results prepared through monitoring and evaluation. The overseeing body will have to have capabilities for economic evaluation and forecasting, social and environmental evaluations, and various specialised analytical tasks. The budget office within the MoF will be responsible for financial monitoring and analyses, and a statistics division will be accountable for such issues as population and demographics, healthcare, education, employment, and labour data.

6.39 Each division would be responsible for annual plans (action plans) that capture program and project activities, structured with quarterly performance indicators that meet the full criteria of being appropriate, sufficient, and feasible. Line ministries would have aggregated plans that reflect these annual action plans that, taken together over time, could provide the basis for long term (five-year) national development plans. In effect, at the end of each year, the process of rolling these annual plans forward can generate new 'five-year' plans (not merely second or subsequent years to one five-year plan that eventually must be replaced with new and extensive long-term criteria). This can be achieved by extending the fifth year every year as a new annual plan emerges. However, this is a policy decision. At minimum, the annual results should produce a revised set of plans for the upcoming year whilst also providing the overseeing body with greatly enhanced information on subsequent years.

6.40 Ultimately, the planning process should not be budget-driven, nor be subordinated to international financial mandates. It should address the social, economic, and human development priorities of East Timor and, with appropriate diligence, consider what can be realistically accomplished given budget constraints. All proposed programs and projects put forward by the divisions in all sectors should remain within the development plans, even if they cannot be feasibly pursued in the near term. They should not be lost for current lack of resources or capacity, but simply prioritised given the nation's limitations. Finally, the planning process should be fully participative, linking each level of government, and fully involving civil society and community organisations in planning, monitoring, and evaluation activities.

PART 2

ECONOMIC OUTLOOK

Chapter 7. MACROECONOMIC POLICY FRAMEWORK

Chapter 8. MEDIUM TERM ECONOMIC AND FINANCING
OUTLOOK



7. MACROECONOMIC POLICY FRAMEWORK

VISION

7.1 To sustain our vibrant traditional culture and beautiful environment, while moving to faster growth in production and employment, so as to provide significant improvements in opportunities, living standards and services for all East Timorese. Central to achieving our vision will be the management of our economy and finances in efficient, transparent and corruption free ways.

INTRODUCTION

7.2 This chapter focuses on the policy framework for macroeconomics and public finance, mainly over the five-year planning period, but also in relation to the longer term. The related *State of the Nation* Report addressed itself to recent macroeconomic and public finance policies and conditions in East Timor and should be read in conjunction with this chapter, which is essentially forward policy oriented in nature. Chapter 8 (Medium Term Economic and Financing Outlook) of this document also addresses related macroeconomic issues.

7.3 With the onset of political independence come additional and challenging responsibilities for managing the national economy and public finances. Aspirations and expectations of the people are high. Sound but creative macroeconomic and public finance policies will be needed over an extended period if hopes and expectations are to be met.

7.4 East Timor is still recovering from the extreme difficulties of long periods of external rule, which culminated in the 1999 emergency. Significant further economic adjustment will be needed over the next two to three years as the United Nations fully withdraws and as current investment programs from bilateral donors and the Trust Fund for East Timor (TFET) reduce in size, and in some cases terminate completely.

7.5 In these circumstances the immediate challenge is to consolidate on the economic institutions and framework that have been put in place and particularly to ensure that public finances are placed on a sound and sustainable medium term path. Provided the transition away from the United Nations period is successfully manoeuvred over coming years, the outlook for East Timor is very bright, with the prospect of steadily improving and broadly based growth for decades to come, particularly following the onset of oil production from the Timor Sea and as political liberation leads to economic transformation and improved efficiency throughout the country, especially in agriculture.

7.6 Successive periods of external rule have left East Timor with a fragile economic base and quite low levels of domestic revenues as it commences Independence. Prospects appear bright from around late in the decade that both domestic and foreign resource constraints will ease with the onset of petroleum

and gas production from the Bayu Undan project in the Timor Sea. However, continuing assistance from the international donor community will be critical, not only in the years leading up to this project, but also well beyond it. This Plan asks donors to accept a heavy burden of responsibility for seeing through the generous initial assistance which has been provided. Any move to premature withdrawal on the part of donors would be counter productive for all, and place at risk the important advances made to date. In the short-term, over the next three years, donors are being asked to provide further financial resources to keep basic operations running efficiently and to allow for development of the Government's own modest investment program. In the longer term the need will change more to assistance with the development of capacity and the building of physical and social infrastructure.

GOALS

7.7 The goals for the sector are as follows:

General Goals

- a) Improved capacity and institutional performance of the key central economic Ministries/Agencies (including effective and transparent management approaches).
- b) Reducing poverty.

Macroeconomic Goals

- a) High and sustainable economic growth, particularly in the non-oil economy.
- b) Low inflation.
- c) Growth in employment/decline in unemployment
- d) Stronger banking and finance sector.
- e) Strengthening the external situation (competitive real exchange rate and open trading system).

Public Finance/Fiscal Goals

- a) To pursue growth of budget revenues to improve financial independence.
- b) To effectively manage oil and gas revenues and savings.
- c) To responsibly and productively manage budget expenditures.
- d) To effectively manage the budget deficit and its financing (especially effective aid management, including negotiation of a medium term aid agreement).

GUIDING PRINCIPLES

7.8 Broad principles that will guide economic policy development and the management of the economy and public finances are as follows:

- a) Market economic system; but with strategic and regulatory roles for Government, including the provision of a social safety net during difficult times.
- b) Strong role for the private sector in development.
- c) Open trade and investment policies.
- d) Government's role will be limited to ensuring that physical and social infrastructure and services are provided and to establishing a growth enabling policy and legal environment; including provision of macroeconomic stability.
- e) There are particular areas Government will not venture into, including operating commercial business ventures such as banks and airlines, regulating/controlling prices, or trying to pick winners and providing subsidies/exemptions to particular businesses or industries.
- f) Effective, transparent and corruption free management of the economy and public finances.
- g) Pursuing a fair and equitable economy and society with equal opportunities and improving living standards for all.
- h) Developing in ways that preserve the beautiful environment, traditions and customs of East Timor.

CONSTRAINTS

7.9 While the future is approached with confidence and optimism, there is need to recognise, and address over time, constraints to broadly based economic development, including the following:

- a) The aftermath of conflict has left some people weary – there is a need to consolidate and build confidence while commencing pursuit of economic growth.
- b) The conflict destroyed a lot of property and assets; so property and assets need to be restored as part of the development effort.
- c) Many in the rural areas are used to leading a dualistic subsistence/cash farming lifestyle where production of sufficient food crops to sustain life is of paramount importance. Achieving major transformation and modernisation in the rural areas is a major challenge. Rural/urban imbalances are significant.
- d) The population is young and many young (and old) people cannot get jobs. Without the creation of jobs youth problems and social unrest may develop.
- e) Managing the economy and public finances is a new responsibility for many East Timorese leaders and civil servants. There is need for rapid learning, institutional development and capacity building in macroeconomics and public finance.
- f) With low growth and low per capita incomes, domestic revenue collections are very low. There are limits on the extent to which new public services can be provided, meaning in the short-term high dependence on aid inflows.

- g) The banking system was destroyed in 1999 and needs to be further rebuilt to ensure savings, credit and other financial instruments are available to all the people, and that the people gain confidence to use them. Further legislative reform is likely to be necessary to support financial sector development.
- h) Since 1999 wages have grown very rapidly and the US Dollar has continued to be very strong. Should these trends continue, or should further domestic inflation emerge, then it will be increasingly difficult to compete internationally, particularly until the productivity of labour grows. Economic management will need to closely monitor trends in currency and wage competitiveness. If the package of policies being introduced is not providing for production and employment growth, then bolder measures will need to be considered with currency and wages policies.
- i) Domestic savings and domestically financed investment are both low and need to be enhanced. Over the medium term generating savings and investment from oil earnings and direct foreign investment will be important.
- j) The private sector needs to play a key role in development. Yet for the moment it is weak and will need time, support and an appropriate operating environment to develop (particularly important will be the development of appropriate legislation: company law, foreign investment law, and secure land tenure for investors).
- k) More education and training is needed at all levels, from primary through to tertiary education and vocational training to equip the community with the skills to grow a modern economy.
- l) The health of the population also needs to be improved, especially from energy sapping diseases like malaria, if the productivity of workers in agriculture and the broader economy is to be raised.
- m) Without improved infrastructure (power, roads, transport, communications) it will be difficult to develop either the agricultural sector or industry.

OVERVIEW OF POLICY CHALLENGES

7.10 The overriding goal is to achieve high growth in production and employment. This will be no easy or short-term task. Most growth during the Indonesian and UNTAET periods was generated by high levels of public expenditure. Yet it is clear that combined sources expenditure will fall sharply in the immediate years ahead, thereby acting as a negative force on growth. Future growth must be largely generated by the private sector (including agriculture), but the private sector is currently small and weak. In the short term the UNTAET period has seen wages rising to levels well above those of competitors in Indonesia and elsewhere in the region, with resultant losses in production and jobs. At the same time the extreme strength of the US Dollar since 1999 has further worsened competitiveness. There is also a need to remove impediments to investment, and for the development of laws and institutional arrangements covering land and property rights, foreign investment, lenders collateral and a sound regulatory environment, as well as policies to address inadequate infrastructure and low skill levels in the labour force.

7.11 Recent trends make for a very difficult starting position from which to generate future private sector growth. Short-term economic management will need to closely monitor trends in currency and wage competitiveness and growth. If the package of policies being introduced is not providing growth then bolder measures will need to be considered with currency and wages

policies, particularly as the BPA develops over time the economic management and institutional capacity to run independent monetary and exchange policies.

GOALS, POLICY ACTIONS AND PERFORMANCE INDICATORS

GOAL NO. 1: INSTITUTIONAL STRENGTHENING

7.12 To further strengthen institutional and human capacities in the main central economic institutions (MoF, BPA and MEAD).

Policy Actions for Goal No. 1

- a) Develop corporate plans for key institutions and manage to them.
- b) Undertake a training and staff development needs assessment study and regularly update.
- c) Develop a Human Resources Development Plan for key institutions.
- d) Establish Personal Development Plans for all officials, to include training needs, and to provide for annual assessments.
- e) Develop succession plans for all line positions held by expatriates.
- f) Develop small Economic Policy/Research Units in the MoF and the BPA.
- g) Locate all planning, economic policy and aid coordination functions under one roof, possibly in the MoF - apart from monetary matters to be the responsibility of the BPA.

Performance Indicators for Goal No. 1

- a) Effectively implement all seven policy actions above.

GOAL NO. 2: POVERTY REDUCTION

7.13 To eliminate poverty over time while maintaining an equitable distribution of income and wealth.

Policy Actions for Goal No. 2

- a) Foster a social and political climate supportive of eliminating poverty and maintaining equity.
- b) Promote opportunities for participation and advancement of all members of the society.
- c) Provide opportunities for empowerment of the people as key agents of government processes.
- d) Provide security for all, including: human rights, freedom from hunger and relief from disasters.
- e) Design and manage macroeconomic policies in pro poor ways.

- f) Provide stable economic and political conditions as a prerequisite for assisting the poor.
- g) Implement equitable tax and revenue policies.
- h) Spend government budget money in sectors and within sectors to benefit the poor.
- i) Ensure expenditure allocations allow for an equitable balance between rural and urban areas.
- j) Ensure foreign aid programming is appropriate to national needs, including poverty reduction.
- k) Set monetary and exchange policies so as to support growth, stability and poverty reduction.
- l) Ensure banking, credit and micro finance services are broadly available to the poor.
- m) Implement open trade and investment policies to promote growth to benefit the poor.

Performance Indicators for Goal No. 2

- a) Gini Ratio (currently 0.37) to remain relatively stable over the short and medium term.
- b) Percentage below poverty line of US\$0.55 (currently 41%) to reduce markedly within five years.
- c) Adult illiteracy rate (currently about 50%) to reduce markedly within five years, and halve within 20 years.
- d) Primary school participation (net enrolment rate, currently about 70%) to increase significantly in five years.
- e) Infant mortality rate (currently estimated between twelve and fifteen percent) to decline significantly below eight percent within five years.
- f) Walking time to nearest health clinic (current average 70 minutes) to be reduced in five years.
- g) Maternal mortality rate (currently between 0.4% and 0.6%) to decline within five years.

GOAL NO. 3: PURSUIT OF ECONOMIC GROWTH

7.14 To achieve high, sustainable, and broadly based growth (with stability and poverty reduction).

Policy Actions for Goal No. 3

- a) All macroeconomic policies to be framed as a consistent package to be conducive to growth.
- b) The package of macroeconomic policies to provide for international competitiveness.

- c) All sector policies to be framed as a consistent package conducive to growth (especially policies for agriculture; infrastructure; education; health; regional/rural development; and private sector development).
- d) As 75% of people work in rural areas, but agriculture contributes only around 25% of GDP, sector policies with regard to the transformation of agriculture will receive high priority.
- e) Both public and private sectors of the society will be provided with a policy environment conducive to saving. Foreign investment will be encouraged, as will savings from Timor Sea revenues.
- f) Market oriented mechanisms will allow for higher savings to be channelled into higher capital formation (both private and public – including social capital investment) to support growth.
- g) The package of macroeconomic and sector policies aims to see development of a strong and energetic private sector with much of growth private sector led. This will include related legal reforms in areas such as foreign investment, land tenure, company law and lenders collateral.
- h) Education sector policies (including well-targeted vocational and entrepreneurial education) will be given priority to improve the base knowledge and skills of the workforce.
- i) Health sector policies will receive priority to ensure the basic level of health of the workforce.
- j) Infrastructure policies and investments will be targeted to facilitate growth.
- k) Initial growth is likely to be labour intensive with low to semi-skilled businesses. Policy will support this, but will be ready to move to more mature stages of growth as investment and skills emerge.

Performance Indicators for Goal No. 3

- a) After a likely slump in growth, during the transition away from the UN period, underlying Non-Oil growth by the end of the planning period will reach sustainable levels of five to six per cent per annum.

GOAL NO. 4: PURSUIT OF LOW INFLATION

7.15 To achieve a low level of inflation.

Policy Actions for Goal No. 4

- a) Responsible monetary/currency policy (price stability is the prime objective of the BPA).
- b) Restraint on wages growth (particularly public sector).
- c) Responsible budget policies, with declining deficit levels and zero borrowing.

Performance Indicators for Goal No. 4

- a) Consumer price index inflation in East Timor to be no higher than USA consumer price index inflation over the five years of the Plan (around two to three percent per annum).

GOAL NO. 5: PURSUIT OF MORE EMPLOYMENT

7.16 To achieve growth in employment/decline in unemployment.

Policy Actions for Goal No. 5

- a) Pursue a similar package of policies as those proposed to promote economic growth (see Goal No. 3).
- b) Consistent and supportive package of macroeconomic policies.
- c) Supporting sector policies: agriculture, education, training, youth, health and infrastructure.
- d) Internationally competitive wages, exchange rates, and trade policies.
- e) Encouragement of higher domestic and foreign savings and investment levels.
- f) Promoting conditions conducive to growth of the private sector (laws, land arrangements, labour market information; banking development, vocational training and education).
- g) Gearing policies to support labour intensive growth initially (with high importance given to flexible and moderate wages policy linked to productivity movements).

Performance Indicators for Goal No. 5

- a) Open unemployment rate to decline significantly from recent levels of around 17% of those actively seeking work.
- b) A significant number of new jobs will be created each year.

GOAL NO. 6: PURSUIT OF STRONGER BANKING AND FINANCE SECTOR

7.17 To promote development of a stronger banking and financial sector.

Policy Actions for Goal No. 6

- a) Review and upgrade Banking and Financial Legislation, including Governing Board oversight of BPA, funding and accountability of BPA, and movement to full central banking functions (in line with April 2002 recommendations of the IMF – Preparing for a Central Bank of East Timor).
- b) Maintain appropriate international (mainly Basle) standards for licensing and regulation.

- c) Promote more competition and increasing numbers and types of private banks and financial institutions (including widening rural presence by private banks and the BPA).
- d) Develop regulations and capacities to promote growth of insurance (both general and life).
- e) Develop regulations and capacities to promote growth of private superannuation and other savings schemes (including increased saver education and enhanced security for savings).
- f) Support donors and NGOs to develop micro savings and credit schemes, especially in rural areas.
- g) Develop related Laws important to the expansion of credit to the private sector (Company Law; Contract Law; Collateral Law; Bankruptcy Law; Foreign Investment Code; Land Laws).
- h) Government (mainly through BPA) to increasingly undertake a near full range of central banking type functions and to be a catalyst for significant growth of savings and credit in the sector.

Performance Indicators for Goal No. 6

- a) Effectively implement all eight policy actions above (particularly to increase the range of private sector institutions and products and to significantly expand savings and credit) within the five-year period of the Plan.

GOAL NO. 7: PURSUIT OF A STRONGER EXTERNAL SECTOR

7.18 To achieve a stronger external situation, including a competitive real exchange rate, higher exports and an improving trade balance.

Policy Actions for Goal No. 7

- a) Pursue responsible expenditure policies to constrain domestic demand to levels that can be sustained from domestic revenues and foreign grant aid (without public borrowing).
- b) Pursue a competitive real exchange rate (exchange rate adjusted for inflation), especially in relation to agricultural competitors.
- c) Maintain competitive wage and trade policies to allow competition in export markets and to enhance the ability of domestic producers to compete with imports.
- d) Promote sector policies supportive of private sector growth in exports and improved competitiveness in relation to imports (especially agriculture and agro processing).
- e) Maintain open (low effective protection) trade and investment policies, including moving to observer or membership status of such bodies as ASEAN and WTO.
- f) Pursue diplomatic efforts to increase access rights to key markets; Europe; Australia; and Asia.

Performance Indicators for Goal No. 7

- a) No significant real effective appreciation of the currency over time.
- b) Non-oil merchandise exports to recover significantly from recent negligible levels.
- c) Non-oil and non-aid related merchandise imports to decline to more moderate levels so narrowing the current imbalance on the non-oil/non-aid related trade balance.
- d) Positive overall balance of payments to be achieved without recourse to public foreign borrowing.
- e) By the end of the Plan period net foreign reserves will be in the early stages of a large long-term build-up (mainly from savings policies in relation to Timor Sea oil and gas).

GOAL NO. 8: PURSUIT OF IMPROVED REVENUE COLLECTIONS

7.19 To increase revenue collections to enhance fiscal autonomy, while retaining incentives for private sector development and ensuring equity for the poor.

Policy Actions for Goal No. 8

- a) Maintain existing package of tax and non-tax revenues, while reviewing their appropriateness regularly (including likely introduction of some recommendations of the IMF Mission on tax and revenue policy in the context of the FY 03 Budget).
- b) Improve administrative resources, systems and skills to raise collection yields and levels.

Performance Indicators for Goal No. 8

- a) Domestic (non oil) revenue as a percent of GDP to grow from current levels of five percent of GDP to approach seven percent of GDP by the end of the Plan period.
- b) Collection yields for existing taxes to show at least a 25% improvement over the Plan period.
- c) Any new taxes introduced to be consistent with equity and poverty alleviation goals.

GOAL NO. 9: MAXIMISE COLLECTIONS AND SAVINGS FROM TIMOR SEA REVENUES

7.20 To maximize collections of Timor Sea revenues and to save and sustainably manage significant proportions of them.

Policy Actions for Goal No. 9

- a) Install very strong, internationally competitive resource skills in the MoF/Revenue Service, to ensure regular tax audits and collection of all petroleum taxes due.
- b) Development of effective offshore savings and investment mechanisms, based in part on findings of the Norwegian Technical Assistance Mission undertaken in March 2002.

Performance Indicators for Goal No. 9

- a) Rigorous annual scrutiny of taxation returns and 3 yearly detailed tax audits.
- b) Build up of a secure and growing stock of offshore investments, in line with recommendations of the Norwegian Technical Mission and consistent with estimates published in the MTFF.

GOAL NO. 10: PURSUE CREATIVE AND EFFECTIVE EXPENDITURE PROGRAMS

7.21 To pursue creative and effective expenditure policies; including: (a) restraining total expenditure to levels that are sustainable; and (b) ensuring that expenditure allocations between Agencies/Functions are consistent with plan objectives and particularly that currently high central administration expenditures fall to the benefit of priority areas of health, education, agriculture and infrastructure.

Policy Actions for Goal No. 10

- a) Improving the capacity of all public officials to prepare and manage effective budgets.
- b) Use of MTFF to control aggregate expenditure.
- c) Use of MTFF to determine the current/capital expenditure split.
- d) Use of MTFF and work of Planning Groups to determine an appropriate allocation of expenditures.

Performance Indicators for Goal No. 10

- a) Total expenditure to grow at an annual average rate, which is in line with the (sustainable) MTFF.
- b) Average proportions of current/capital expenditure over the plan period to be in line with responsible levels contained in the MTFF.
- c) Expenditure allocations finally determined by CoM as being appropriate to be implemented with close monitoring over the 5 years in line with MTFF allocations.
- d) Currently high shares of central administration expenditures to fall to the benefit of priority areas of health, education, agriculture and infrastructure.

GOAL NO. 11: PURSUE APPROPRIATE DEFICIT AND FINANCING POLICIES

7.22 Budget deficit levels to reduce sharply over time with any deficits to be grant and not debt financed; and donor grant deficit financing over time to be in line with a Public Investment Program developed by the Government.

Policy Actions for Goal No. 11

- a) MTFF in conjunction with donor negotiations to plan for gradual deficit reduction as domestic and Timor Sea revenues grow.

- b) A preferred forward Public Investment Program to be developed over time and then to be updated annually with significant improvements in project identification, preparation and appraisals over time.

Performance Indicators for Goal No. 11

- a) Total deficit to fall sharply by the end of the Plan period, in line with MTFF estimates.
- b) Government preferred forward Public Investment Program in place and improved on annually.

SUMMARY OF PROGRAMS / PROJECTS SPECIFIC TO MACROECONOMICS / PUBLIC FINANCE SECTOR

Table 7.1: Recent and Forward Estimates of Program / Project Expenditures (US\$ 000)

Item	FY 00 Actual	FY 01 Actual	FY 02 Revised Budget	FY 03 Prelim. Budget	FY 04 Estimate	FY 05 Estimate	FY 06 Estimate	FY 07 Estimate
1. Banking and Payments Authority								
CFET Operations	26.5	1,374.0	1,374.0	1,325.0	963.0	1,026.0	1,092.0	1,150.0
(Of Which Own Revenues)	(0.0)	(0.0)	(0.0)	(245.0)	(350.0)	(450.0)	(550.0)	(650.0)
U.N. Assessed Contributions	0.0	1,060.0	933.0	900.0	800	0.0	0.0	0.0
Total	26.5	2,434.0	2,307.0	2,225.0	1,763.0	1,026.0	1,092.0	1,150.0
2. Ministry of Finance (Minister; Core CFA; Customs;								
TFET Taxes; Payroll; External Audit; Others – but excluding Contingencies / Reserves):	35.0	917.0	1,698.0	2,247.0	2,221.0	2,348.0	2,300.0	2,200.0
CFET Operations	0.0	0.0	305.0	445.0	0.0	0.0	0.0	0.0
TFET Bilateral Projects	35.3	1,016.0	5,623.0	3,016.0	3,259.0	3,333.00	1,801.0	1,000.0
UN Assessed Contributions	0.0	3,940.0	3,563.0	3,200.0	2,400.0	0.0	0.0	0.0
Total	70.3	5,873.0	11,189.0	8,908.0	7,880.0	5,681.0	4,101.0	3,200.0
3. Economic Affairs (Trade, Investment, Industry, Mineral Resources and Tourism):								
CFET Operations	0.0	457.0	440.0	521.0	391.0	407.0	484.0	500.0
TFET	0.0	0.0	1,000.0	700.0	100.0	0.0	0.0	0.0
Bilateral Projects	0.0	0.0	280.0	220.0	50.0	0.0	0.0	0.0
UN Assessed Contributions	0.0	2,170.0	1,110.0	900.0	700.0	0.0	0.0	0.0
Total	0.0	2,627.0	2,830.0	2,341.0	1,241.0	407.0	484.0	500.0
4. Planning Commission (Previously NPDA)								
CFET Operations	0.0	225.1	113.0	0.0	0.0	0.0	0.0	
Bilateral Projects	0.0	0.0	350.0	0.0	0.0	0.0	0.0	
UN Assessed Contributions	0.0	0.0	135.0	0.0	0.0	0.0	0.0	
Total	0.0	225.1	598.0	0.0	0.0	0.0	0.0	0.0

Source: Ministry of Finance for FYs 00 to 02 and Preliminary Planning Commission estimates for FY 03 to FY 07

Table 7.2: Summary of Major Ongoing and New Projects

	Organisation / Project	Likely Funding Source
1.	Banking and Payments Authority	
1.1	Development of data processing systems	ADB
1.2	Foreign training and attachments	Various Central Banks and IMF
1.3	New Central Bank building	Donor Sought
1.4	Capitalization for full Central Bank	Donor Sought
2.	Ministry of Finance	
2.1	Phase 3, Freebalance Information Systems	Donor Sought
2.2	Establish Office of Budget independently	No additional cost
2.3	Capacity building (Budget Office/Statistics)	TFET
2.4	Public sector management capacity building	ADB
2.5	Ministry wide institutional strengthening	AusAID
2.6	Technical Assistance Ministry wide	Portugal
2.7	Continue 13 UNVs in District Offices	UNTAET
2.8	Open 2 new Regional Revenue Offices	Government Budget
2.9	External Legal Advice	Donor Sought
2.10	Operationalise Board of Tax Appeals	Government Budget
2.11	Senior Managers Development Program	Donor Sought
2.12	Establish professional library	Donor Sought
2.13	Additional common services by OGCS	Budget + UNTAET
2.14	Training programs in Knowledge Centre	Budget + World Bank
2.15	New Customs building	Donor Sought
2.16	Refurbish Customs regional warehouses	Donor Sought
2.17	Introduce ASYCUDA FMIS in Customs	UNDP
2.18	Transfer Macro Policy, Planning; and Aid Coordination	No additional cost
2.19	Transfer Statistics Office	No additional cost
2.20	Develop statistics laws / regulations	Donor Sought
2.21	Conduct national census	UNFPA
2.22	Develop trade statistics	Donor Sought
2.23	Compile National Accounts annually	World Bank
2.24	Update CPI basket	Donor Sought
2.25	Capacity building with poverty statistics	World Bank
2.26	Establish Performance Monitoring Unit	Government Budget

Notes: *1 Based on five year priorities developed by the Macroeconomics / Public Finance Working Group. Implementation will depend on the availability of funding, either from the CFET Budget or Bilateral Donors.*

Projects and Programs of the Department of Economic Affairs and Development have been included in the Chapter on Industry, Trade and the Private Sector.

8. MEDIUM TERM ECONOMIC AND FINANCING OUTLOOK

INTRODUCTION

8.1 This chapter provides a medium term economic and financing outlook for the Plan period. Much of the information underlying the outlook presented is summarised in the statistical tables in the appendix and illustrated in the charts below. Two important words of caution are made with regard to the outlook presented:

- a) Preparation of economic forecasts has not received significant attention so far in the building of East Timor's central economic institutions. Accordingly, there does not exist a consolidated database of historical macroeconomic information, nor have macroeconomic forecasting models been developed.
- b) Forecasting is notoriously difficult in small open economies, which are prone to shocks from a wide range of sources, with macroeconomic trends likely to be volatile rather than smooth.

8.2 The medium term outlook presented is a modest first attempt by the central economic institutions. One of the goals for institutional improvement within the Macroeconomics and Public Finance Sector is to significantly strengthen capacities in macroeconomic policy formulation and management. Assuming progress is made in this regard, future medium term planning exercises will be able to build on the first efforts made here.

8.3 What follows is a base case outlook. It takes account of:

- a) past underlying trends and relationships in the economy throughout the 1990s;
- b) estimates of the build-up of foreign assistance during the UNTAET period, and its forthcoming anticipated decline;
- c) likely policy, program and project developments in different sectors of the economy, as set out in the sector chapters of this plan;
- d) the views of the sector working groups on the base case outlook for different sectors; and
- e) prospects for Timor Sea Oil and Gas revenues based on the best information available to the Government at this time.

8.4 Even more than most outlooks attempted, the base case scenario presented is subject to significant risks and uncertainty. Providing the policies and approaches set out in the Plan are closely adhered to and the human responses are positive and reasonably rapid, there is an upside potential for more rapid development than in the case presented, especially in the later years of the Plan period. Nevertheless, the risks of slow policy development and response remain;

and unexpected external shocks are always lurking for small and open economies. Accordingly, risks of lower potential also exist.

ECONOMIC GROWTH

8.5 Estimates of the economic growth outlook are presented in Appendix Table 1 and in Figures 8.1 to 8.3 in the text. It should be noted that for the time being for statistical purposes oil producers in the Timor Sea Zone of Cooperation are being treated as non-residents pending clarification of their status. Accordingly, GDP is effectively calculated on a Non Oil basis. The growth outlook can be summarized as follows.

- a) Total real growth is estimated to be negative in 2002 and 2003 (-0.5% and -2.2% respectively); before commencing recovery in 2004 and 2005 (1.2% and 3.3%); and then going on to achieve its longer term underlying potential of 5.1%; and 5.9% in 2006 and 2007, respectively. Significant progressive withdrawal of the international presence from 2002 is the main negative influence on growth in the early years of the Plan period (with negative impacts on transport and communications, wholesaling, hotels and restaurants, utilities, construction, finance, rents, business services and government services).
- b) A number of sectors are expected to sustain positive growth throughout the Plan period, notwithstanding the decline in foreign presence. The main sectors with expected positive growth are: (a) agriculture, forestry and fisheries; (b) quarrying; and (c) manufacturing.
- c) Most other sectors are expected to directly or indirectly experience negative effects from the international drawback, before recovering and reaching their underlying production and potential growth levels beginning from around 2004. Many of the transitional negative effects will be felt in the urban areas; with large parts of the population insulated from them, providing growth in productive sectors (especially agriculture) can be sustained.
- d) The largest structural change expected to occur over the period relates to the declining importance of Government Services, which fall from 33.7% of GDP in 2000 to 27.7% of GDP in 2007 (in constant prices). This mainly reflects the decline of UNTAET influence, which is currently large.

Figure 8.1: Real Total GDP Growth, 2000-2007 (%)

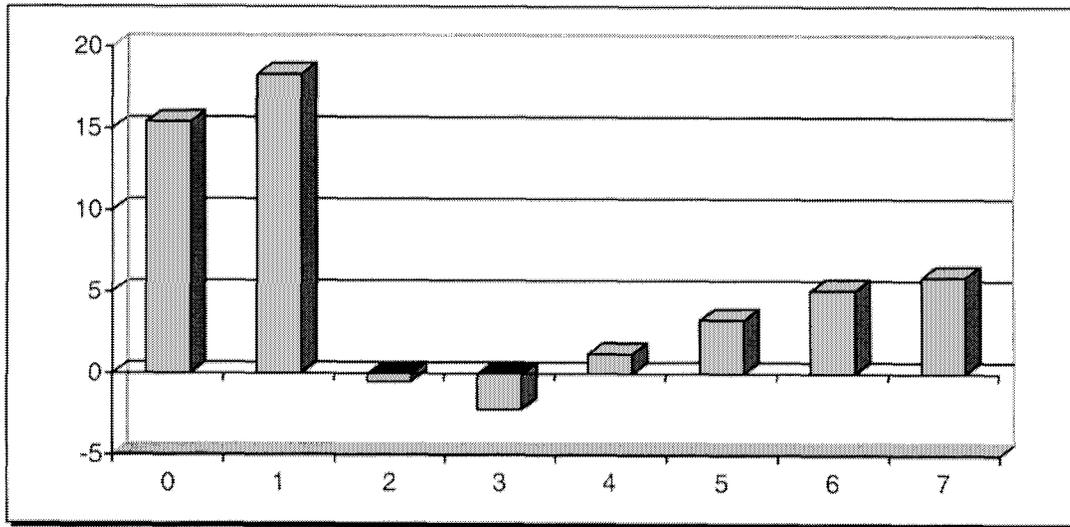


Figure 8.2: Sector Components of Real Total GDP (%)

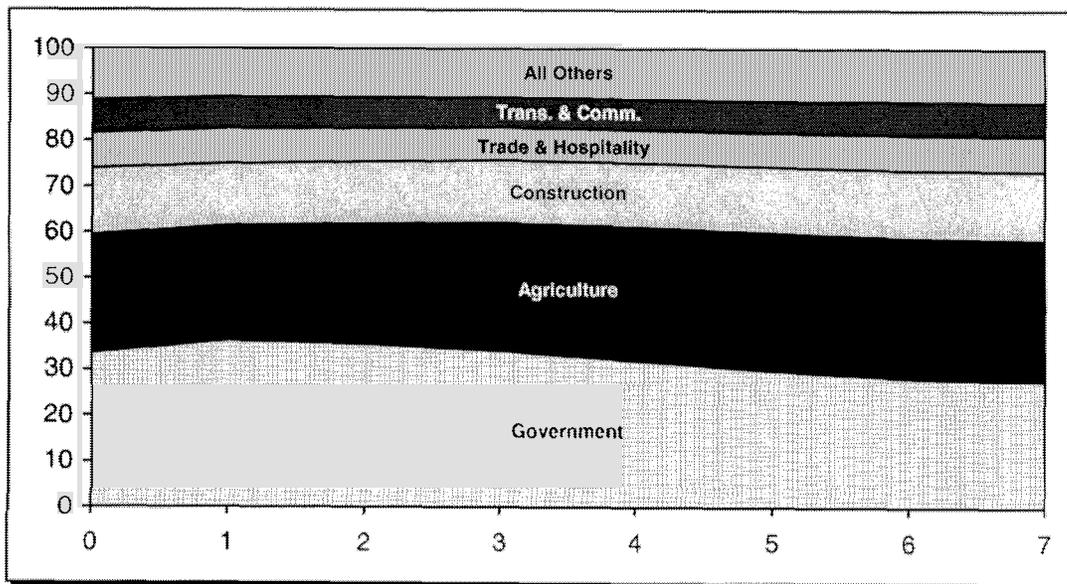


Figure 8.3: GDP Sector Growth, 2001-2007 (%) Figure 8.3: Cont...

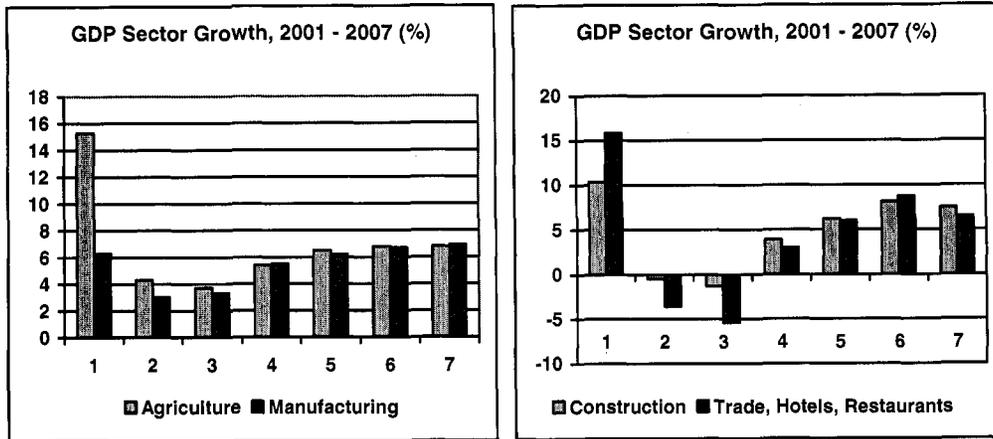
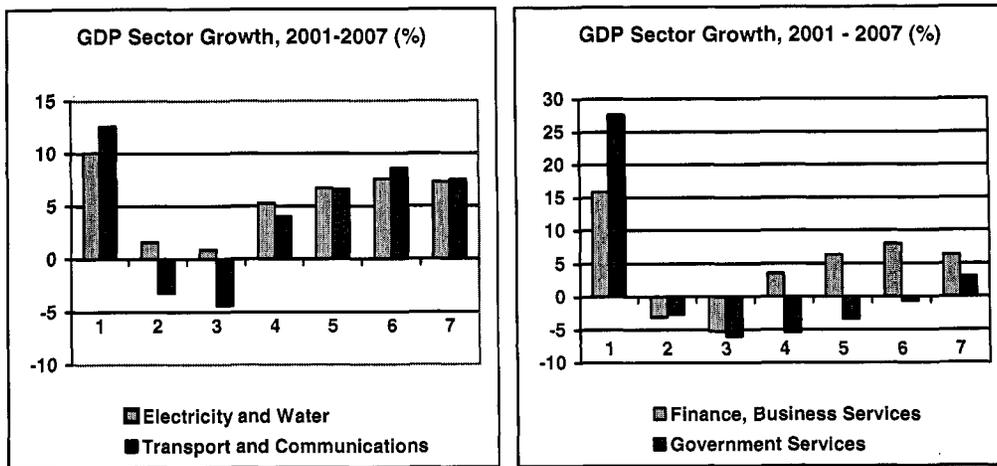


Figure 8.3: Cont...

Figure 8.3: Cont...



EMPLOYMENT/UNEMPLOYMENT

8.6 The most recently available estimates on employment along with the outlook to 2007 are presented in Table 8.1 and Figure 8.4. Because of data deficiencies these estimates should not be regarded as forecasts, but rather as broad indications of the types and levels of employment generation that will be needed if the Government's goal of significantly reducing the unemployment rate is to be achieved. The outlook presented suggests the following:

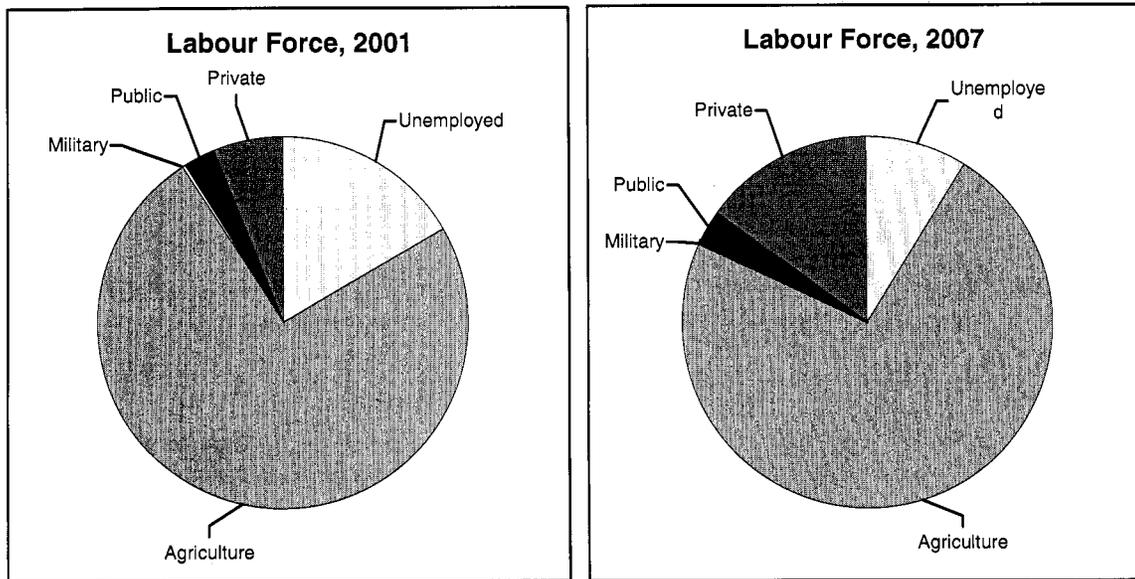
- a) The goal is to increase employment and reduce the unemployment rate during the Plan period. The analysis below attempts to estimate the magnitude of employment generation needed to achieve a major reduction in the open unemployment rate from an estimated 16.8% at present to 9.0% in 2007. The achievement of this target will be extremely challenging.

- b) In the short term there is a severe squeeze on the growth of public sector employment and this is expected to be more or less maintained over the course of the Plan period. The public sector does not present a direct solution to the unemployment problem.
- c) Agricultural growth is projected to be reasonably strong over the Plan period and this will allow for significant numbers of workers to be absorbed there. However, over the longer term (beyond the current plan period) agricultural growth is likely to be achieved increasingly by more rapid transformation towards modernisation and improved efficiency, with a resultant freeing of labour for other private sectors of the economy. Agriculture alone is not the solution.
- d) Given the above constraints around 40,000 new jobs in the private sector (excluding agriculture) would need to be created over the Plan period, if the target for unemployment reduction is to be met. This implies an annual growth of private sector employment of around 20% per annum, which is well above the projected private sector GDP growth. It highlights the difficulties in reducing unemployment if the private sector of the economy cannot grow rapidly. In the absence of very rapid private sector growth, the target for reducing the unemployment rate will only be partially achieved. Promoting agricultural and informal employment will remain of high importance given the major challenges in the promotion of formal sector employment.

Table 8.1: Labour Force Outlook, 2001 and 2007

ITEM	2001		2007	
	No.	%	No.	%
Labour Force (Actively Seeking Work)	325,930	100.0	406,400	100.0
- Of Which Openly Unemployed	54,851	16.8	36,576	9.0
- Of Which in Agriculture	240,928	73.9	296,672	73.0
- Of Which in Military / Police	900	0.3	1,000	0.3
- Of Which in Public Administration	9,605	2.9	11,200	2.8
- Of Which Other Private / NGO	19,646	6.1	60,952	14.9

Figure 8.4: Labour Force in 2001 and 2007

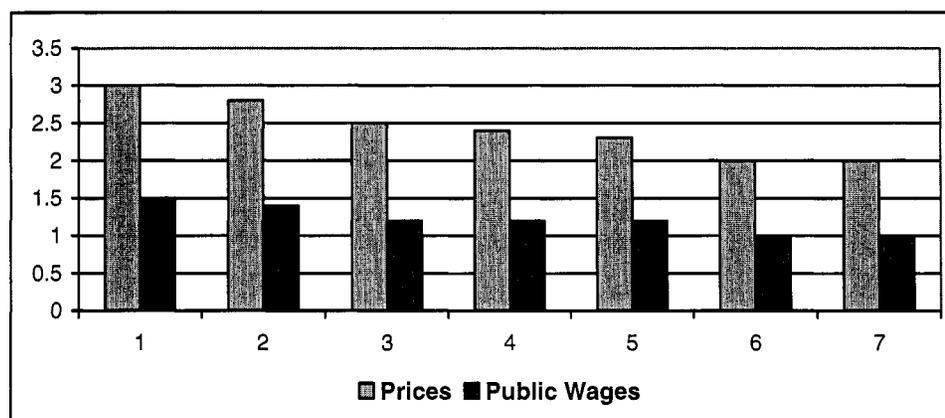


PRICES AND WAGES

8.7 Recent price movements have been subdued with year on year inflation to March 2002 recording a negative -2.2%. The policy stance and outlook for prices and wages are as follows.

- a) The maintenance of price stability is a key goal, which will be pursued principally through the policy on continued use of the US Dollar as the national currency along with a package of consistent macroeconomic policies. In these circumstances the outlook is for continued subdued inflation at levels that are no higher than projected United States inflation of two to three percent per year.
- b) The pursuit of moderate wage growth is seen as important for furthering a number of macroeconomic goals, including - higher economic growth - employment generation; and improved international competitiveness to reduce external trade imbalances. It will be important for the public sector to lead rather than follow the market in wage setting and ensure that the growth in public wage levels are below price inflation throughout the Plan period. Flexibility in wage setting will still occur where necessary to respond to market circumstances, but the wage increases occasioned by skills shortages are likely to be offset by relative wage reductions in areas of skills surpluses.

Figure 8.5: Changes in Consumer Prices and Public Wages, 2001-2007 (%)



FISCAL/BUDGET

Domestic Revenues

8.8 Domestic revenues have recently been very low at around five percent of GDP or US\$19 million a year. Government policy is to gradually increase the amount of domestic revenue raised, consistent with the current fragile and narrow economic base. At the time of preparation of the Plan, recommendations of the March 2002 Mission of the IMF (which reviewed tax and revenue policies) are under consideration, with a number of new initiatives possibly to be included in the FY 2003 budget (rates may rise modestly on: import duties, sales tax, services tax, general excise, excise on cars, and specific excise rates). Attempts are to be made to raise efficiency and yields in collecting existing taxes. Notwithstanding that some policy and administrative reforms are likely for FY 2003, and later during the Plan period, the scope to dramatically raise domestic revenues is limited in the short to medium term.

8.9 The medium term outlook for domestic revenues is contained in Appendix Table 2 and Figure 8.6. It indicates that total collections will grow from recent levels of US\$19 million per year to US\$27.6 million by 2006/07. Domestic revenues as a proportion of GDP are expected to rise moderately over the Plan period. Indirect taxes, especially taxes on imports, currently dominate domestic revenues and this trend is expected to continue over the Plan period.

Timor Sea Oil and Gas Revenues

8.10 On July 5, 2001, East Timor and Australia signed the Timor Sea Arrangement (TSA) with the intention of converting this to a Treaty upon East Timor's Independence. The TSA establishes a Joint Petroleum Development Area (JPDA) in the Timor Sea pending a final delimitation of seabed boundaries. Under the TSA, East Timor will receive 90% of petroleum from the JPDA and Australia 10%.

8.11 There is one small producing oilfield in JPDA, Elang Kakatu; although this is expected to close around the end of 2002. The Bayu Undan liquids project (condensate and liquid petroleum gas) was approved in 2002 and should begin production early in 2004. Full gas development at Bayu Undan depends upon Australian regulatory approval of part of the understandings on fiscal terms reached between East Timor and Bayu Undan contractors in December 2001. Meanwhile,

in March 2002 the contractors announced a gas sales agreement with Japanese utilities for LPG from Bayu Undan Gas. The Greater Sunrise gas-condensate field lies partly within the JPDA as defined in the TSA. A development arrangement for this field has yet to be agreed among the joint venture partners.

8.12 There is still much uncertainty about revenue prospects from the Timor Sea. The main uncertainty relates to whether particular projects will proceed at all. Further uncertainty remains about the gas pricing method. Even if these uncertainties abate, East Timor will still be exposed to the risk of lower than expected world prices for oil and gas. It is therefore appropriate for East Timor to forecast Timor Sea revenues with caution.

8.13 If oil prices remain above US\$18 per barrel (Brent Crude) then the Bayu Undan field is estimated to yield (in current prices) US\$1.8 billion to US\$ 3.2 billion to East Timor over the project life up to 2021. The higher figure assumes that full gas development occurs, while the lower assumes it does not. This is a “base” forecast, with an equal chance of a better or worse outcome. Accordingly, East Timor’s fiscal planning should use conservative estimates until there is confirmation of higher prices or new development outcomes.

8.14 The Bayu Undan Phase-2 project, if developed would be a dry gas project based around either a pipeline to Darwin or a floating manufacturing facility at the well site. Possible additional capital costs (extraction only) are around US\$500 million. Gas reserves are estimated at 3 trillion cubic feet. The potential revenue to East Timor over a 20-year site life has been tentatively estimated at US\$1.4 billion (current prices).

8.15 Annual revenues from Bayu Undan from FY 2006 to FY 2009 (oil and gas) are unlikely to exceed US\$100 million; perhaps just sufficient to support planned public (budget) expenditures during those years. Thereafter, revenues are estimated to be higher for a decade or more. East Timor needs to finalise and implement a revenue smoothing and savings strategy well before then.

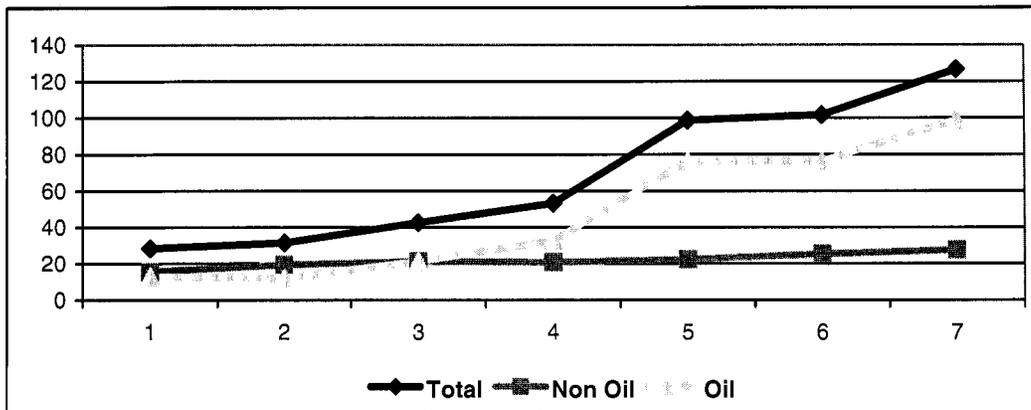
8.16 While there may be substantial uncertainty about Timor Sea revenue flows, it is clear that for the next three years at least such revenues under any scenario will be insufficient to finance government expenditure needs. There are also prospects that there will be shortfalls in revenue beyond FY 2005. The position may improve in the following years, but no substantial excess of revenue is likely until around FY 2010.

8.17 The long term implications of the oil and gas sector are covered in more detail later in this chapter. The remainder of this section concentrates on anticipated revenues to FY 2007, which are detailed in Appendix Table 2, Table 8.2 and Figure 8.6.

Table 8.2: Distribution of Timor Sea Revenues, FY 01 to FY 07

ITEM	FY 01	FY 02	FY 03	FY 04	FY 05	FY 06	FY 07	TOT. 01/07	%
Total Oil Revenues	12.9	12.0	21.3	32.7	76.4	76.4	99.1	330.8	100
Oil Revenues to Budget	9.8	6.0	20.5	26.1	52.2	78.0	84.0	276.6	83.6
Oil Revenues Saved	3.1	6.0	0.8	6.6	24.2	(1.6)	15.1	54.2	16.4

Figure 8.6: Components of Total Government Revenue, FY 2001 – FY 2007 (US\$m)



Total Expenditures

8.18 Expenditure planning is occurring in the context of an MTFP covering the period FY 03 to FY 05. The analysis in this plan uses this period and the MTFP as the fundamental building block for expenditure planning, but also adds to it fiscal years 06 and 07. Detailed information on the outlook for expenditure is contained in Appendix Tables 3, 5, 6, 8, 9 and 10; Table 8.3 and Figures 8.7 to 8.9.

8.19 At the time of plan preparation the CFET budget for FY 03 was still in the very preliminary approval stages having been tentatively endorsed by the COM, but yet to be considered by the National Parliament. Furthermore, due to uncertainties about the availability of external donor financing, the Council approval covered a range of total expenditure possibilities for FY 03, from a core of US\$67.4 million to a peak and preferred level of US\$77.2 million.

8.20 This Plan supports the provision of external donor financing to allow for total expenditures of US\$77.2 million in FY 03. In the Appendix tables and in the analysis which follows, this amount is used for the FY 03 estimate and as the base for expenditure planning over the full Plan period. Should financing levels to support this expenditure base not be forthcoming then modest adjustments will be needed to total expenditure numbers for FY 03 and possibly for FYs 04 and 05. However, no such adjustments should be necessary to estimates for FYs 06 and 07 which can be Government financed at proposed levels without recourse to donor CFET budget support. The Planning Commission considers the base expenditure level of US\$77.2 million for FY 03 to be appropriate for the following reasons:

- a) Total combined sources expenditure is projected to drop sharply in FY 03 (by 24%) as is Nominal GDP (by 8.5%). It is important for public expenditure to hold up economic activity in the coming difficult years, to the maximum extent possible. Had very significant expenditure outlays during the UNTAET period been conserved somewhat better over time than occurred, a smoother contraction would have been possible, and smoothing the transition still warrants support.
- b) Significant UNTAET common and other services are to be discontinued in FY 03 and will need to be directly or indirectly picked up by CFET. The net effect of UNTAET withdrawal from service delivery will be a significant real decline in resources available for public service delivery in FY 03 (and beyond) compared to FY 02.

- c) The proposed expenditure base for FY 03 combined with gradually and smoothly growing planned expenditures over the remainder of the Plan period, leads to levels of expenditure in 2007 that are sustainable in relation to both the Government's and the IMF's assessment of long term resource availability from Timor Sea oil and gas.

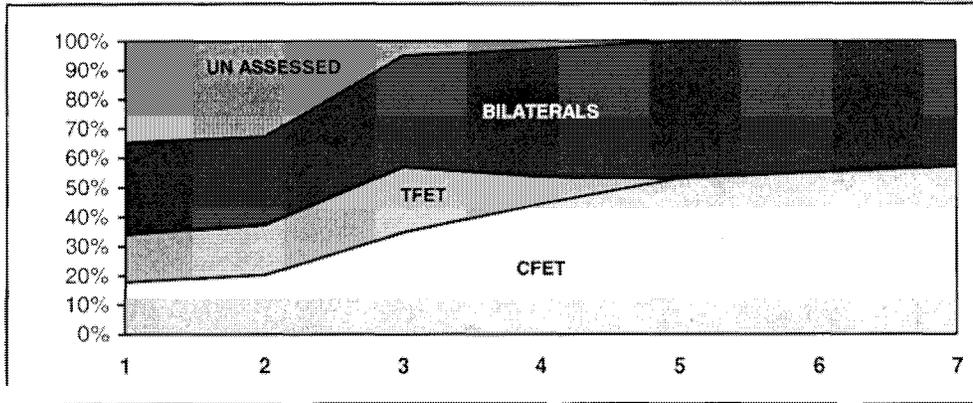
8.21 At present there are various dimensions to public expenditure in East Timor. The CFET covers the Government's own budget and sets out expenditure over which the Government has most direct control (although in the short term it will continue to rely heavily on donor financing to support it). Other elements of expenditure which go to make up Total Combined Sources Expenditure are: (a) TFET, which is a project trust fund financed by donors and administered by the World Bank and Asian Development Bank jointly; (b) Bilateral development projects; and (c) UN Assessed Contributions supporting the Budget (mainly foreign staff). Over the Plan period the CFET budget is expected to grow in significance while all other forms of expenditure will decline significantly. Total combined sources expenditures are expected to decline very sharply over the next 3 years. Trends in total levels of expenditure of each of the components are set out in Table 8.3 and Figure 8.7.

Table 8.3: Growth Rates of Combined Sources Expenditure Components, FY 2001 to FY 2007 (%)

ITEM	FY02	FY03	FY04	FY05	FY06	FY07
Total CFET	13.8	32.2	11.1	11.5	8.0	8.0
TFET	6.5	0.0	(63.9)	(100.0)
Bilateral Projects	22.0	(3.7)	(2.0)	0.0	0.0	0.0
UN Assessed	(5.0)	(88.4)	(54.5)	(100.0)
Total Combined Sources	0.6	(23.2)	(12.9)	(6.6)	4.2	4.4

Note: Numbers in brackets signify negative numbers

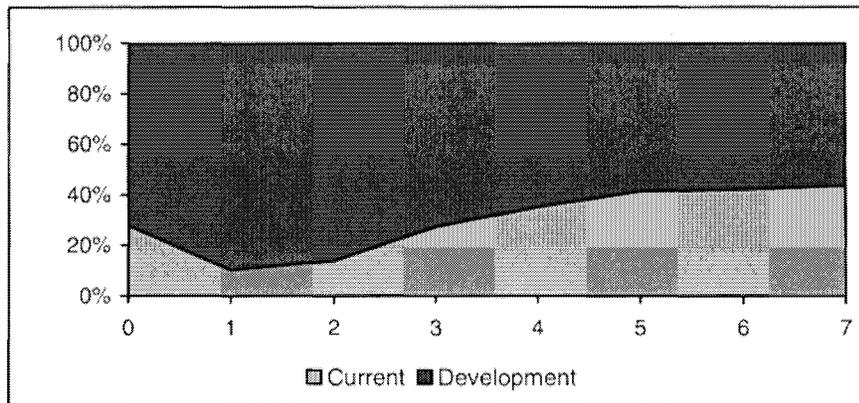
Figure 8.7: Components of Combined Sources Expenditure, 2001-2007 (%)



Recurrent and Capital / Development Shares of Total Combined Sources Expenditure

8.22 In recent times the share of capital and development expenditures in total combined sources expenditure has been very high, buoyed by donor expenditures (Appendix Table 3). This situation is not expected to continue over the Plan period with the share of capital and development expenditure declining towards more normal levels. Expected trends are set out in Figure 8.8. To some extent the recent trends shown are an overstatement, because much of recent donor spending categorised as development has not been strictly capital or developmental in nature, but rather has included large components of current outlays (particularly in the form of Technical Assistance). The outlook for 2007 is that development expenditure will have fallen to around 56% of the combined budget and 25% of GDP. While still quite high it assumes continued high levels of bilateral support and this is considered appropriate for East Timor’s current early stage of development. The proposed nature and composition of the future development budget is set out in Appendix Tables 8 to 10 and is commented on in more detail below.

Figure 8.8: Shares of Current / Development in Combined Sources Budget, 2001-2007 (%)



Expenditure Allocations by Agency and Function

8.23 Anticipated trends in the Agency and functional composition of CFET total expenditures between FY 2002 and FY 2007 are set out in Appendix Tables 5 and 6 and Figure 8.9. Analysis of the recent situation (FY 2002 revised budget) in terms of expenditure allocation by Agency and function reveals three important concerns for the development of future expenditure policy:

- a) By international standards there is a quite high amount spent on bureaucracy and administration at present. The functional data indicates a significant 15% of the CFET budget allocated to General Public / Administrative Services. Most countries aim to keep this ratio below 10%. (However, comparison of East Timor's budget situation with other countries requires caution).
- b) Subsidies to the energy sector are very high at US\$ 6.8 million, representing 11.6% of all budget expenditures. There is an obvious need to progressively reduce and remove this subsidy over a relatively short period of time.
- c) As a result of the above expenditure patterns, resources available to priority areas of Government are far less than they should be. This applies particularly to education, health, infrastructure maintenance and development; and agricultural extension and investment. These patterns in part reflect the post crisis nature of the economy and with good management can be expected to even out over time.

8.24 Future planning policy needs to focus on progressively changing these inherited difficulties. At this point in time the Government is not sufficiently well advanced in its planning to have very hard sector and Agency ceilings in place for each of the 5 years of the Plan. Furthermore, all countries need to maintain reasonable flexibility with forward expenditure plans. Accordingly, neither the MTFF nor the Plan presents very hard numbers for outer years of the Plan. Notwithstanding this it will be critically important to actively manage and monitor expenditure allocations over time to ensure that they are consistent with planning and policy priorities.

8.25 Rather than set out hard plans for expenditure allocations over the course of the Plan period one illustrative example is now provided of a policy based approach to gradually changing the composition of expenditures over time. In this regard an example of a relatively challenging reform to the composition of expenditures over time is set out in Tables 5 and 6 and in Figure 8.9. This example of one possible reform to the composition of expenditure reflects moderately different outcomes than the forward estimates presented in the Budget documents. The forward estimates in the Budget documents set out the future ongoing costs of existing policies and programs. In contrast this Plan sets out an example of ongoing change to the composition of expenditures over time in the direction of higher funding for priority areas identified in the planning process. If new spending policies and priorities were implemented over coming years, the nature of the forward estimates would also change.

8.26 The main operational policies driving this illustrative example are:

- a) Allocations for the FY 03 budget are taken as given in line with preliminary decisions of the COM in April 2002.
- b) Most administrative, defence, police and general public service expenditures over the Plan period FY 04 to FY 07 are constrained to annual expenditure growth of 2% per annum, thus approximately maintaining real expenditure levels.

- c) The subsidy on energy is progressively withdrawn during the Plan.
- d) Bulk funding for infrastructure and capital development is provided at relatively high levels and broadly in line with the April COM Budget Meeting and consistent with the Preliminary Forward Estimates (US\$15.5 million in FY 04; US\$17.5 million in FY 05, US\$17.9 million in FY 06; and US\$ 14.6 million in FY 07).
- e) The remaining wedge of resources is made available to education, health, agriculture and water and public works expenditures. These four priority areas are able to grow considerably faster than all other budget areas, at an annual average growth rate of 21% throughout the Plan period.

8.27 In summary in the example presented, the main expenditure composition results that could be achieved over time are:

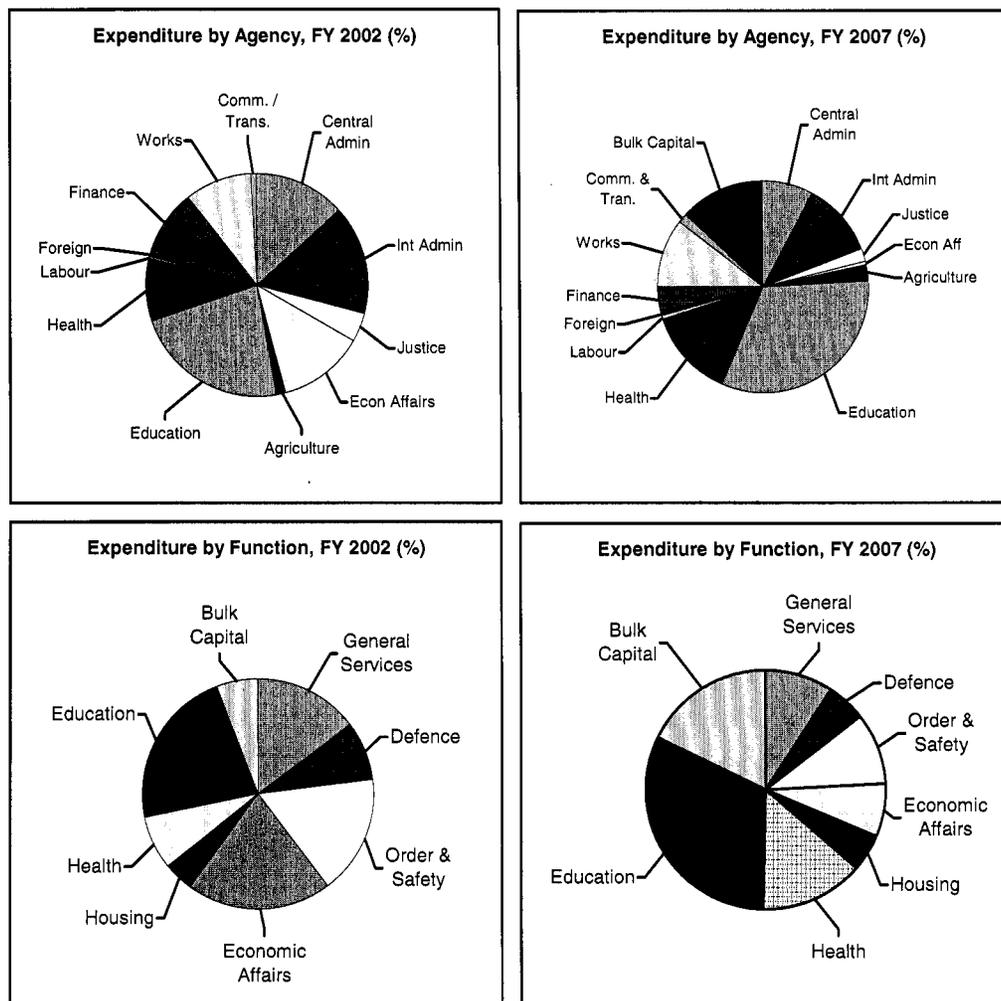
- a) The share of General Public Services expenditure would fall from 14.6% of Total Expenditure in FY 2002 to 9.2% in FY 2007. Major relative declines would occur in the administrative expenditures of the Government.
- b) The share of Defence would decline from 8.4% in FY 2002 to 5.2% in FY 2007.
- c) Outlays on Public Order and Safety would decline from 16.8% of total in FY 2002 to 9.8% of total in FY 2007.
- d) Outlays on Economic Affairs would fall from 20.3% of total in FY 2002 to 7.1% of total in FY 2007. Within this sector the major gainer would be Agriculture while the major downward adjustment would be on subsidies to electricity consumers which would be phased out (these account for the whole decline).
- e) The share of Environment, Housing and Community Development would rise from 4.1% of total in FY 2002 to 5.2% of total in FY 2007 (mainly due to increased funding to water supply).
- f) The share of Health would rise significantly from 7.6% of total in FY 2002 to 13.7% of total in FY 2007.
- g) The share of Education would rise significantly from 22.4% of total in FY 2002 to 32% of total in FY 2007.
- h) In 2002 there were no significant funds available for infrastructure development. Proposed bulk funding for infrastructure would see around 20% of the total CFET budget allocated to infrastructure every year through the Plan period (17.8% in 2007).

8.28 Overall, in this illustrative example the main relative gainers are education, health, infrastructure and agriculture. The main downward adjustments are to central administration and bureaucracy, police, defence and electricity subsidies. However, apart from electricity subsidies (which are completely phased out) all other Agencies maintain the real value of their FY 2003 expenditures, even though they do not grow as fast as the priority areas. The allocation policies in this illustrative example reflect priorities that have been identified and agreed in the planning process and are elaborated on in more detail in the sector and strategy sections of the document. They represent one example of challenging targets to aim for over the course of the Plan.

8.29 The main point in presenting this illustrative example is not to recommend it as the only possible approach to allocating budget resources over the medium term. Indeed current political (not Plan) perceptions are that higher levels of resources should go to defence, foreign affairs and police than are provided for in the example. Rather the purpose of the illustrative example is to draw out some more general pointers for expenditure planning approaches over time. The broader messages are:

- a) The Government if it desires it strongly enough can change the compositional nature of the budget over time to better reflect Government priorities and development needs.
- b) Sectors and Agencies in most countries are able to manage their resources and affairs more effectively where they have reasonable medium term clarity concerning likely levels of available budget resources.
- c) Further institutional, technical and coordination strengthening at both political and public service levels will be needed in East Timor to improve expenditure planning over time, particularly to more closely equate expenditure allocations with policy and planning priorities.

Figure 8.9: CFET Expenditure by Agency and Function, FYs 2002 and 2007 (%)



Financing the Deficit and Aid

8.30 The outlook for combined sources financing over the Plan period is contained in Appendix Table 4. Large fiscal deficits are anticipated over all years of the Plan (-50.2% of GDP in FY 2003; -39.9% of GDP in FY 2004; -22.1% of GDP in FY 2005; -21.7% of GDP in FY 2006; and -16.0% of GDP in FY 2007). All deficits are to be financed with donor grants with no public borrowing planned. Donor support to run the CFET budget is required for FYs 2003, 2004 and 2005, but from then on oil revenues are estimated to be adequate to fund the CFET budget.

8.31 All of the projected combined sources deficits in the years FY 2003 to FY 2007 are assumed to be financed by donor grants. It is anticipated that this will include contributions from: (a) a donor facility to support on budget current and development expenditures under CFET, at least for FYs 03, 04 and 05 and if necessary beyond that; (b) TFET; (c) Bilateral Projects; and (d) UN Assessed Contributions. By FY 2006 all of these financing sources apart from bilateral projects will have wound down to zero. Trends in projected deficit and financing levels over the course of the Plan period are set out in Figures 8.10 and 8.11 below.

Figure 8.10: Combined Sources Deficit (-) as % of GDP, FY 2000 to FY 2007

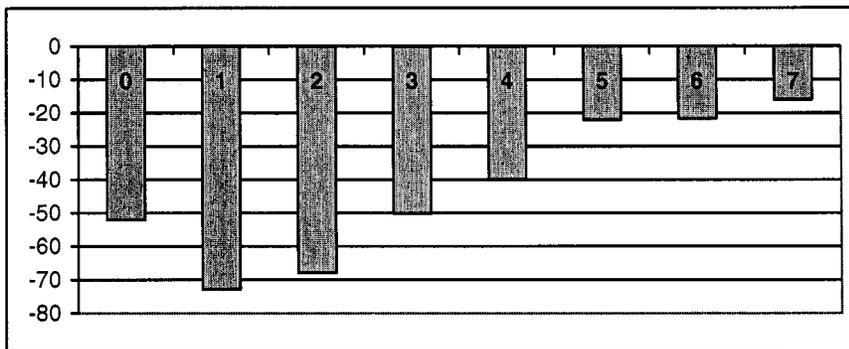
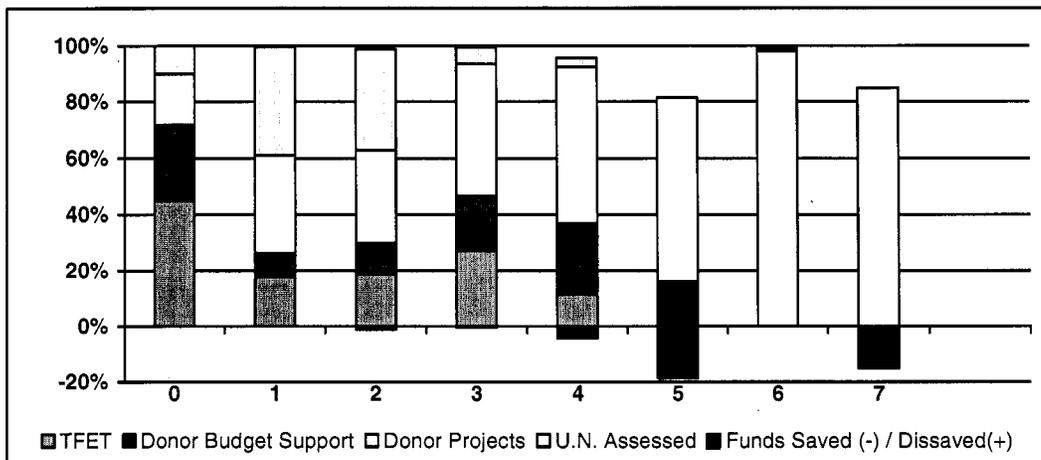


Figure 8.11: Combined Sources Financing Components, FY 2000 to FY 2007 (as % of Total)



BANKING AND FINANCE

8.32 For the immediate future the Government intends to retain the United States Dollar as East Timor's currency. This along with responsible management of the package of macroeconomic policies should ensure price stability. Given dollarisation, there is essentially no scope at this stage for the application of flexible monetary and currency policies by the Government. In these circumstances – and in view of the paramount objective of ensuring a competitive position for East Timor's producers – it will be important to follow closely developments in the real effective exchange rate (which is the exchange rate adjusted for inflation) for East Timor, and to assess its implications for economic growth and external balance.

8.33 In the meantime, there will continue to be a broadening and deepening of the capabilities of the BPA, with a view to preparing it to perform the fully-fledged functions of a central bank. Accordingly, the phased process of institution building that has been developed with support from the IMF will be continued. In particular, further efforts will be made to train East Timorese staff in performing central banking functions, including reserve management, provision of banking services to the government, development of the payments system and supervision of banking institutions in accordance with core Basle principles. Moreover, there will be growing emphasis on developing the economic analysis capability of the Authority, with the creation of an incipient economic and financial research department. In this context, importance will be attached to the further development of banking, financial and balance of payments statistics.

8.34 Other major elements of the new institutional set up are expected to include:

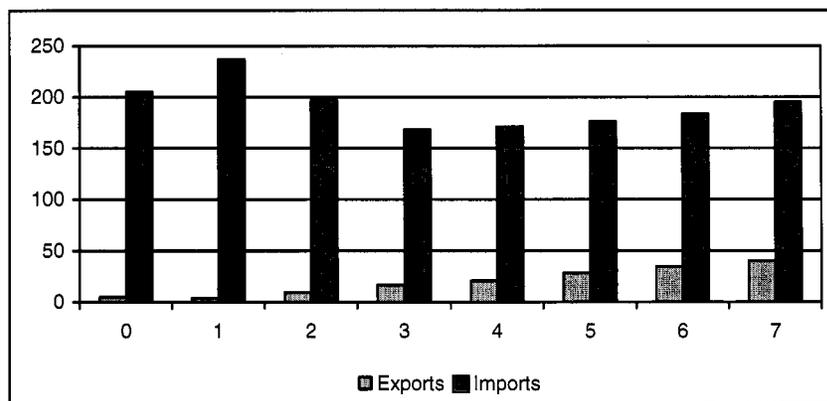
- a) Legislative review and upgrading of laws within the sector (to occur by early 2003).
- b) A rise in the number of licensed commercial banks beyond the current number of two.
- c) Increased diversity in the sector with a number of non-bank financial institutions having commenced operations by the end of the Plan period (leasing; finance companies etc).
- d) Access to branch or agency offices of financial institutions will have broadened to include at least minimum access in all main district centres.
- e) Establishment by the end of the Plan period of at least some institutions relating to:
 - General and life insurance.
 - Micro savings and credit schemes.
 - Private superannuation and related savings schemes.
- f) A significant increase in Bank deposits (demand and time) and lending compared with recent levels.

EXTERNAL/BALANCE OF PAYMENTS

8.35 The external and balance of payments outlook is summarized in Appendix Table 7 and in Figure 8.12 below. Key elements of the external outlook are as follows:

- a) Non oil exports will recover somewhat from recent levels, though at US US\$40 million per year by plan end will remain quite low, with potential for higher levels if agricultural export growth can be stimulated.
- b) New oil revenues from the Bayu Undan field from 2004 will assist the balance of payments through receipts of royalty and taxation payments. As the Timor Sea producers are being treated as non-residents, Trade, Services, Income, Capital and Financial transactions from the project are not recorded. In any event the project is expected to be enclave in nature, with most foreign retention occurring in the form of revenue payments to East Timor.
- c) Activities of UNTAET and the international donor community have had a major influence on the external accounts in recent periods, fuelling a large growth in imports on the Trade Account to be offset by Donor grant financing, with no net impact on the Overall Balance. The impact of these foreign flows is expected to diminish throughout the Plan period. General imports (which are not related to either aid or oil imports) are expected to be relatively modest throughout the period, although still significantly higher than merchandise exports.
- d) As a result of the above trends the estimated current account deficits are moderately high in all years of the Plan period (averaging 12% of GDP), which are to be largely financed by international grant and capital inflows.
- e) In terms of overall balance, there are small negative balances projected for 2002, 2003 and 2004 following which there is a gradual build-up of positive balances to 2007. In the main these positive overall balances are represented by savings of Timor Sea oil revenues, which will be built up in a special offshore savings facility to be introduced.

Figure 8.12: Merchandise Imports and Exports, 2000-2007 (US\$m)



TWO CRITICAL FINANCING ISSUES

8.36 Arrangements for financing expenditure over the Plan period take on importance in East Timor. There are two significant issues for medium term financing, which are:

- a) Proposed management approaches and outlook for oil and gas revenues.
- b) Aid management policy and the preferred forward aid program.

PROPOSED MANAGEMENT APPROACHES AND OUTLOOK FOR OIL AND GAS REVENUES

Introduction

8.37 The short to medium term outlook for oil revenues has been set out at 8.10 above. It depends heavily on the outlook for Bayu Undan which is currently under construction. Apart from this approved petroleum liquids project (with approval on the gas phase still pending), there is one other highly promising site under consideration, but not yet approved for development. This is the Sunrise Troubador project, which if developed would be mainly (about 90%) a dry gas project, also based around either a pipeline to Darwin or a floating manufacturing facility at the well site. Based on the feasibility work undertaken the possible capital costs (extraction only) are around US\$700 million. Gas reserves are estimated at a significant 10 trillion cubic feet, with potential production of 1,970 petajoules of gas and 70 million barrels of condensate. Potential total revenue to East Timor over a 20-year site life has been tentatively estimated at US\$1.0 billion (current values).

8.38 Because no development contracts are yet in place for this potential project and because of engineering, commercial and international diplomacy uncertainties, no direct account has been taken of it in the current national planning exercise. However, it is current Government policy to pursue arrangements whereby these projects will come to full fruition in future years. This will depend on reaching agreement with potential developers on terms and conditions that are satisfactory for both the developers and the people and Government of East Timor.

8.39 The remainder of this section concentrates on the longer-term outlook and management approaches to the Bayu Undan Project. However, while the economic and commercial outlooks for different projects will vary, similar management approaches (as those set out below) are likely to be pursued for all future projects.

Proposed Management Approaches

8.40 Important elements and guiding principles of the management approaches that will be pursued are as follows.

- a) The risks of Dutch Disease are now widely known and Government policy seeks to avoid such effects. Common elements of this disease include: (a) booming conditions in the oil sector can cause real upward movements in currency, price and wage levels, leading to diminished competitiveness and prospects for other sectors of the domestic economy, such as agriculture, industry and tourism; and (b) frequently, Government expenditure rises to levels above the effective absorptive capacity of the economy, leading to wastage in both recurrent and capital expenditures of the government budget.
- b) Once higher oil revenues start to flow (currently expected to reach peak levels around FY 2010), oil revenues will not be taken directly into the budget, but will go initially into an offshore pool of foreign financial savings and investments. These investments will be of a secure nature (Investment Grade AAA only) and will aim to provide a secure stream of interest and dividends income, that can be brought into the budget without diminishing the real capital value of the Fund over time (after it reaches its projected peak level, around twenty years into the Bayu Undan project).

- c) The precise mechanisms to implement the above savings goals are still being developed, partly in consultation with officials from the Norwegian Government Agencies responsible for similar mechanisms for supervising and managing oil revenues in Norway. While it is likely that a Norwegian type model and legislation will be introduced within the next 6 to 12 months it is still too early to be precise on all the fine details. However, important elements of the management approach are likely to be as follows:
- The approach will be backed by strong legislation, which will provide quite limited discretionary powers to Ministers to adjust legislated flows of finances either into or out of the Fund. In the first instance all funds received are likely to be deposited offshore.
 - The legislation is likely to contain principles to apply to the collection and draw down of funds, with close integration with the budget processes. Some flexibility will need to be built into the principles to allow for changing circumstances and particularly during the early years, to allow for some draw down of capital until such time that the fund reaches its peak capital and earnings level. However, all significant matters affecting the flows of funds are expected to require legislative backing.
 - After peak capital levels are achieved, a central principle is likely to be that the real capital value (value adjusted for price and currency movements) of the offshore fund will be at the very least maintained (hopefully it will grow) over time.
 - Thus amounts drawn into the budget will be at levels that are sustainable in terms of maintaining the real capital value of the Fund. At the same time the aim will be to draw down amounts in a consistent and regular fashion each year, to allow medium term management of expenditures and the budget in smooth and predictable ways, without abrupt changes from year to year. Appropriate management of expenditures and the total budget from year to year will be critical for successful management of oil revenues.
 - Offshore investments will be managed by a diversified range of AAA Grade Investment Funds. Regular monitoring of investment performance of individual Managers and the Total Fund will occur by the MoF and the BPA.
 - The Timor Gap Authority (which regulates licensing, production sharing and other matters in joint areas of the Timor Sea) will maintain high standards and will be staffed only with people of high international standing, so as to fulfil properly its licensing and regulatory functions and also to undertake the important role of monitoring collection of tranche 1 and tranche 2 oil payments to East Timor.
 - The Revenue Service will be strengthened to ensure proper administration of the collection of oil revenues, using the highest international standards. Where necessary international technical assistance and the international contracting out of particular tasks will be undertaken. Regular and complete tax audits of oil operators will be a common feature of future tax administration.

Financial Outlook

8.41 Important elements of the financial outlook for Bayu Undan Project (both liquids and gas phases) are as follows:

- a) Total of 370 million barrels of condensate and LPG and 3 trillion cubic feet of gas over the 20-year life of the project.
- b) Estimated total revenue (from all sources) to East Timor of approximately US\$3.2 billion over the course of the project (at current prices).
- c) Recent modelling by both the Government and the IMF under quite conservative assumptions of the build up of the offshore savings fund indicate:
 - That the fund will achieve peak level in excess of US\$1.3 billion (2000/2001 constant prices) in the early 2020s.
 - That beyond this peak the Fund should be able to support regular drawings of around US\$60 to US\$70 million per year (2000/2001 values, but to be adjusted annually to approximately maintain the real value of drawdowns).
 - Provided there is solid growth over time in the Non Oil domestic revenues to around 10 to 12% of GDP, the budget should be able to maintain annual total expenditures of around 25% of GDP (US\$ 97 million in 2001 values), without recourse to CFET debt financing (though capital and technical forms of donor assistance are still sought over the longer term). This total level of expenditure is broadly equivalent to current plan estimates (where total CFET expenditure in 2006 / 07 levels out at around 25% of GDP – Appendix Table 3).
 - In the event that the Bayu Undan phase-2 gas component did not eventuate a somewhat lower level of expenditures would be needed to sustain the real value of the offshore fund in perpetuity.
- d) To the extent that oil prices are significantly above US\$18 a barrel or that Sunrise Troubador and other prospective sites are developed at a later stage, then the situation presented would be even more promising. In these circumstances it is likely that the peak capital size of the Fund would increase sharply beyond the currently projected levels and that there would be scope for either higher annual levels of capital and development expenditures through the budget than are currently planned or for higher levels of savings for future generations, or a combination of both.

AID MANAGEMENT POLICY AND THE PREFERRED FORWARD ODA PROGRAM

CFET Budget Support

8.42 Foreign aid (or ODA) in its various forms has funded the bulk of public expenditures since 1999. This trend is expected to continue for the full period of the Plan, although the largest need will be in the first three years of the Plan. Beyond that it is anticipated that there will be no need for donor budget support, (although there are risks that this situation will change if oil revenues do not reach expectations).

8.43 Other ODA is expected to continue for varying periods throughout the Plan (refer to Figure 8.7). TFET is expected to wind down sharply from FY 2003 and to cease completely in FY 2004. The UN Assessed Contributions are expected to be phased out in FY 2004. It is anticipated that bilateral capital projects and technical assistance will continue over the longer term, and it is hoped that these can be maintained over the medium term to levels of at least US\$ 85 million per year. This is the minimum level needed over a long period of time to sustain the growth and development projections.

8.44 Reaching agreement with donors on the amount of budget support to be provided in FYs 2003 to 2005 (and if necessary beyond) is a matter of major importance for the Government. The processes and terms and conditions of such assistance are also of great importance. At present discussion is still proceeding as to amounts and processes to apply. It is hoped that broad agreement will be reached before the May 2002 Donor Conference, which will be asked to endorse the proposed arrangements.

Aid Policy

8.45 As at April 2002 discussion is occurring in terms of a possible single ODA facility to cover budget support funding in the coming financial years before significant oil revenues arrive. It seems likely this facility will include contributions from a number of participating donors, but will probably be managed and coordinated through one or two donors. The more important policy positions of the Government on the finalization of such a facility (and more generally in relation to aid policy) are as follows:

- a) There is a strong policy preference for grant forms of assistance with no borrowing in the early years of independence.
- b) Significant assistance is needed in the early years in the form of direct budget support to assist the general current operations of government and to finance a small capital development fund. While it is hoped that the need for assistance will not extend beyond FY 05, the Government recognizes the need to be cautious as to the actual levels of oil revenue collections and requests donors to remain flexible in their provision of budget support beyond FY 2005 should developments in the oil sector require it.
- c) Future aid planning makes some provision for longer-term technical assistance in the five years after independence (around three hundred longer term positions). This TA support is specifically meant to cover long term line positions, initially to be filled by expatriates. Beyond these identified positions (and any subsequently identified), the Government's preference is for a much lower proportion of TA than occurred in the UNTAET period (In the period from 1999 to June 2002 it is estimated that TA spending will represent US\$114.2 million out of the total ODA spending of US\$323.1 million, or 35% of the total). It is preferred that the great bulk of future ODA support goes into capital and development projects that have been identified by the Government and agreed with donors.
- d) The Government lacks the capacity to manage a facility with a large and complex conditionality matrix. To the extent that any conditionality matrix at all is required, Government is of the view that it should be simple, containing only a small number of conditions, most of which should relate to total levels of CFET expenditure and agreed targets for the composition and nature of both current and development expenditures.

- e) All future ODA should take close account of Government's Vision, Goals, Guiding Principles, Policies and allocational priorities between sectors as contained in this plan, to assist in the identification and formulation of future programs and projects of assistance. In relation to formulating ODA programs and projects within sectors this should extend to understanding and supporting the various sector chapters of this plan, which set out goals, priorities and policies for future assistance within each of the sectors (along with indicative programs and projects). Appendix Table 9 provides information on the composition of already approved and programmed bilateral ODA over the period, FY 00 to FY 07. In many respects existing and planned bilateral assistance has been favourably consistent with the priorities of the Plan. For example 18% of the total has gone to Agriculture and Fisheries, 14% to Education, 11% to Health and 22% to Infrastructure areas of Water, Public Works, Communications and Transport. On the other hand significant amounts have also been devoted to central administration (around 30% of total bilateral ODA). In some areas overlaps between donors' contributions, particularly in competing forms of TA, have occurred and this needs to be addressed.
- f) As part of institutional strengthening it is proposed during the course of the Plan to centralize all aid coordination and management functions under one roof, possibly in the Ministry of Finance. This should allow for easier integration of the current and development budgets and a closer linking of ODA with the MTFF, budget preparation and management.
- g) The UNTAET Regulation 2001/13 makes provision for a Special Funds budget to cover aid in kind and external financing that does not pass through the Consolidated Fund. All Government Ministries and Agencies are required to provide the necessary project and financial information through the budget formulation process. To increase the comprehensiveness of coverage the MoF has introduced a database which aims to include all approved forms of ODA and to track disbursements against financing agreements, mainly using information collected from donors. It is proposed in future years to present more comprehensive information as an annex to the budget documents with regard to all forms of ODA that are not directly on budget. The full support and assistance of donors in building up this information base is sought.

Future ODA Programs and Projects

8.46 Apart from the above general policies, other key elements of the Government's future ODA program and project needs are set out in the sector chapters of this Plan. The preferred programs and projects have been developed through the eight sector working groups involved in the preparation of the Plan. The Government seeks to gain as much future support as possible to fund these new initiatives. This includes support for projects that are to be directly on budget and also projects the bilateral donors administer more directly themselves. The sector chapters provide the details.

APPENDIX: MEDIUM TERM ECONOMIC AND FINANCING OUTLOOK TABLES

Table 1

Constant (2000) Price GDP by Sector, 2000 - 2007. (US\$ Millions; and %)

	2000	2001	2002	2003	2004	2005	2006	2007
	Estimate	Estimate	Outlook	Outlook	Outlook	Outlook	Outlook	Outlook
1. Agriculture, Forestry and Fisheries	83.3	96.0	100.1	103.8	109.4	116.5	124.5	133.0
Annual Growth (%)	-12.5	15.3	4.3	3.7	5.4	6.5	6.8	6.8
As % of GDP	25.9	25.3	26.5	28.1	29.3	30.2	30.7	31.0
2. Mining and Quarrying	3.1	3.2	3.3	3.5	3.6	3.8	4.1	4.3
Annual Growth (%)	0.0	5.5	3.3	3.5	5.1	5.4	6.0	6.0
As % of GDP	1.0	0.9	0.9	0.9	1.0	1.0	1.0	1.0
3. Manufacturing Industry	8.7	9.3	9.5	9.9	10.4	11.0	11.8	12.6
Annual Growth (%)	10.0	6.3	3.0	3.3	5.5	6.2	6.7	6.9
As % of GDP	2.7	2.4	2.5	2.7	2.8	2.9	2.9	2.9
4. Electricity, Gas and Water	2.6	2.9	3.0	3.0	3.1	3.4	3.6	3.9
Annual Growth (%)	13.3	10.1	1.6	0.9	5.3	6.7	7.6	7.3
As % of GDP	0.8	0.8	0.8	0.8	0.8	0.9	0.9	0.9
5. Construction	45.9	50.6	50.4	49.7	51.7	54.9	59.3	63.8
Annual Growth (%)	33.4	10.4	-0.5	-1.3	3.9	6.2	8.1	7.5
As % of GDP	14.3	13.3	13.3	13.5	13.8	14.2	14.6	14.8
6. Trade, Hotels and Restaurants	25.1	29.1	28.0	26.5	27.3	29.0	31.5	33.5
Annual Growth (%)	44.7	15.8	-3.6	-5.4	3.0	6.0	8.7	6.5
As % of GDP	7.8	7.7	7.4	7.2	7.3	7.5	7.8	7.8
7. Transport and Communications	23.2	26.1	25.3	24.2	25.1	26.8	29.1	31.3
Annual Growth (%)	45.8	12.6	-3.2	-4.4	4.0	6.6	8.6	7.5
As % of GDP	7.2	6.9	6.7	6.5	6.7	6.9	7.2	7.3
8. Finance, Rents & Bus. Services	21.1	24.4	23.7	22.4	23.2	24.7	26.6	28.3
Annual Growth (%)	24.5	15.9	-3.1	-5.3	3.5	6.3	8.0	6.3
As % of GDP	6.6	6.4	6.3	6.1	6.2	6.4	6.6	6.6
9. Services	108.2	138.1	134.5	126.5	119.8	116.0	115.3	118.8
Annual Growth (%)	27.0	27.6	-2.6	-6.0	-5.2	-3.2	-0.6	3.1
As % of GDP	33.7	36.4	35.6	34.2	32.1	30.0	28.4	27.7
Total (Constant Price) GDP	321.1	379.8	377.8	369.4	373.7	386.0	405.7	429.4
Annual Real Total Growth (%)	15.4	18.3	-0.5	-2.2	1.2	3.3	5.1	5.9
Total Nominal GDP	321.2	389.3	370.6	345.2	357.4	382.5	417.3	454.9
Annual Nominal Total Growth (%)	18.9	21.2	-4.8	-6.9	3.5	7.0	9.1	9.0

Sources: (a) Ministry of Finance for 2000; (b) I.M.F. for 2001; and © I.M.F. and Planning Commission for 2002 - 2007

Note: Excludes oil and gas production with Oil Companies operating in the Zone of Cooperation treated as non residents pending clarification of their status

Table 2.**Combined Sources Revenues and Grants, FY 00 to FY 07 (US\$ Millions and %)**

	FY00 Actual	FY01 Actual	FY02 Budget Revised	FY03 Budget Prelim.	FY04 Estimate	FY05 Estimate	FY06 Estimate	FY07 Estimate
A. TOTAL REVENUE (B+C)	2.0	28.4	31.4	42.6	53.4	98.8	101.7	126.7
Total Revenue as % of GDP	0.7	8.0	8.3	11.9	15.2	26.7	25.4	29.1
B. DOMESTIC REVENUE (B1+B2+B3)	2.0	15.5	19.4	21.3	20.7	22.4	25.3	27.6
Total Domestic Revenue as % of GDP	0.7	4.4	5.1	6.0	5.9	6.1	6.3	6.3
B1. Direct Taxes (Taxes on Income)	0.0	0.8	4.6	4.3	4.3	4.6	5.0	5.4
Direct Taxes as a % of GDP	0.0	0.2	1.2	1.2	1.2	1.2	1.3	1.2
Individual Income Tax	0.0	0.6	2.3	2.2	2.2	2.4	2.6	2.9
Income and Final Withholding Tax	0.0	0.2	2.3	2.1	2.1	2.2	2.4	2.5
B2. Indirect Taxes (Taxes on Commodities)	2.0	11.4	12.4	14.3	13.7	14.5	15.3	17.0
Indirect Taxes as a % of GDP	0.7	3.2	3.3	4.0	3.9	3.9	3.8	3.9
Sales Tax	0.0	3.0	3.2	4.0	4.0	4.2	4.4	4.9
Excise	0.0	4.0	4.3	5.0	5.0	5.2	5.4	5.9
Import Duties	2.0	2.6	2.9	3.4	2.8	3.1	3.3	3.7
Export Duties	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Service Tax	0.0	1.7	2.0	1.9	1.9	2.0	2.2	2.5
B3. Non Tax Revenue	0.0	3.3	2.4	2.7	2.7	3.3	5.0	5.2
Non Tax Revenues as % of GDP	0.0	0.9	0.6	0.8	0.8	0.9	1.3	1.2
User Fees and Charges	0.0	2.6	1.3	1.4	1.5	1.5	1.6	1.7
Other Non Tax Revenues (Including Interest)	0.0	0.6	1.1	1.3	1.2	1.8	3.4	3.5
C. Timor Sea Oil / Gas Revenue	0.0	12.9	12.0	21.3	32.7	76.4	76.4	99.1
Oil / Gas Revenue as % of GDP	0.0	3.6	3.2	6.0	9.3	20.6	19.1	22.7
First Tranche Petroleum	0.0	3.0	6.0	0.8	6.6	24.2	22.3	29.5
Taxes	0.0	9.9	6.0	20.5	26.1	52.2	54.1	69.6
D. FOREIGN GRANTS	154.2	258.2	260.9	180.7	146.7	106.1	85.0	85.0
Foreign Grants as a % of GDP	52.1	72.7	68.7	50.5	41.8	28.7	21.3	19.5
Trust Fund for East Timor	69.1	46.2	49.2	49.0	17.7	0.0	0.0	0.0
Direct Donor Budget Support	41.6	22.0	30.0	35.7	39.0	21.1	0.0	0.0
Projects Administered by Bilateral Donors	27.9	90.0	86.7	85.0	85.0	85.0	85.0	85.0
U.N. Assessed Contribution	15.6	100.0	95.0	11.0	5.0	0.0	0.0	0.0
F. TOTAL REVENUE AND GRANTS (A+D)	156.2	286.6	292.3	223.3	200.1	204.9	186.7	211.7
Total Revenue and Grants as % of GDP	52.8	80.7	76.9	62.4	57.0	55.4	46.7	48.6

Sources: (a) Ministry of Finance for FY 00 to FY 03; and (b) Planning Commission for FY 04 to FY 07

Notes:

1. First tranche petroleum revenue is currently accumulated in a Special Timor Sea Account. In future all oil revenues may go firstly to an offshore account.

2. General U.N. assessed contributions only include estimates of U.N. funded activities that are likely to directly affect the operations of Government through the CFET budget (This reflects mainly TA and staffing. Non recurring items such as peacekeeping; New York activities etc. are not included here).

Table 3.

Combined Sources Expenditure (Economic Format), FY 00 to FY 07 (US\$ Millions)

	FY00	FY01	FY02	FY03	FY04	FY05	FY06	FY07
	Actual	Actual	Budget Revised	Budget Prelim.	Estimate	Estimate	Estimate	Estimate
A. RECURRENT EXPENDITURE (CFET Only)	28.7	29.6	47.0	60.9	68.2	73.7	79.5	85.9
As % of GDP	9.7	8.3	12.4	17.0	19.4	19.9	19.9	19.7
As % of Total Expenditure	18.4	10.3	16.2	27.4	35.2	40.8	42.2	43.7
Wages and Salaries	14.6	13.9	20.7	25.8	27.4	29.6	32.0	34.5
Goods and Services	14.1	15.7	26.3	35.1	40.8	44.1	47.6	51.4
B. CAPITAL & DEVELOPMENT EXPENDITURE	127.5	257.9	242.3	161.3	125.3	107.0	108.8	110.7
As % of GDP	43.1	72.6	63.8	45.1	35.7	28.9	27.2	25.4
As % of Total Expenditure	81.6	89.7	83.8	72.6	64.8	59.2	57.8	56.3
Consolidated Fund for East Timor	14.9	21.7	11.4	16.3	17.6	22.0	23.8	25.7
Trust Fund for East Timor	69.1	46.2	49.2	49.0	17.7	0.0	0.0	0.0
Bilateral Development Projects	27.9	90.0	86.7	85.0	85.0	85.0	85.0	85.0
UNTAET Indirect CFET Budget Support	15.6	100.0	95.0	11.0	5.0	0.0	0.0	0.0
C. TOTAL EXPENDITURE (A+B)	156.2	287.5	289.3	222.2	193.5	180.7	188.3	196.6
As % of GDP	52.8	80.9	76.1	62.1	55.1	48.8	47.1	45.1
Memorandum Items:								
Total CFET Expenditure	43.6	51.3	58.4	77.2	85.8	95.7	103.3	111.6
Growth in CFET Expenditures (%)		17.7	13.8	32.2	11.1	11.5	8.0	8.0

Sources: As per Table 2

Notes:

1. General U.N. assessed contributions only include estimates of UN funded activities that are likely to directly affect the operations of Government through the CFET budget (non recurring items such as peacekeeping; New York activities etc.) are not included here
2. All TFET; Bilateral and UNTAET expenditures recorded as Capital and Development, though significant portions of them are actually recurrent in nature
3. Preliminary estimates for FY 03 are based on total outlays of US\$ 77.2 million, notwithstanding that COM is still considering a range of outlays between US\$ 67.4 million and US\$ 77.2 million. Reasons justifying the use of US\$ 77.2 million are set out at section 7.20 of the text

Table 4.

Combined Sources Financing (Economic Format), FY 00 to FY 07 (US\$ Millions)

	FY00 Actual	FY01 Actual	FY02 Budget Revised	FY03 Budget Prelim.	FY04 Estimate	FY05 Estimate	FY06 Estimate	FY07 Estimate
A. TOTAL REVENUE (Excluding Grants)	2.0	28.4	31.4	42.6	53.4	98.8	101.7	126.7
Total Revenue as % of GDP	0.7	8.0	8.3	11.9	15.2	26.7	25.4	29.1
B. MINUS TOTAL EXPENDITURE	156.2	287.5	289.3	222.2	193.5	180.7	188.3	196.6
Total Expenditure as % of GDP	52.8	80.9	76.1	62.1	55.1	48.8	47.1	45.1
C. EQUALS DEFICIT (-) / Surplus (+)	-154.2	-259.1	-257.9	-179.6	-140.1	-81.9	-86.6	-69.9
Total Deficit as % of GDP	-52.1	-72.9	-67.9	-50.2	-39.9	-22.1	-21.7	-16.0
D. FINANCING OF DEFICIT								
Trust Fund for East Timor	69.1	46.2	49.2	49.0	17.7	0.0	0.0	0.0
Direct Donor Budget Support	41.6	22.0	30.0	35.4	39.0	21.1	0.0	0.0
Projects Administered by Bilateral Donors	27.9	90.0	86.7	85.0	85.0	85.0	85.0	85.0
U.N. Assessed Contribution	15.6	100.0	95.0	11.0	5.0	0.0	0.0	0.0
Increase (-) / Decrease (+) in Cash Balances	0.0	0.9	-3.0	-0.8	-6.6	-24.2	1.6	-15.1
TOTAL FINANCING	154.2	259.1	257.9	179.6	140.1	81.9	86.6	69.9
Memorandum Item:								
Cumulative Cash Balance Levels	0.0	-0.9	2.1	3.0	9.9	35.1	34.5	51.1

Sources: As per Tables 2 and 3

Table 5.

Consolidated Fund for East Timor. Total Expenditure by Agency, FY 02 to FY 07
(US\$ 000)

	FY02 Revised Budget	FY03 Preliminary Budget	FY04 Estimate	FY05 Estimate	FY06 Estimate	FY07 Estimate
1. Government and Administration	7,767	7,903	8,061	8,222	8,387	8,554
1.1 Chief Ministers Office	783	461	470	480	489	499
1.2 Legislative Assembly	851	883	901	919	937	956
1.3 Independent Electoral Commissioner	11	59	60	61	63	64
1.4 Banking and Payments Authority	1,374	1,080	1,102	1,124	1,146	1,169
1.5 ETDF Command	4,214	4,429	4,518	4,608	4,700	4,794
1.6 Office of President	90	404	412	420	429	437
1.7 Other Ministers - Bulk	382	539	550	561	572	583
1.8 Ombudsman	62	48	49	50	51	52
2. Ministry of Internal Administration	9,272	11,769	12,004	12,244	12,489	12,739
2.1 East Timor Police Service	6,707	7,806	7,962	8,121	8,284	8,449
2.2 Internal Administration / Local Administration / Other	2,565	3,963	4,042	4,123	4,206	4,290
3. Ministry of Justice	2,390	2,078	2,120	2,162	2,205	2,249
4. Ministry for Economic Affairs and Planning	7,256	4,565	3,478	3,142	553	564
4.1 Department of Natural and Mineral Resources	115	168	171	175	178	182
4.2 Department of Economic Affairs and Development	325	353	360	367	375	382
4.3 Energy Subsidy	6,816	4,044	2,947	2,600		
5. Ministry for Agriculture and Fisheries	881	1,373	1,716	2,060	2,471	2,966
6. Ministry of Education, Culture and Youth	13,061	16,653	20,816	24,980	29,975	35,970
7. Ministry of Health	5,313	7,079	8,849	10,619	12,742	15,291
8. Labour and Solidarity	234	480	490	499	509	520
9. Ministry of Foreign Affairs and Cooperation	272	671	684	698	712	726
10. Ministry of Finance	5,727	3,782	3,858	3,935	4,013	4,094
10.1 Ministry Operations	3,742	2,247	2,292	2,338	2,385	2,432
10.2 Whole of Government Payments / Contingencies	1,985	1,535	1,566	1,597	1,629	1,662
11. Ministry of Water and Public Works	5,601	5,467	6,834	8,201	9,841	11,809
12. Ministry of Communications and Transport	460	1,388	1,416	1,444	1,473	1,502
13. Bulk Unallocated Funding / Other	146	14,004	15,474	17,495	17,928	14,616
13.1 Recurrent	146	2,112	1,300	1,350	1,400	1,500
13.2 Capital		11,892	14,174	16,145	16,528	13,116
14. Total Expenditure (Current + Capital)	58,380	77,212	85,800	95,700	103,300	111,600

Sources: (a) Ministry of Finance for FYs 02 and 03 and; (b) Planning Commission estimates for FYs 04 to 07

Notes:

1. Data for FY 03 based on very preliminary budget data
2. Estimates for FY 04 to FY 07 based on a policy based scenario of the Planning Commission's as set out in Chapter 7 of the Development Plan

Table 6

**Consolidated Fund for East Timor, Expenditure, FY 02 to FY 07 (by Functional Classification)
(US\$ 000 and %)**

Function	FY02 Revised Budget	FY03 Preliminary Budget	FY04 Budget	FY05 Budget	FY06 Budget	FY07 Budget
1. General Public Services	8,529	9,484	9,674	9,867	10,064	10,266
As % of Total CFET	14.6	12.3	11.3	10.2	9.7	9.2
Executive and Legislative Organs	3,025	4,268	4,353	4,440	4,529	4,620
Financial and Fiscal Affairs	3,554	3,785	3,861	3,938	4,017	4,097
Foreign Affairs	272	671	684	698	712	726
General Services	1,678	760	775	791	807	823
2. Defence	4,903	5,323	5,429	5,538	5,649	5,762
As % of Total CFET	8.4	6.9	6.3	5.7	5.5	5.2
3. Public Order and Safety	9,812	10,150	10,353	10,560	10,771	10,987
As % of Total CFET	16.8	13.1	12.1	10.9	10.4	9.8
Police Services	6,807	7,806	7,962	8,121	8,284	8,449
Fire Protection Services	470	374	381	389	397	405
Law Courts and Prisons	2,535	1,970	2,009	2,050	2,091	2,132
4. Economic Affairs	11,855	9,865	9,227	9,352	7,309	7,957
As % of Total CFET	20.3	12.8	10.8	9.7	7.1	7.1
General Economic, Commercial & Labour Services	299	319	325	332	339	345
Agriculture, Forestry, Fishing and Hunting	775	1,097	1,371	1,646	1,975	2,370
Fuel and Energy	6,841	4,106	3,000	2,655	64	70
Mining, Manufacturing, Construction	987	437	546	656	787	944
Other Industry	8	306	312	318	325	331
Transport	2,658	2,749	2,804	2,860	2,917	2,976
Communications	287	851	868	885	903	921
5. Environment, Housing and Community Development	2,417	2,743	3,393	4,043	4,823	5,758
As % of Total CFET	4.1	3.6	4.0	4.2	4.7	5.2
Community Development	0	90	92	94	96	97
Water Supply and Sanitation	2,343	2,588	3,235	3,882	4,658	5,590
Environment	74	65	66	68	69	70
6. Health	4,411	7,080	8,850	10,620	12,744	15,293
As % of Total CFET	7.6	9.2	10.3	11.0	12.3	13.7
7. Education, Recreation, Culture, Religion	13,061	16,528	20,660	24,792	29,750	35,700
As % of Total CFET	22.4	21.4	24.1	25.6	28.8	32.0
8. Unallocated (Mainly Capital / Infrastructure)	3,392	16,039	18,214	21,928	22,189	19,878
As % of Total CFET	5.8	20.8	21.2	22.7	21.5	17.8
TOTAL	58,380	77,212	85,800	96,700	103,300	111,600

Sources: As per Table 5

Notes:

1. Data for FY 03 based on very preliminary budget data
2. Estimates for FY 04 to FY 07 based on a policy based scenario of the Planning Commission's as set out in Chapter 7 of the Development Plan

Table 7

Balance of Payments, 2000 - 2007, US\$ (Millions)

	2000	2001	2002	2003	2004	2005	2006	2007
	Estimate	Estimate	Outlook	Outlook	Outlook	Outlook	Outlook	Outlook
Trade Balance	-199.9	-233.5	-187.3	-151.4	-150.1	-147.6	-147.7	-155.0
As % of GDP	-62.2	-60.0	-50.5	-43.9	-42.0	-38.6	-35.4	-34.1
Merchandise Exports	4.9	4.0	9.4	16.7	20.7	28.4	34.8	40.0
As % of GDP	1.5	1.0	2.5	4.8	5.8	7.4	8.3	8.8
- Coffee	4.4	2.9	5.2	9.5	11.4	16.4	20.6	24.0
- Other	0.5	1.1	4.2	7.2	9.3	12.0	14.2	16.0
Merchandise Imports	-204.8	-237.5	-196.7	-168.1	-170.8	-176	-182.5	-195
As % of GDP	-63.8	-61.0	-53.1	-48.7	-47.8	-46.0	-43.7	-42.9
- Public	-152.0	-143.0	-99.6	-72.3	-70.1	-66.5	-63.0	-65.0
Of which UNTAET and humanitarian	-112.2	-59.2	-13.2	-8.9	-3.0	0.0	0.0	0.0
- Private	-52.8	-94.5	-97.1	-95.8	-100.7	-109.5	-119.5	-130.0
Services Account (Net)	-57.7	-61.3	-49.9	-38.4	-25.1	-20.6	-19.2	-18
As % of GDP	-18.0	-15.7	-13.5	-11.1	-7.0	-5.4	-4.6	-4.0
Income (Net)	3.0	4.4	1.6	3.0	19.1	29.6	28.5	31.0
As % of GDP	0.9	1.1	0.4	0.9	5.3	7.7	6.8	6.8
Of which Oil Royalties	3.0	4.2	2.3	5.0	20.6	31.0	29.6	32.0
Current Transfers (Net)	307.2	279.7	165.8	131.3	105.1	103.8	105.3	108.0
As % of GDP	95.6	71.8	44.7	38.0	29.4	27.1	25.2	23.7
Of which Oil Tax Revenue	2.5	10.3	16.8	31.1	52.2	70.9	70.9	70.0
Of which UNTAET and humanitarian	232.0	171.9	64.4	43.4	14.5	0.0	0.0	0.0
Current Account Including Official Transfers	52.6	-10.7	-69.8	-55.5	-51.0	-34.8	-33.1	-34.0
As % of GDP	16.4	-2.7	-18.8	-16.1	-14.3	-9.1	-7.9	-7.5
Current Account Excluding Official Transfers	-254.5	-290.0	-235.1	-185.7	-154.1	-136.2	-135.6	-134.2
As % of GDP	-79.2	-74.5	-63.4	-53.8	-43.1	-35.6	-32.5	-29.5
Capital and Financial Account	-4.2	36.0	46.9	29.0	35.8	35.1	49.2	51.0
As % of GDP	-1.3	9.2	12.7	8.4	10.0	9.2	11.8	11.2
Of which Capital Account	49.6	67.0	61.6	45.9	13.8	10.5	10.1	10.0
Of which Financial Account	-53.8	-31.0	-14.7	-16.9	21.9	24.6	39.1	40.0
Errors and Omissions	-32.4	-17.6	0.0	0.0	0.0	0.0	0.0	0.0
Overall Balance (Before Financing Support)	16.0	7.7	-22.9	-26.5	-15.2	0.3	16.1	17.0
Gross Reserves (Before Financing Support)	19.0	26.7	3.8	-22.7	-37.9	-37.6	-21.5	-4.5
Timor Sea Offshore Account	0.0	3.0	9.1	10.4	17.6	42.9	42.0	58.5

Source: Planning Commission and IMF

Table 8.

Approved and Programmed Foreign ODA by Country and Type, FY 00 TO FY 07. (US\$ 000)

	FY00 Actual	FY01 Actual	FY02 Estimate	FY03 Estimate	FY04 Estimate	FY05 Estimate	FY06 Estimate	FY07 Estimate	Total Period Estimate
A. TRUST FUND FOR EAST TIMOR (TFET)									
ADB - Capital	-	10,342	13,104	9,824	8,000	-	-	-	41,270
ADB - TA	-	5,257	4,195	1,641	-	-	-	-	11,093
ADB - Total	-	15,599	17,299	11,465	8,000	-	-	-	52,363
WB - Capital	-	27,167	25,974	33,106	8,487	-	-	-	94,733
WB - TA	-	3,390	5,927	4,430	1,213	-	-	-	14,960
WB - Total	-	30,557	31,901	37,535	9,700	-	-	-	109,693
Total - Capital	-	37,509	39,078	42,929	16,487	-	-	-	136,003
Total - TA	-	8,647	10,122	6,071	1,213	-	-	-	26,053
Total TFET	-	46,156	49,200	49,000	17,700	-	-	-	162,056
B. MULTILATERALS AND BILATERALS (NON TFET)									
ADB - Capital									
ADB - TA		150	5,023	350					5,523
ADB - Total		150	5,023	350					5,523
Australia - Capital	375	2,835	14,862	9,400	8,040	2,200			37,712
Australia - TA	2,105	8,587	19,849	15,805	12,226	3,090			61,662
Australia - Total	2,480	11,422	34,711	25,205	20,266	5,290			99,374
Canada - Capital		260	1,115	835	690	105			3,005
Canada - TA	680	2,385	2,542	580	250	100			6,537
Canada - Total	680	2,645	3,657	1,415	940	205			9,542
ECHO - Capital	5,425	5,980	7,730						19,135
ECHO - TA	400	315	210						925
ECHO - Total	5,825	6,295	7,940						20,060
Japan - Capital	750	18,832	7,311	10,270	5,920	4,810			47,893
Japan - TA	857	9,995	4,747	3,317	1,140	29			20,085
Japan - Total	1,607	28,827	12,058	13,587	7,060	4,839			67,978
Portugal - Capital	6,752	8,731	7,928	5,229	2,090	100	100	700	31,630
Portugal - TA	630	6,923	7,747	6,570	1,480				23,350
Portugal - Total	7,382	15,654	15,675	11,799	3,570	100	100	700	54,980
USAID - Capital	7,850	9,657	5,600	2,300	1,550				26,957
USAID - TA	270	3,207	5,048	698					9,223
USAID - Total	8,120	12,864	10,648	2,998	1,550				36,180
Other Bilaterals - Capital	643	8,439	7,658						16,740
Other Bilaterals - TA	1,134	2,706	3,217						7,057
Other Bilaterals - Total	1,777	11,145	10,875						23,797
UNDP Capital	32	1,042	900						1,974
UNDP TA			3,762	1,481	886	1,450	1,450		9,029
UNDP Total	32	1,042	4,662	1,481	886	1,450	1,450		11,003
Other Multilaterals - Capital			1,584						1,584
Other Multilaterals - TA			2,955	100					3,055
Other Multilaterals - Total			4,539	100					4,639
GRAND TOTAL - Capital	21,827	55,776	54,688	28,034	18,290	7,215	100	700	186,630
GRAND TOTAL - TA	6,076	34,268	55,100	28,901	15,982	4,669	1,450	-	146,446
GRANDTOTAL - Capital + TA	27,903	90,044	109,788	56,935	34,272	11,884	1,550	700	333,076
C. (TFET + NON TFET)									
GRAND TOTAL - Capital	21,827	93,285	93,766	70,963	34,777	7,215	100	700	322,633
GRAND TOTAL - TA	6,076	42,915	65,222	34,972	17,195	4,669	1,450	-	172,499
GRANDTOTAL - Total	27,903	136,200	158,988	105,935	51,972	11,884	1,550	700	495,132

Source: Ministry of Finance, ODA Database and Planning Commission

Note: Only includes approved and fully programmed projects. Does not include bulk amounts notionally targeted by Donors for future plan years

Table 9.

Total Approved and Programmed Bilateral ODA by Agency, FY 00 to FY 07. (US\$ 000)

		FY00	FY01	FY02	FY03	FY04	FY05	FY06	FY07	Total Period	% Of
		Actual	Actual	Estimate	Total						
1. Transitional Administration	- Total	738	9,290	21,623	9,833	5,934				47,418	14.2
	- Capital	50	2,017	9,594	4,560	2,050				18,271	5.5
	- TA	688	7,273	12,029	5,273	3,884				29,147	8.8
2. Internal Administration	- Total	2,529	3,258	4,160						9,947	3.0
	- Capital	1,800	786	300						2,886	0.9
	- TA	729	2,472	3,860						7,061	2.1
3. Justice	- Total	695	3,203	2,135	198					6,231	1.9
	- Capital	420	2,320	285	-					3,025	0.9
	- TA	275	883	1,850	198					3,206	1.0
4. Econ. Affairs & Development	- Total		7,461	3,336	585	150	100			11,632	3.5
	- Capital		5,840	1,577	325	-	-			7,742	2.3
	- TA		1,621	1,759	260	150	100			3,890	1.2
5. Agriculture & Fisheries	- Total	4,763	19,073	13,620	8,578	7,236	5,809	1,450		60,529	18.2
	- Capital	4,412	17,163	5,247	5,280	6,230	4,330	-		42,662	12.8
	- TA	351	1,910	8,373	3,298	1,006	1,479	1,450		17,867	5.4
6. Education, Culture, Youth	- Total	2,071	9,184	15,023	13,231	6,526	1,190			47,225	14.2
	- Capital	1,795	3,272	4,270	1,000	1,000	-			11,337	3.4
	- TA	276	5,912	10,753	12,231	5,526	1,190			35,888	10.8
7. Health	- Total	8,962	9,239	7,354	5,270	4,365	500	100	700	36,490	11.0
	- Capital	8,490	8,505	3,566	2,800	2,300	100	100	700	26,561	8.0
	- TA	472	734	3,788	2,470	2,065	400			9,929	3.0
8. Labour and Solidarity	- Total	3,605	5,610	9,037	4,500	1,851				24,603	7.4
	- Capital	3,605	3,647	4,339	2,029	-				13,620	4.1
	- TA		1,963	4,698	2,471	1,851				10,983	3.3
9. Foreign Affairs	- Total	20	80	3,707						3,807	1.1
	- Capital	-	-	3,629						3,629	1.1
	- TA	20	80	78						178	0.1
10. Finance	- Total	315	877	4,460	1,700	1,500	1,500			10,352	3.1
	- Capital	135	201	2,175	-	-	-			2,511	0.8
	- TA	180	676	2,285	1,700	1,500	1,500			7,841	2.4
11. Water, Public Works	- Total	3,605	18,569	21,583	11,720	5,310	1,785			62,572	18.8
	- Capital	1,120	10,140	19,216	10,720	5,310	1,785			48,291	14.5
	- TA	2,485	8,429	2,367	1,000					14,281	4.3
12. Communications & Transport	- Total	600	4,200	3,750	1,320	1,400	1,000			12,270	3.7
	- Capital	-	1,885	490	1,320	1,400	1,000			6,095	1.8
	- TA	600	2,315	3,260						6,175	1.9
Total All Sectors		27,903	90,044	109,788	56,935	34,272	11,884	1,550	700	333,076	100.0
Total - Capital		21,827	55,776	54,688	28,034	18,290	7,215	100	700	186,630	
Total - TA		6,076	34,268	55,100	28,901	15,982	4,669	1,450	-	146,446	

Source: Ministry of Finance, ODA Database and Planning Commission

Notes: 1. Excludes expenditures under the Trust Fund for East Timor
 2. Only includes approved and fully programmed projects. Does not include bulk amounts notionally targeted by Donors for future plan years

Table 10.

Profile of the Forward ODA Program Needed to Finance the Plan, FY 03 TO FY 07 (US\$ Millions)

	FY03	FY04	FY05	FY06	FY07
	Estimate	Estimate	Estimate	Estimate	Estimate
A. FORWARD ODA PROGRAM SOUGHT BY THE GOVERNMENT					
Trust Fund for East Timor	49.0	17.7	0.0	0.0	0.0
Direct Donor Budget Support	35.4	39.0	21.1	0.0	0.0
Projects Administered by Bilateral Donors	85.0	85.0	85.0	85.0	85.0
U.N. Assessed Contribution - Recurrent; Capital; and Development	11.0	5.0	0.0	0.0	0.0
TOTAL SOUGHT	180.4	146.7	106.1	85.0	85.0
B. AMOUNTS APPROVED / FIRMLY COMMITTED					
Trust Fund for East Timor	49.0	17.7	0.0	0.0	0.0
Direct Donor Budget Support	0.0	0.0	0.0	0.0	0.0
Projects Administered by Bilateral Donors	56.9	34.3	11.9	1.6	0.7
U.N. Assessed Contribution - Recurrent; Capital; and Development	11.0	5.0	0.0	0.0	0.0
SUB TOTAL	116.9	57.0	11.9	1.6	0.7
C. AMOUNTS NOT YET APPROVED / FIRMLY COMMITTED					
Trust Fund for East Timor	0.0	0.0	0.0	0.0	0.0
Direct Donor Budget Support	35.4	39.0	21.1	0.0	0.0
Projects Administered by Bilateral Donors	28.1	50.7	73.1	83.4	84.3
U.N. Assessed Contribution - Recurrent; Capital; and Development	0.0	0.0	0.0	0.0	0.0
SUB TOTAL	63.5	89.7	94.2	83.4	84.3

Source: As per Tables 4,8 and 9

