

Economic and Social Development Brief

August 2007



*Prepared by The World Bank Group and the Asian Development Bank,
in consultation with Development Partners*



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I. Healing the Nation: Today's Economic Priorities

1. The new Government will give top priority to resolving Timor-Leste's political and security crisis. Achieving stability, however, also means reviving the stagnant economy and tackling the country's alarming social problems. This paper and its attachments concentrate on how this socio-economic revival can be initiated. The paper and the sector notes accompanying it have been prepared by The World Bank Group (including the World Bank and IFC) and the ADB as a service to the new Government, and are offered in a spirit of friendship and commitment to the country's future.

2. The economy will not revive without better security and the restoration of people's faith in their leaders. This means radical reform of the police and the army. It means halting community violence so that IDPs feel safe enough to return home. It means delivering proper justice, and holding to account those who broke the law in 2006. These subjects will be addressed in detail in the brief that the United Nations is preparing, but their fundamental importance needs acknowledging here.

3. Provided the Government tackles the security situation decisively, economic progress is definitely feasible. Turning possibility into reality, however, will take leadership and great focus. In this Brief we suggest six priority economic areas, progress in which can lead the transformation of Timor-Leste's underperforming economy and can help restore the people's confidence in a future in which they can obtain work, feed their families and live lives of dignity.

4. There is an overarching need for the Government to communicate its goals and programs more clearly to the population than in the past. If the citizenry are kept honestly informed, they will develop greater trust in their leaders. If they are asked to help design and monitor the development programs that affect them, their commitment to those programs will increase and they will contribute a great deal to their successful realization.

Priority One---Transparent Management of the Country's Petroleum Revenues

5. Timor-Leste's petroleum reserves are the key to the country's prosperity and independence. Total petroleum savings amounted to US\$1.4 billion on June 30, 2007, with approximately US\$100 million in new revenues each month. Mindful of the problems that many countries rich in natural resources have experienced---wasteful spending, widespread corruption---the previous Government created a petroleum management structure which is seen as an international 'best practice' model. First, petroleum revenues are deposited in a Petroleum Fund managed by the Banking and Payments Authority (BPA). Because oil and gas reserves will not last forever, BPA then invests all the proceeds to ensure that Timor-Leste will maintain the real dollar value of its petroleum earnings in perpetuity; and interest income of the Petroleum Wealth is passed on to the Government Budget. At present, over US\$300 million is sustainably available for the Budget each year.

6. It is vital that the current petroleum revenue management arrangements are preserved. It is equally important that the revenues allocated to the budget are invested in programs that build the nation's capital and enhance productivity in non-oil sectors---that is to say, in investments in infrastructure and human development (education, health and social protection---paragraph 15), increasing delivery of services.

7. It is recommended that the petroleum savings policy be preserved and the current framework further strengthened to ensure continued transparency and the preservation of the country's oil wealth.

Economic Stagnation

By fiscal year 2004-5, economic growth had turned positive, and macroeconomic stability had been achieved through sound fiscal management. In mid-2006, however, economic activity in Dili came to a virtual stand-still. Outlying districts suffered disruptions to supply, the loss of a significant part of the coffee crop, and a failure of the transport system. Almost all Timorese earn their living in the non-oil sectors, where per capita incomes have been stagnant in real terms since 2002. Consumer prices have also increased by about 13% since March 2006. Companies and individuals have struggled to make loan payments, and around one-third of the nation's loan portfolio is now non-performing. Private investment is minimal, with insecurity compounding one of the most unattractive business climates in the world (paragraph 11). As a result, job creation has stalled---it is estimated that some 15,000 young people enter the labor market each year, while only 400 formal jobs are being created. According to the 2004 census, unemployment in Dili was estimated at 23%, and youth unemployment at 40%, rising to 58% for the 15-19 year-old age bracket. With half the population under 18, urban youth unemployment and the problems associated with it are destined to increase unless vigorous growth in the non-oil sectors can be created. Poverty in Timor-Leste---defined as capacity to buy food and non-food consumption requirements equivalent to earnings of less than US\$0.55 per day---afflicted about 39.7% of the population in 2001 and is on the increase.

Note: US\$0.55 cents in Timor are equivalent to US\$1.5 in international dollars using the Purchasing Power Parity measure.

Priority Two---Budget Execution

8. In time, a vibrant private sector should become the main source of economic growth and job creation. For now, given the undeveloped nature of the private sector, Government spending has to perform this role. At present, though, the Government is unable to spend the resources at its disposal, due to weak capacity and cumbersome, over-centralized systems. By the end of the third quarter of fiscal year 2006-7, only US\$81 million had been spent from a Central Government Budget of US\$320 million. Execution of the Capital Budget was particularly poor, with only 2.6%, or US\$3 million out of US\$120 million, spent by the end of the third quarter.

9. This problem can be fixed, however, and immediate steps can be taken to improve budget execution. These include:

- A concerted Ministry of Finance program of training key line ministry personnel in basic financial management procedures;
- Access to the computerized financial management information system, *Freebalance*, for line ministries and state agencies;
- Raising the delegated procurement threshold for line ministries from US\$100,000 to at least US\$250,000; and
- Reintroduction of imprest accounts for all state agencies and ministries to expedite small but urgent, purchases.

Government spending on infrastructure and services will serve as the engine of economic growth in the immediate future. It will be important to pay close attention to the composition of spending---in particular, excessive increases in public sector wages can further increase the country's comparatively high wage rates.

Priority Three---Addressing the Youth Crisis

10. The prevailing image of Timorese youth is one of street gangs, arson and anarchy---yet this is the generation that needs to build the new nation: the 15-29 year-old age group is likely to represent almost 40% of all Timorese by 2010. Far too many young people today are unemployed, and few have marketable skills. Many suffer domestic violence, drink heavily, feel disconnected from their communities and distrust the Government and the older generation. The breakdown in social control since April 2006 has also encouraged some young people to act without fear of retribution.

11. Rectifying this critical issue and releasing the positive energy of Timor-Leste's young people will demand a high degree of Government commitment and a comprehensive, long-term approach. Turning today's disaffected youngsters into tomorrow's economic pioneers requires a holistic national strategy and the clear designation of a powerful Government office to lead it. Key components of such a strategy will need to include

- Efforts to keep youngsters in school (paragraph 15), since numerous benefits accrue to both the individual and society when youth complete their education; 'second chance' programs that encourage dropouts to return to education are also needed;
- Attacking youth employment, not least because unemployed youngsters are susceptible to manipulation and to being drawn into violence and risky behavior. Taking account of institutional capacities, the World Bank believes it feasible to put in place a nation-wide public works program that would employ at least 50,000 workers for 50 days per annum initially, building to 100,000 workers for 75 days at an annual cost of about US\$25 million. This program could be oriented to youth as well as to the poor (paragraph 15).
- Connecting youth with their communities by reinvigorating youth centers, and searching for ways of involving young people in nation-building, for example by

the creation of representative youth councils that would be given important responsibilities in the development process.

Priority Four---Creating an Environment for Private Investment

12. Timor-Leste is reputed to be the second-worst country in the world for ease of doing business, ranking as an embarrassing 174 out of 175 countries profiled in the World Bank/International Finance Corporation's *Doing Business* reports. Many administrative procedures are burdensome and expensive; the courts are overloaded and ineffective, and resolving contract and labor disputes is nearly impossible; infrastructure is poor and business input costs very high (telecommunication charges are four times those in Indonesia, and wages several times those in surrounding countries); business support services such as accounting, auditing and private legal practices are almost non-existent.

13. As the country's oil wealth begins to be invested, contractors and investors will be attracted to the country---but only provided the business environment is fixed. Immediate steps that can be taken include

- Approval of the Land Law, drafted in 2005, which clarifies ownership and facilitates land sales; once enacted, this law will encourage the use of land as collateral and is likely to spur investment in agricultural development and resource conservation. The Directorate for Land and Property at the Ministry of Justice should also commence work on building a register of land ownership and mapping plots, supported by appropriate donor technical assistance;
- Amending laws that are inconsistent and overly complex will reduce red tape and encourage new investment; examples of legislation needing revision include the Commercial Societies Act (company law), the Commercial Registry Code (business registration) and the investment laws. A proposal to ease business start-up procedures was considered by the Council of Ministers at the end of 2006, but has not yet been approved and implemented;
- Supporting the growth of microfinance: supportive measures would include provisions for safely transferring cash around the country, the establishment of a credit registry, and exploring options for providing insurance. At the same time the Government should avoid providing credit guarantees or establishing new banks: access to investment capital is needed, but is best provided on commercial terms by established banks and microfinance agencies.

Priority Five---Improving Service Delivery

14. In October 2006, the Council of Ministers approved a decentralization policy under which authority and resources would be devolved to 30-35 new sovereign municipalities. This initiative warrants reconsideration. While decentralization could, in time, empower local communities and bring public services closer to the population, the immediate result in the Timorese context could be weaker service provision and financial accountability at a time when the Government needs to deliver effective, clean services throughout the country. Finding staff

for the proposed new structures would also strain today's limited supplies of skilled personnel. A more cautious approach is therefore advised.

- A preliminary step might be the mapping of existing service delivery systems at the local level and the identification of service gaps;
- Identified gaps as well as plans for service expansion and quality enhancement can then be addressed by greater delegation of authority for planning, procurement and financial management to the district and sub-district levels, combined with a greater degree of community involvement in service programming and monitoring;
- At the same time, promising mechanisms such as the new district budget initiatives, the Local Development Program and Suco Council projects could be strengthened, and provided with more systematic support from the Central Government, particularly in financial management;
- This approach would provide time to explore and test appropriate models of decentralization, but without risking setbacks in the delivery of the services by which the population will judge the efficacy of the new Government.

Priority Six---Protecting the Most Vulnerable

15. Timor-Leste's petroleum wealth allows a prudent program of targeted subsidies to the poor and vulnerable; these would not only increase equity but would contribute materially to the human capital formation essential to sustained growth. In the short term, several possibilities are worth exploring, always with attention to their sustainability over time. These include

- The public works program mentioned in paragraph 11 above;
- A program of modest transfers to the disabled, and of pensions to the elderly (as well as commencing the payment of veterans' pensions);
- Conditional cash transfers (CCTs) in the area of health and education, which have registered clear benefits in many countries and could usefully, be piloted in Timor. CCTs provide cash payments to poor families to promote health or education goals, such as the vaccination of children, delivering at health facilities, or sending children to school/keeping them enrolled.

II. Sector Notes

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1. Sector Note: Agriculture

Overview

Agriculture dominates Timor-Leste's economy and the livelihoods of the majority of Timorese. Agriculture makes up 30% of non-petroleum GDP, and 80% of the population is dependent on agriculture, forestry, and fisheries for their livelihoods. A third of Timorese households rely on subsistence agriculture exclusively. 98% use firewood as their primary source of energy. But agricultural productivity is low and quality problems also hinder exports. Improved productivity, including addressing losses due to spoilage and pests, enhancing the quality of agricultural crops, increasing investment in rural areas and addressing the issue of land property¹ are key steps in reducing rural poverty and improving food security.

Key Issues

- ***Enhancing agricultural productivity.*** Productivity can be raised through a functioning agricultural extension system. This includes testing and promoting the adoption of improved seed varieties, improving water management and also animal husbandry practices. Mitigating agricultural losses due to spoilage and pests, such as rodents and insects (currently very high) will also improve productivity and reduce vulnerability to food shortages.
- ***Developing agricultural markets.*** Investment in value-added and export commodities is essential. Provision of better information on prices and export opportunities will help stimulate agricultural markets. Functioning markets will contribute to reduce vulnerability to food shortages.
- ***Improving agricultural productivity and diversify sources of rural income through better private investment climate in rural areas.*** Passing the land law and creating a system for land registration is essential to increasing investment. Improved rural infrastructure, including transport and electricity, and access to credit are also important.
- ***Managing environmental degradation.*** There is tremendous pressure on agricultural, pasture and forest land which is impacting on agricultural productivity. The flow of environmental (e.g. hydrological, erosion control) services could be disrupted if land is not sustainably managed.

The Sector

Food crops (maize, rice, peanut, cassava and sweet potato), tree crops (candlenut, coconut, coffee, cinnamon and cloves) and livestock are Timor-Leste's major agricultural

¹ Land property is addressed also in the Private Sector Development section of this Brief.

commodities. Coffee is the primary non-petroleum export and approximately 28% of households earn some income from coffee. Coastal fisheries are extremely rich but lie in a narrow patch of reef and are therefore particularly vulnerable to over-exploitation. Offshore resources include tuna, deep sea snappers, and deep sea shrimp, but the size and status of these resources is largely unknown.

Jobs can be created in the agricultural sector, particularly through private sector investment and export market development. The new Agribusiness Directorate in the Ministry of Agriculture and Fisheries (MAF) is focusing on removing constraints to agribusiness development. However, this is not sufficient to cover all the demand and will require actions in other sectors, such as improving rural infrastructure.

Agricultural productivity in Timor-Leste is low. Yields are low (some of the lowest in the region) with maize yields averaging about 1.4 MT/ha and paddy rice yields averaging about 1.5 MT/ha. Access to and adoption of quality inputs and technologies are limited. Further, given the heavy dependence on subsistence agriculture, Timorese farmers are highly vulnerable to food shortages. 70-80% of villages report food shortages between December and January. This vulnerability could begin to be addressed by investments leading to diversification in farmers' off farm income, promoting early warning systems to warn farmers in drought years, safety nets for the most vulnerable, investing in irrigation systems which can be easily maintained, and promoting plant varieties resistant to extreme weather events.

A major problem in the sector is the weak management of natural resources and increasing environmental degradation. The challenge is to integrate environmental concerns into agricultural growth strategies. Priority interventions in the natural resource sector include preservation of the genetic stock of sandalwood, co-management of forest plantations, natural forests and coastal areas with local communities, and improving the management of offshore resources. This can be achieved by leveraging on and improving traditional law and communal systems. Co-management with communities is feasible through by-laws or memorandum of understanding with the Government. Managing offshore resources remains a concern given the high potential for corruption and unscrupulous exploitation.

MAF faces a fundamental challenge in helping farmers adjust to markets that are very different from pre-1999, while dealing with reduced support from the state and a smaller public administration. MAF has concentrated resources and efforts on strengthening institutional capacity in service delivery. One major challenge is the low capacity and availability of educated labor. To address some of the specific problems, Government will need to establish an efficient agriculture knowledge and information system. It will also be necessary to formulate policies and programs that address productivity and agriculture health, and promote the development of new markets through strengthening product supply chains. Priority areas in the short-term are (a) professional (post-graduate) training for senior staff in areas such as irrigation engineering, agriculture economics, and animal health; (b) organizational restructuring to further integrate MAF's services; and (c) developing partnerships with NGOs and the private sector for agriculture service delivery.

Timor-Leste's National Development Plan aims at having sustainable, competitive and prosperous agricultural, forestry and fisheries industries that support improved living standards by 2020. Five strategic priorities have been formulated under the plan: (a) improve food security and raise self-reliance; (b) increase value-added production and marketing; (c) achieve sustainable production and management of natural resources; (d) strengthen the balance of trade by promoting commodity exports; and (e) increase income and employment in rural areas. There are Sector Investment Programs (SIP) for “Agriculture and Livestock”, “Forestry”, and “Fisheries”. These are in the process of being revised.

Facts and Figures

Key figures for sector

Rural population (% of total population)	2005	73.5
Rural population growth (annual %)	2005	4.8
Agriculture, value added (% of GDP)	2004	31.6
Agriculture, value added (annual % growth)	2004	10.1
Cereal yield (kg per hectare)	2005	1,926.2
Improved water source, rural (% of rural population with access)	2004	56.0
Food production index (1999-2001 = 100)	--	113.0
Arable land (% of land area)	--	8.2
Permanent cropland (% of land area)	--	4.6

Source: World Bank (2005)

Production and value of major agricultural commodities, including percentage of households growing crops

Commodity	Value (\$1,000)	Production (MT)	Households Growing crop (%)
Rice, Paddy	13,938	65,433	26 ²
Coffee, Green	11,446	14,000	28 ³
Indigenous Pig-meat	10,208	10,080	--
Maize	8,154	70,175	81
Roots and Tubers	5,149	43,000	--
Vegetables Fresh	3,002	16,000	--
Cassava	2,992	41,525	68
Sweet Potatoes	2,613	26,000	44

Source: FAO (2005) for production data; Timor Lorasae Household Survey (2002) for percentage of household growing crops

² All ecosystems (not limited to paddy).

³ Includes cherries and dry beans.

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2. Sector Note: Communication

Overview

Timorese communities are inadequately served by the media, telecommunications, and Government information efforts, leading to insufficient access to information. Channels of communication among state institutions, between Government and civil society, and Government and the public remain underdeveloped. Ineffective communication between Government and the public has been identified as contributing to the crisis of 2006, while limiting the ability of state institutions to address the crisis. Systematic dissemination of information by Government to the public is central to effective implementation of Government programs, accountability, and countering rumor and misinformation. It is also a fundamental human right. Currently most state agencies have insufficiently developed skills, mechanisms, and systems for regularly sharing information internally or with the public.

Key Issues

- ***Establishing state agencies as sources of regular information.*** In the short-term this could include the appointment of trained spokespeople for Parliament, the office of the President, the office of the Prime Minister, judiciary, police, and army, moving toward the establishment of media units in each state agency. A culture of information sharing can be reflected in an information policy and protocols that encourage the sharing of information on Government plans, programs, and activities. This will promote better communication with civil society and the public and will improve engagement of all stakeholders in development process.
- ***Information flows within and between state agencies.*** Improving systematic flow of information within institutions is essential to providing information to the public. Within many agencies information is centralized, lacking systems for ensuring all staff are well-informed as to goals, programs, and activities. Establishing mechanisms, protocols, and skills, as well as a culture of openness among senior staff can lead to improved movement of information.
- ***Strengthening the legal framework for media.*** There are several areas in which the enabling legal framework for the media could be strengthened, including the RRTL legislation, broadcast licensing, and registration, which may be addressed through a single media law or a series of specific laws. Currently the draft penal code criminalizes defamation. Greater public discussion on this question may be useful, given the possibly chilling effect of the criminalization of defamation on Timor-Leste's nascent media.

The Sector

The sharing of information from state agencies with civil society and the public is unsystematic. State institutions lack designated spokespeople or mechanisms for keeping the public regularly updated. Improving information dissemination will depend on the development of communication skills, policies, mechanisms, and protocols, including adding communications responsibilities to the job descriptions of key staff. The work of the Government Information Office (GIO), a communications training unit under the office of the Prime Minister, provides a basis on which to build. Operating since 2004, the GIO trains ministry staff to interact with the media and the public. The GIO has already trained staff from 15 ministries and state institutions, however mechanisms to use these skills have not been systematically instituted across ministries. Other measures could include upgrading the Government website and improved access to the national gazette, *Journal da Republica*.

The national public broadcaster, Radio Televisaun Timor-Leste (RTTL), is the most important source of information in the country. Maintaining RTTL's independence and improving reach and quality is central to improving information flows. As of the end of 2006, weekly radio reach was 78% in Dili but much lower in the districts, at 28% in Viqueque.⁴ To help remedy this RTTL has recently introduced television coverage and new FM transmission equipment to seven district capitals, to be expanded shortly to another five districts. Additionally a new AM transmitter is being installed, which will ensure near 100% coverage across the country.

As a national public service broadcaster, RTTL is funded by the state budget but should remain independent. Only the state has sufficient resources to support a radio and television station with national coverage. Community radio stations play a role in providing local news and local language programming but have limited capacity to provide national news. RTTL is currently governed by law 2002/6 On the Establishment of the Public Broadcasting Service of East Timor, amended in 2004. The current law could be strengthened through greater clarity regarding the broadcaster's relationship to Government with more safeguards to its independence.

There are gaps in the regulatory framework for the media. There is no body to license or regulate radio and TV stations, including criteria for establishment, governance structure, or the assignment and management of frequencies. Accountability for media professionals can be greatly strengthened using various regulatory options with enforcement of sanctions. This could be handled by legislation or through self-regulation by a professional body, such as a press council. Self-regulation through a press council may be the most practical solution for Timor-Leste. This can be backed up with civil lawsuits rather than criminalization. In the process of drafting the media law or laws, consultation with the media, civil society, and public will be essential.

Expanding the reach of media and Government public information to rural areas will require creativity. For example, use can be made of the TVs and DVD players placed in each suco as part of the Ministry of Education's literacy program. The Government could also

⁴ Foundation Hirondelle, *Timor-Leste National Media Survey, Final Report*. May 2007

examine the possibility of subsidizing daily newspaper distribution to all schools, hospitals, and Government offices.

Facts and Figures

Journalist Associations: Associaaun Journalista Timor-Lorosa’e, Sindicato, Associaaun Radio Komunitade Timor-Leste, Press Club

Daily Newspapers: Timor Post, Suara Timor-Lorosa’e, Diario Nacional

Weekly Newspapers: Tempo Semanal, Journal Labarik, Seminario Nacional, Lifau Post

Radio Stations - Dili Community Radio Stations (6): Radio Lourico Lian, Radio Rakambia, Radio Klibur, Radio Falintil, Radio Voz, Radio Atauro; **District Community Radio Stations (13):** RC Povo Viqueque, RC Lifau Atoni, RC Café Ermera, RC Baucau, RC Covalima (off air as of June 2007), RC Ainaro, RC Aileu, RC Maliana, RC Los Palos, RC Manatuto, RC Ainaro, RC Bobonaro, Radio Liquica; **Church Stations (2):** Radio Timor Kmanek, Baucau

Table 1 - Most Important Source of Information

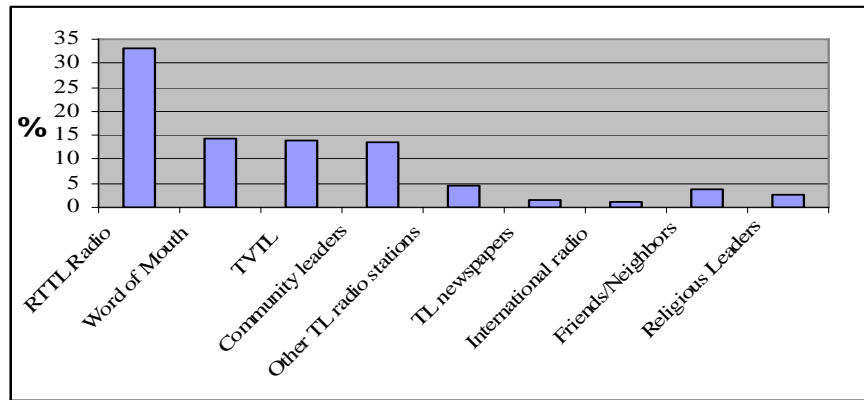


Table 2 – Leading Radio Stations

Station	Weekly Reach	Spontaneous Awareness
RTTL	35%	58.7%
Radio Timor Kmanek	16%	27.2%
Radio Rakambia	8.9%	14.4%
Radio Falintil	5.5%	9.6%
Radio Povo Viqueque	6.5%	3.1%
Radio Klibur	4%	4.7%
Radio Australia	3.6%	5.4%
BBC	3.4%	3.8%
Radio Lorico Lian	3.3	3.6%
Radio Baucau	2.4	5.2%

Source: Foundation Hironnelle, *Timor-Leste National Media Survey, Final Report, May 2007.*

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3. Sector Note: Economy and Economic Growth

Overview

Since independence, Timor-Leste has made tremendous progress in creating the institutions of the state essential for running the economy. However, economic performance in terms of growth, employment generation, and poverty reduction has been disappointing. With limited immediate prospects for private investment, Government spending is the main source of economic growth in the short-term. With petroleum revenue increasing, the state is no longer as constrained as previously in public investment and spending. Limited capacity, however, remains the key constraint to the execution of planned investments and productive spending of resources. Measures to enhance execution capacity together with efforts to develop a social safety net will be important in the short term for bolstering economic growth and providing support to the vulnerable. To promote growth over the medium term, steps to improve conditions for private investment and entrepreneurship will be necessary.

Key issues

- ***Growth in petroleum income.*** Timor-Leste now has large budgetary and external surpluses and faster-than-anticipated accumulation of savings in the petroleum fund. This provides an important resource base to develop the economy and reduce poverty. The growth of petroleum revenue has meant that “sustainable” budget spending - spending that can continue in perpetuity - is presently estimated at over \$300 million per year. This figure will likely grow once resources from the Timorese share of the Greater Sunrise field come on stream, but may vary according to world energy prices.
- ***Economic outcomes over the past five years have been weak.*** The non-oil economy has stagnated and unemployment and poverty are high and rising. Virtually all Timorese earn their livelihood in the non-petroleum sectors of the economy. However, per capita income in the non-oil economy is stagnant in real terms since 2002. At the same time, national income per person, including the oil sector, has doubled due to increased revenue from petroleum (Table 1). About 40% of the population was estimated to be poor in 2001, and has likely increased significantly, given the decline in real non-oil per capita incomes during 2001-2006.
- ***Minimal public or private investment has resulted in few new employment opportunities.*** In 2005, overall unemployment in Dili was estimated at 27%, while youth (ages 15-24) unemployment was estimated at 40%. With about half the population under age 18, urban unemployment is destined to increase unless stronger economic growth can be sustained. According to a recent report by FAO/WFP, up to 220,000 Timorese will need food assistance during the lean months of October 2007 to March 2008.

The Sector

The primary mechanism to jump-start the economy in the short term will be increased Government spending. Under present circumstances of social fragility, private investment in the local economy (i.e. outside the offshore energy sector) cannot realistically be expected to lead the economy.

The Government will thus need to substantially improve its ability to execute spending priorities as reflected in its annual budgets. Past budgets have unfortunately been characterized by weak execution particularly for capital spending. For example, by the end of the third quarter of FY2006-07, less than 3% of capital expenditure on a commitment basis was actually disbursed, frustrating legitimate development objectives. Stronger budget execution would allow infrastructure development and reconstruction to progress as intended, and thus provide the basis for raising incomes through job creation. Specific recommendations have been provided by international agencies on expediting budget execution.⁵ Of particular importance is delegating specific responsibility, particularly in the case of procurement, both across and within ministries in line with available capacity in order to unblock bottlenecks. Efforts to strengthen capacity by filling vacant managerial and advisory positions with local or expatriate staff must also be pursued. Making provisions for greater access to and utilization of financial management software by line ministries and utilizing externally-funded Project Management Offices to boost local capacity in the short run are additional critical steps. International outsourcing of large infrastructure projects should also be considered, and foreign expertise should be used as a means to increase investment and job creation.

There is an urgent need to develop a social safety net to provide immediate support to the poor and vulnerable segments of the population. In the short term, the following programs are worth considering: (i) a public works program to offer low-wage employment to those amongst the poor who can work; (ii) a transfer program for the disabled; (iii) a school feeding or conditional cash transfer program that can improve enrolment and retention rates for school-age children; and (iv) a modest universal cash transfer program to share a fraction of the gains from rising petroleum revenue with the population. These programs can not only yield immediate gains in terms of poverty reduction, but can also contribute directly to increasing labor absorption in the economy, enhancing household food security, and building human capital that will be much needed for future growth.

In the medium term, Timor-Leste's economy can only prosper if the conditions for private investment and entrepreneurship become more favorable. In this respect, an improved business environment also needs to be pursued. In light of the comfortable fiscal position and prospects, reducing and simplifying import tariffs and income taxes for the non-oil economy (but not user and utility charges) may be warranted as part of an overall effort to improve the attractiveness of Timor-Leste as a destination for private investment. This would also be preferable to elaborate tax incentives or preferences, which are complex to implement, particularly given capacity constraints.

⁵ See, for example, World Bank Aide Mémoire of July 26, 2006.

Facts and Figures

Table 1. Timor-Leste: Key Economic Indicators

	2002	2003	2004	2005	2006 e/
Output and Prices					
GDP (non-oil) real growth rate, %	-6.7	-6.2	0.3	2.3	-1.6
Inflation, % change	9.5	4.2	1.8	0.9	5.7
GNI, at current prices, \$ million	352	349	507	692	847
Non-oil GDP	343	336	339	350	356
Oil and gas income	9	13	168	342	492
Population, thousands	892	922	952	983	1015
Non-oil GDP per Capita, \$	385	364	356	356	351
GNI per Capita, \$	395	378	532	704	835
External Sector, \$ million					
Merchandise Exports	6	8	8	9	8
Merchandise Imports	218	194	163	137	141
Trade Balance	-211	-186	-154	-127	-133
Services, net	-44	-37	-32	-27	-33
Foreign Income, net	4	4	43	83	117
o/w: Oil and gas royalty and interest	2	2	39	79	115
Current Transfers, net	123	134	246	363	460
o/w: Oil and gas tax revenue	7	11	129	264	377
o/w: International assistance	116	123	118	100	82
Current Account Balance	-128	-85	103	292	411
Capital and Financial Account	148	103	18	49	71
o/w: Official capital transfers	59	44	41	41	44
Overall Balance	20	18	121	341	482
Fiscal Operations (Central Government Budget, cash basis, fiscal year (July-June)), \$ million					
	FY02-03	FY03-04	FY04-05	FY05-06 p/	FY06-07 Q1-Q3
Total Revenue, inc. grants	81.3	105.4	336.7	485.0	702.1
Oil and gas revenue	30.9	40.3	261.0	448.0	674.3
Domestic revenue	19.3	29.2	36.9	33.4	27.8
Expenditure	68.5	68.4	71.4	93.0	80.8
Current expenditure	53.3	53.1	56.4	66.3	75.2
Capital expenditure 1/	4.7	2.4	2.8	15.7	5.6
Overall Fiscal Balance	12.8	37.0	265.3	392.1	621.3
Memo: Cumulative Oil and Gas Savings	10.5	13.9	70.1	649.8	1,218.0

e = estimate, p = preliminary;

1/ \$10.5 million of the \$15.7 million capital expenditure for FY2005-06 was for the capitalization of the BPA

Sources: Timor-Leste authorities, IMF, and World Bank

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4. Sector Note: Education

Overview

There has been some progress in education since independence. The increase in total number of children enrolled in school is offset by the need to accommodate a rapidly rising school age population, poorly prepared teachers, insufficient or poor physical infrastructure, weak budget execution, and lack of access to textbooks and other teaching and learning materials. Drop out and repetition rates are high - only 46% of children starting primary school reach grade 6, 80% children starting lower secondary education reach grade 9. The Ministry of Education is implementing a Strategic Plan for Universal Primary Completion that is designed to create the opportunity, by 2015, for every child in Timor-Leste to complete a quality primary education. MoE has yet to outline a strategy for secondary and tertiary education.

Key Issues

- ***Establishing a strong teaching force:*** A first step would be the articulation of a teacher training strategy that illustrates how the Government will establish, maintain and train capable teachers. Concrete actions required are: (i) a determination of need (numbers by level/by location) over medium to long term; (ii) establish training pre- and in-service programs and develop locations for training; (iii) approve teaching competency framework; and (iv) incentive program to support teacher placement and continual professional development/career paths.
- ***Increasing the current procurement threshold to \$250,000:*** Currently, the MoE has the authority to internally process contracts up to US\$100,000, but this is now insufficient given that most school building contracts are higher. Raising the threshold to \$250,000 will help the MoE to stay on track with the planned construction/rehabilitation of 120 schools in 2007/08. This is critical as 83% of classrooms need rehabilitation or replacement.
- ***Improving the way in which official languages are taught to teachers and in schools:*** Assessing how Portuguese and Tetum are currently being taught, with support of mother tongue, in schools will be an important first step to achieve the stated goal of all children to be fluent in Portuguese and Tetum at the end of grade 6. A strategy for effective teaching of the two official languages will need to take into account that around 60% of the children do not speak either of these two languages in their communities.
- ***Access to high quality textbooks:*** Most schools do not have textbooks and other instructional materials. In support of this objective, MoE should establish effective and transparent procedures to develop, select, procure, and distribute books, and other teaching learning materials.
- ***Continuing and improving the School Grants Scheme:*** The program started in end 2006. So far about US\$900,000 have been disbursed to schools. There is evidence that the MoE program design needs to be strengthened, that program safeguards, program monitoring, and the assessment of schools' needs can all be improved.

The Sector

With one of the highest fertility rates in the world, Timorese society is very young with about 50% of the population under 15. This will put pressure on the Government to constantly increase the number of classrooms, books, and teachers for the increased number of children entering school every year.

Teacher competency is the most important input to schools. If education quality is to increase substantially, it is essential that the MoE strengthens pre-service and in-service teacher training and enforces standards for its delivery, oversight, and impact assessment. A teacher competency framework, which describes the minimum standards required of a teacher in Timor-Leste, has been developed. It is intended to serve as a tool for the MoE to ensure that all teacher-training provided is of an adequate standard and is appropriately designed and delivered.

No school in Timor-Leste has adequate learning materials. The only material all primary and pre-secondary students receive currently is the *Lafaek* magazine. *Lafaek* is produced and distributed by CARE. The MoE finances the magazine and has overall editorial control. Additionally, teaching learning materials designed in Timor Leste for grade 1 were distributed in 2006/07 to support the new primary curriculum. Materials for other grades will follow over the coming years as the new primary curriculum is rolled out. More materials – both textbooks and teaching learning materials - are needed. The ministry needs to establish selection criteria and transparent procurement processes that will ensure both quality and cost-effectiveness. The ministry also needs to build capacity for the development of materials as well as the assessment and selection of external resources. It is also important that textbooks reflect the new curriculum which has not always been the case.

Less than 50% of school children speak Tetum as their mother tongue. Far less speak Portuguese when they start school. Children may be facing both linguistic and conceptual problems in the classroom, as they attempt to transition from their mother tongue to either Tetum and/or Portuguese in the early grades. They may not learn to read and write properly in any of the languages and are more likely to drop-out of school. Research shows that basic literacy and numeracy skills are learned best when taught in the mother tongue and that a additional language is learned best when children begin the learning process in their mother tongue. Research also shows that additional language(s) are learnt best when teaching practices build on the knowledge that these languages are not mother tongue languages. In order to promote a quality education system, it is crucial to assess how the Tetum and Portuguese are taught in schools and it is also fundamental that the Ministry of Education and all the Development Partners work closely on the urgent development of a planned and continuous training of teachers that would enable them to acquire specific competencies on both official languages.

Student achievement is low. As an example, survey in 2006 found that 80% of grade 3 students failed to meet a minimum level of learning in mathematics. It is most likely that the low quality of education is a major contributor to the high repetition and drop out rates. There is a need for a comprehensive, standardized assessment system to determine system and individual performance.

In late 2006, MoEC started a nationwide school grants program to substitute the “caixa escolar”. Funds are disbursed to schools through district directors. Schools spend these grants

according to their own needs (e.g., minor repairs), although many school principles are unclear for what purposes they are allowed to spend the grant. School grants are a good vehicle to transfer funds to the school level, to involve parents and consequently could contribute to better schooling. Parent Teacher Associations (PTAs) are laying a foundation for involving communities in the education process. Involving communities in schools, for example in monitoring school grants, is very important as a means of social mobilization, participation, and enhancing the accountability of schools to parents.

Although there are about 16 institutions providing tertiary education, there is no accreditation or quality control system. This lack of regulation means that the quality of all institutions is unknown. In response to this situation the MoE has begun developing quality assurance arrangements for the tertiary education section and drafting regulations and statutes regulating standards and cooperation in higher education.

Facts and Figures

School Year	2003/04	2004/05	2005/06
Primary			
Schools ¹	744	761	762
Students	169,958	169,341	151,393
Teachers	4,862	5,415	5,087
Student-Teacher Ratio	36	33	37
Gross enrollment	101	98	87
Net enrollment	77	77	69 ²
Repetition rate (%)		11	16
Drop-out rate (%)		12	25
Junior Secondary			
Schools	120	129	135
Students	40,368	41,516	44,651
Teachers	1,135	1,652	1,289
Student-Teacher Ratio	36	25	35
Gross enrollment	59	59	62
Net enrollment	33	31	32
Senior Secondary			
Schools	55	76	65
Students	20,23	24,493	26,433
Teachers	670	725	585
Student-Teacher Ratio	31	34	45
Gross enrollment	36	40	41
Net enrollment	21	34	33

Note: ¹ While the increase in the number of schools is relatively small these figures mask both the substantial increase in the number of useable classrooms that has taken place over the last five years and the fact that a large number of schools has been fully rehabilitated.

² Note that enrollment in 2005 was substantially lower than in the two previous years. This is almost certainly an aberration due to extensive, wide spread civil conflict in 2005/06 and should not be seen as evidence of a downward trend. This has also had the effect of reducing the GER and NER indicators for 2005. When the IDP student data for 2006/07 are entered and processed the enrollment levels for 2005/06 can be adjusted and the accuracy of the time series preserved. Notwithstanding that adjustment, in 2003/04 and 2004/05 total enrollment actually fell although the size of the primary school age cohort grew by more than 2% over that period. Unless the rate of growth of enrollments exceeds the rate of growth of the school age population access and participation indicators will not improve.

Measurement of Learning Achievement:**Percentage of Students Failing to demonstrate a Minimum Level of Learning**

Grade	Subject	Percentage
3	Tetum	86%
3	Portuguese	96%
3	Mathematics	79%
5	Tetum	83%
5	Portuguese	90%
5	Mathematics	76%

A minimum level of learning was defined as demonstrated acquisition of 50% of the curriculum, where that 50% is comprised of those skills found to be the most easily acquired.

Tertiary Enrollments in Timor-Leste

	2005/06	2006/07
1. Universidade Timor-Lerosa'e	10,461	10,467
2. Universidade Dili	1,414	450
3. UNPAZ (Dili)	1,476	1,591
4. Universitas Oriental (UNITAL Dili)	550	858
5. Universidade Mau Lear (UNMA, Dili)	388	340
6. Universidade Comunidade Matebian (UCM, Baucau)	175	176
7. Universidade Dom Matinho Lopes (UNIMAR, Dili)	191	360
8. Universidade Jupiter (UNTER, Dili)	150	N/A
9. Boa Venura Agriculture University (Same)	112	N/A
10. Dili Institute of Technology (DIT, Dili and Oecussi)	493	205
11. Escola Catolica de Formacao de Professores de Baucau	153	150
12. Intituto Superior de Formacao de Professores e Ciecncias	435	
13. ISUFPROCED Aileu - Teachers Training Branch	72	N/A
14. ISUFPROCED Los Palos-Teachers Training Branch	45	N/A
15. Intituto de Ciencias Religiosas (ICR, Dili)	135	150
16. Profissional de Canossa (INTEC, Dili)	113	148
17. The Institute of Business (IoB, Dili West)	222	150
18. East Timor Coffee Academy (ETICA, Gleno)	150	207
19. Akademi Computer Manajemen Sistem (CLICK, Dili)	374	110
20. Academy for International Relations (Instituto Superior de Ciencias-Politica e Letras, Dili)	180	NA

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5. Sector Note: Environment and Natural Resources

Overview

Low income countries are typically characterized by very low wealth per capita and by a very high share of such wealth in the form of natural resources. As such, Timor-Leste heavily relies on natural capital – namely subsoil resources, agricultural land and forests – for its livelihood. Petroleum reserves account for the most important share of Timor-Leste’s natural wealth. But land wealth is also important with 73.5% of the population living in rural areas, where agriculture accounts for 95% of the product. Most of what the rural poor have is provided by nature (e.g. fuelwood, non-timber forest products, crops), rather than in the form of produced assets (e.g. buildings and infrastructure). Deforestation and land degradation driven mainly by slash and burn agriculture and fuel wood extraction threatens the country’s natural wealth and source of livelihoods. Land degradation in its several forms is likely to affect water (via erosion affecting water bodies), biodiversity (via land habitat loss, coral reef, and coastal fisheries degradation), and soil (via soil loss). In addition, other forms of natural resources such as deep sea fisheries may be subject to overexploitation. Part of Timor-Leste’s investment in the future can be improving Timor-Leste’s environmental institutions and legal framework, which are underdeveloped. The country lacks the capacity to face environmental challenges and thus sustainably use its natural wealth.

Key Issues

- ***Arresting deforestation and land degradation.*** Timor-Leste has one of the highest rates of deforestation in the region and is losing forest area at an unprecedented pace. 53.7% of Timor-Leste’s land is forested, but the rate of deforestation is approximately 1.2% a year.
- ***Investing in environmental and natural resource programs.*** Timor-Leste has a unique opportunity to transform exhaustible natural capital into other forms of capital that can be sustainably exploited for the development of the country. For this to occur, it is important to invest in environmental and natural resource programs to arrest environmental degradation. Such programs can be labor-intensive and target rural areas, including, for example, reforestation with native species, eradication of the siam weed, and controlling erosion. Taking into account conservation and long term sustainability in planning and building infrastructure is also critical.
- ***Creating an appropriate environmental legal and institutional framework.*** Most promulgated and draft regulations are based on laws from other countries. These have adopted without a critical analysis of whether they are appropriate to conditions in Timor-Leste. This results in overly burdensome regulations in some areas like the proposed environmental impact assessment law, which entails excessively complex processes. In other areas there are important gaps, such as forestry, water, land, a national environmental law among others.

The Sector

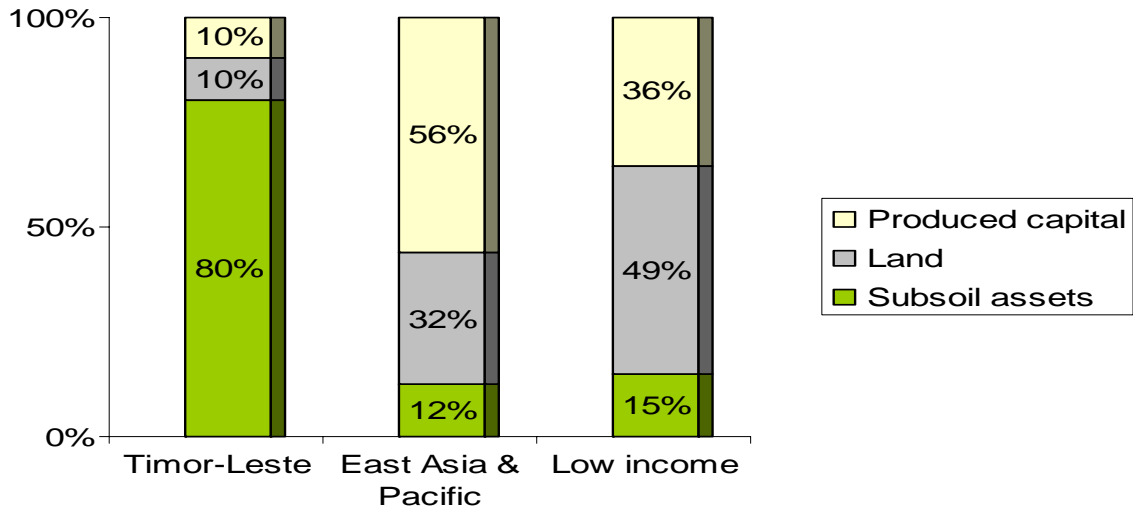
Much more needs to be known about the state of the environment in Timor-Leste, including the causes of forest depletion and environmental degradation. Fuelwood extraction appears unlikely to be the main cause of forest depletion. Demand for fuel wood by households and commercial activities is below the natural growth of accessible forests. Conversion of forest to agriculture is more likely to be a major driver of deforestation. 76% of labor force in Timor-Leste is dedicated to subsistence farming. Assuming there is no growth in productivity and a population growth in rural areas of nearly 5%, agricultural land expansion so as to maintain a constant rural density could be taking place at a rate of about 15,000 hectares per year. If expansion takes place in forested areas, this would represent a decline in forest area of about 1.8% per year. This conversion of forest to agricultural land will not be sustainable.

While precise social causes are still to be determined, it is likely that environmental degradation with ill-defined property rights over natural resources may provide an incentive to degrade the environment. At least two factors relating to land ownership seem to drive forest land clearing in different parts of the country. Forests are not perceived by communities as a scarce resource and hence little communal control is exercised over their use. Alternatively property rights over forest land may not be as clearly defined as for agricultural land, and an open access regime may dominate. For households the benefits from additional agricultural land may outweigh the benefits of abundant forest. The customary systems for administering land and resolving land tenure dispute may not be as well suited to ensuring that key ecosystems are conserved in the face of population pressure. While the constitution recognizes state ownership over forest resources, these have been traditionally considered a communal resource available for the community's needs. In the absence of enforcement, this creates *de facto* an incentive to convert forest land into agricultural land thus securing the exclusive right of using the land.

Environmental conservation and regulation is by its nature multi-sectoral. To date, in Timor-Leste, natural resources and environmental responsibilities was shared across the former Ministry of Natural Resources, Minerals and Energy Policy, the former Ministry of Agriculture, Forest and Fisheries, and the former Secretary of State for Environment Coordination, Territorial Ordinance, and Physical Development. The shared responsibilities reflect the cross-sectoral nature of the issue, but also generate some confusion and overlap. It is important to maintain a separation between the regulatory functions from the standard sectoral functions to avoid conflict of interest. Equally, it is important that these functions receive similar weights. Previously, several environmental regulatory functions were under the Secretary of Environment, who did not have the same status as Ministries in the Council of Ministers. It is critical to give the same level of importance to environmental regulatory functions as the sectoral ministries that these are supposed to regulate.

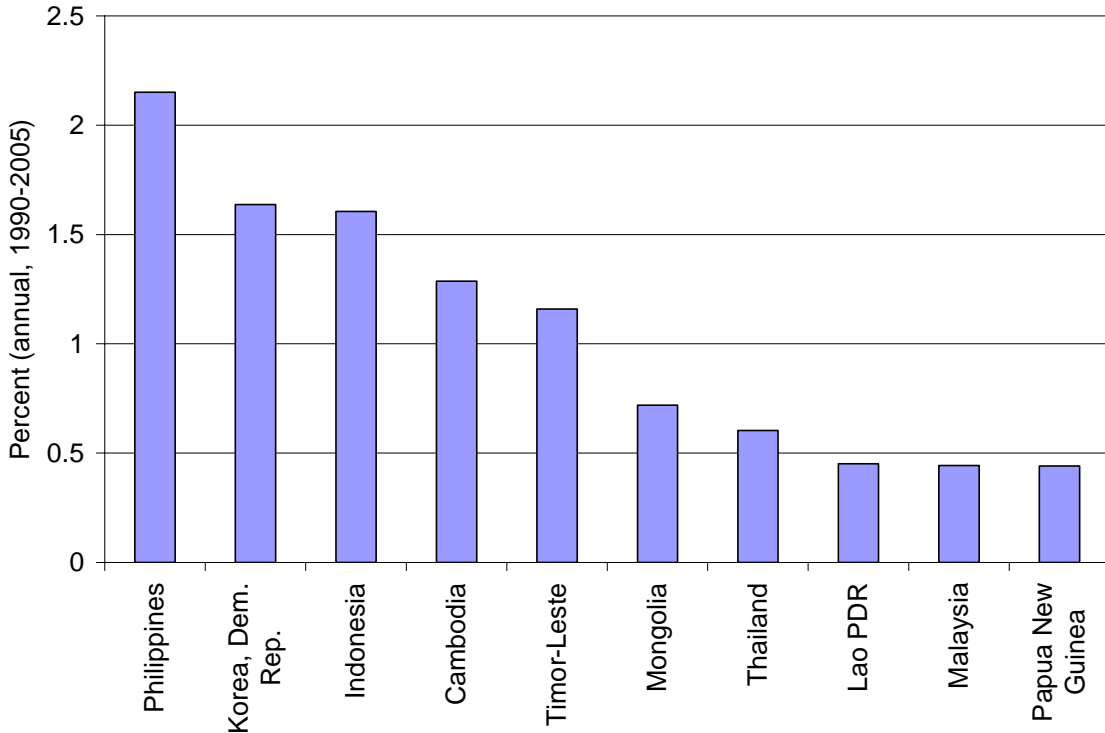
Facts and Figures

Tangible wealth in Timor-Leste



Source: World Bank staff estimates (draft)

Top-ten deforestation rates in East Asia and Pacific



Source: World Development Indicators

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6. Sector Note: External Oversight and Internal Control

Overview

Timor-Leste has established key institutions and mechanisms of external oversight and internal control. These can ensure that national resources and state power are used appropriately, but more work is needed to make them fully effective. It is critical to strengthen parliamentary oversight, consolidate the role of independent bodies, and clearly signal Government commitment to economic governance. Important steps could include the formation of asset and income registers, movement towards the transition of external audit to Court of Appeals management, and the creation of internal audit offices in line ministries supported and coordinated by the Office of the Inspector General. Effective action in cases of corruption, maladministration, and abuse of power is central to public confidence in the state.

Key Issues

- ***Strengthening the role of Parliament.*** Parliament could strengthen its oversight of Government through scrutiny of Government accounts and audits, and monitoring budget execution. Open parliamentary committee and plenary discussions can provide a forum to follow up on results with ministries. Monitoring adherence to petroleum revenue management arrangements, including tracking of withdrawals from the Petroleum Fund, should also be a priority for Parliament.
- ***Empowering the Office of the Provedor.*** Amending the organic law of the Office of the Provedor (PDHJ) to remove excessive restrictions on the use of material gathered during investigations as evidence in criminal prosecutions (section 47 of the PDHJ Law refers) would make the PDHJ more effective. The operational effectiveness of the Office would also benefit from allowing it to have a higher degree of financial independence.
- ***Creating an income and asset register.*** Mechanisms to receive, monitor and store asset declarations from senior Government officials, procurement and Customs officers, members of the Investment Advisory Board for Petroleum Fund Investments, and Consultative Council members would improve the management of conflicts of interest and deter corruption.
- ***Approving the organic law for the OIG.*** A draft is pending in the Council of Ministers. Approval is required to enable the OIG to conduct independent investigations, audits and inspections, and to create inspections capability in the ministries and district administrations.

The Sector

Oversight mechanisms can provide a vital check and balance on executive action. The Parliament, Presidency, Provedor, Judiciary, and independent media are some of the oversight mechanisms in

Timor-Leste, each of which is in a different stage of development. Internal controls, such as the Office of the Inspector General and internal audit offices, are designed to detect wrongdoing and promote best practices in governmental operations.

Parliament has rarely asserted its constitutional role of scrutinizing draft laws, Government policies or Government actions. As a result it has been widely perceived as an extension of executive power. To strengthen its role in oversight, Parliament could regularly invite ministers to deliver briefings on programs and progress in service delivery. Rigorous scrutiny of the state budget would also be helpful. It could also engage directly in dialogue with the Consultative Council, which is mandated to advise parliament on questions related to the Petroleum Fund. The Council aims to report to the public each quarter on petroleum fund management and to conduct annual public consultations on public expenditure priorities with a view to report back to parliament with specific recommendations (section 30, Petroleum Fund Act 2005).

Opened in March 2006, the PDHJ is mandated by the constitution to fight corruption, promote good governance, rule of law and human rights, and to redress violations and injustice. The office has an important responsibility to address unfair or poorly-judged state actions and does so through monitoring, investigation, and public outreach. Currently with a staff of 46, the challenge ahead is to expedite the processing of complaints and finalize reports on investigations (of 123 complaints reviewed only one report is concluded). The formation of collaborative partnerships with the Office of the Inspector General, police, and Office of the Prosecutor General for complaints investigation and prosecution will also be important. Operations are also hindered by the absence of financial independence that would enable the office to run its daily business more effectively.

Complaints submitted to PDHJ - July 2007

	Complaints	Action taken	Pending
Maladministration	64	Seven referred to PNTL for further investigation One resulted in formal recommendation to MoE	56
Human Rights	41	Six referred to PNTL for further investigation	35
Corruption	18	One case referred to PDHJ by MSA referred to PG for prosecution	17
	123		108

Note: Eight cases were initiated on the basis of the PDHJ's legal power to initiate investigations, (article 35 of the PDHJ Law). They included one human rights case; two maladministration cases; three anti-corruption cases; two combined maladministration/anti-corruption cases.

Diagnostic tools could be employed to identify existing levels of corruption, vulnerable public offices, and agencies in which public trust is low. An external audit of procurement procedures might be particularly useful. The “Doing Business” Survey (2006) showed that corruption is damaging the business environment, deterring investment and jobs, and undermining public confidence. But there are no up-to-date thorough data on existing levels of corruption in Timor-Leste. Weak supervisory mechanisms, lack of a professional civil service ethic, and difficulty in recognizing and dealing with conflicts of interest provide an environment in which corruption can

flourish. Previous attempts to tackle corruption include a series of transparency, accountability, and ‘integrity in the state’ workshops, and reshuffle of some Cabinet posts. Codes of ethics, linked to the Civil Service Law, improved information flow, and open dialogue within Government and with civil society would contribute to strengthen integrity inside the administration. Leadership training can help high level officials to model integrity, which may be more influential than rules and regulations.

Inadequate internal and external audit and weak fiscal accountability mechanisms reduce the ability of Government to oversee public spending and protect against corruption. External audits were contracted by the former Ministry of Planning and Finance (MoPF) to an accounting firm. The Government audit of the FY05/06 state annual accounts is completed and the FY2006/2007 audit should be tabled in Parliament before year end. The Petroleum Fund Audit was also recently published, though several months after completion. The High Tax and Audit Court, responsible for external audit does not yet exist, the capacity to create it will not exist for several years to come. The Court of Appeals cannot serve this function in the short-term. Movement towards the arrangements laid down in the constitution could include the formation of a judicial Audit Committee to oversee the Ministry of Finance (MoF) management of the contract. A transition study to outline appropriate steps towards eventual judicial adoption of this function might be helpful. For example services could be provided to assist the Court of Appeals to manage the contract for the audit firm and interpret audit results. Mechanisms must also be created to receive, cross reference and store asset and income declarations to increase transparency and manage conflicts of interest, deter illicit conflicts, and ensure compliance with the law. Development of mechanisms and guidance for managers and staff on what to do in a situation of conflict of interest would also be important. Asset and income registers alone are not enough.

The primary internal audit office for the Government, the Office of the Inspector General is charged to carry out investigations and inspections. Inspections ensure that public administration is conducted in accordance with established rules and regulations, while investigations are conducted to examine alleged wrongdoing. Since its establishment in 2000, the OIG has completed 96 audits (16), inspections (3) and investigations (78) and has posted case summaries on its website. Ten cases have been referred to the Prosecutor General for criminal prosecution though none have been prosecuted. The organic law for the OIG has not been passed by the Council of Ministers. This has delayed plans to set up and train internal audit offices in key line ministries. Internal audit offices were established in the MoPF, MoH, MoI, and MSA. Risk based assessments of line ministries also cannot begin until the office is empowered by its Organic Law to do so. The Office has placed considerable emphasis on public engagement through media releases, district visits and inspections designed to raise community awareness of the existence and functions of the OIG and to strengthen the internal audit capacities of local administrations. Publication of OIG case summaries has been an effective in reaching the public.

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7. Sector Note: Gender

Overview

No country can reach its full potential if half of its population, women and girls, do not benefit equally with men and boys from goods and services offered by its government and society in general. Female education is one of the indicators which correlates most closely with overall development and economic growth. Equal rights of the sexes are enshrined in Timor-Leste's constitution and reflected in its National Development Plan. It has ratified CEDAW⁶ and its Optional Protocol. Since independence the Government of Timor Leste has undertaken major steps to promote gender equality, significantly through the former Office of Promotion of Equality (OPE) under the Prime Minister's Office.

Key Issues

- ***Approving legislation against domestic violence.*** The draft law on domestic violence remains an outstanding priority. Domestic and gender-based violence are major issues, accounting for more than 50% of criminal cases reported to the police.
- ***Involving women in peace building.*** Despite women being among the most affected by the many years of conflict in Timor-Leste, they have been sidelined in formal decision-making processes and reconciliation efforts. For example, there were few efforts to engage women as mediators in the early stages of the 2006 crisis. Consideration could be given to creating a special commission in which women are involved from the outset in the design and implementation of peace building initiatives.

The Sector

Major gender inequalities exist in Timor-Leste in many areas including health, education, employment, and political participation. Concrete efforts are needed to address these. Women make up only 23% of the public service, with only two women holding positions at the highest (L-7) level. In the health sector the main priorities are the reduction of fertility and maternal mortality rates, expansion of family planning programs to include men and boys, and addressing the gender dimensions of HIV/AIDS and STIs. In education priorities should be tackling the drop-out of girls. Only 29% of primary and secondary teachers are women. Developing a gender-sensitive secondary curriculum and increasing the number of female teachers in junior and senior secondary schools – including serving as role models – are additional priorities. Increased access to secondary and tertiary education as well as to non-formal education programs to increase literacy levels of both women and men is needed. Coupled with vocational training these efforts can promote economic empowerment

⁶ Convention on the Elimination of Discrimination Against Women

particularly in rural areas. Women's economic empowerment is critical, particularly in the agricultural sector, encompassing food security and agro-business.

During the re-constitution of the police force a critical issue is gender awareness training, including on gender-based violence and CEDAW. Key branches where gender training and tools are required are Community Policing, the Vulnerable Persons Unit (VPU) and the Criminal Police.

Drafted in 2004, the law against domestic violence has been actively promoted as a priority by OPE and gender advocates. To-date the draft has not been submitted to parliament. Harmonization with the new pending penal code has raised new issues. Gender advocates have recommended that Article 151 (sub-paragraph 2) of the penal code be removed to make the code consistent with article 26 of this draft law against domestic violence which specifies domestic violence as a public crime. As promulgation of the new penal code is still pending there is an opportunity to revise it. Once this law is passed, a comprehensive multi-sectoral plan of action needs to be put in place to disseminate, implement and enforce the new legislation.

OPE, located in the Prime Minister's Office, has received support from high levels of Government. But the office alone cannot ensure that gender issues are addressed across the whole of government. Much stronger high level support is needed to encourage line ministries to address gender within their sectors. OPE has not been an implementing agency but an advisory body that sensitizes, advocates, coordinates, monitors, and evaluates initiatives undertaken by the whole of government. To facilitate the gender mainstreaming process, OPE has appointed gender focal points (GFPs), at levels 5 and 6, in each ministry and agency and in the districts. However the GFP mechanism needs to be strengthened, through a clear formulation of terms of reference and regular coordination meetings. The involvement of central and district level planning focal points, already trained in gender analysis and gender sensitive planning, could enhance this reflective process.

During FY06/07 the gender mainstreaming process has been strengthened in the Ministry of Health, the Ministry of Education, and the Ministry of Agriculture and Fisheries with the appointment or planned appointment of sectoral gender advisors in coordination with OPE. The former Ministry of Labor and Community Reinsertion was the first to establish an operational gender unit and conduct a gender analysis within the ministry. Work is in progress with the sectors of trade and tourism. During FY 2006, OPE was assigned a permanent seat in each Sectoral Working Groups of the Sector Investment Programs (SIP) to raise relevant gender issues in each sector and ensure the inclusion of gender responsive activities. So far it is unknown how successful their input has been.⁷ The promotion of gender equality is part of one of the SIPs: "Rights, Equality and the Justice Sector".

⁷ An illustration, in the SIP of Education and Training, none of the education data presented is disaggregated by sex, although gender equality is mentioned a few occasions.

Facts and Figures

Selected gender indicators across relevant sectors			Source
Total population: 923,198 Female-headed households: 19 % of all private households			Census 2004
<p>Women in National Parliament 2002-2007 - 26% Women elected 2007 - 27.7%) Women votes 2007 - 47%</p> <p>Labor force participation (aged 15+) – women 52% of women; men 69% of men Women make up 52% of the self-employed Women make up 25% of NGO, Government, and UN employees</p> <p>Fertility rate: 7.7 children per woman Infant mortality rate: 90 deaths for 1,000 live births Maternal Mortality: 660 per 100,000 live births Place of delivery: 90% of women delivered at home, 9% in the public sector health facility public and 1% in a facility of the private sector Use of contraception: 90% of married women in 2003 do not use any contraception Violence against women: In 2004 more than 68% of cases reported to PNTL on GBV (N=445) involving women and children concerned domestic violence.</p>			UNIFEM 2006 NEC 2007 NEC 2007 Census 2004 Census 2004 DHS 2003 Census 2004 DHS 2003 DHS 2003 HDR 2006 UNMISSET
Education	<i>female</i>	<i>male</i>	
Gross enrollment ratio (2005)	0.97	1.00	EMIS, MoEC 2005
Net enrollment ratio (2005)	0.75	0.81	
Gross enrolment rate lower secondary school (Rural) (%)	52	63	Census 2004
Population over 6 years (2004)			Census 2004
- attending secondary school for 6 or more years (%)	34	39	
- obtaining diploma	34	44	
Proportion of population 18-49 with some tertiary education (%) (2004)	4	8	Census 2004
Secondary school completion rates (2004) (%)	44	56	Census 2004
Tertiary education completion rates (2004) (%)	25	34	
National Public University students (2003-4) (%)	41	59	Census 2004
Public university staff (%)	27	73	MSA 2005
Private university staff (%)	12	88	
Participation in adult education literacy campaign by Div of Non-formal Education (N=5,310) (2003-4) %	30	70	ADB/UNIFEM CGA 2005
Literacy (2004) (40% for poor women)	52	65	Census 2004

NEC - National Electoral Commission, 2007
 DHS – Demographic and Health Survey, 2003
 HDR – Human Development Report, 2006
 EMIS – Education Management Information System
 CGA – Country Gender Assessment, 2005

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8. Sector Note: Health

Overview

Basic health infrastructure and services have been reestablished in Timor-Leste, but the population still suffers from poor health outcomes. Problems persist with inadequate quality and low utilization of health services, including vaccination, prenatal care, and assisted childbirth. The challenge facing the health sector is translating progress to date into better health services for the population, and to accelerate improvements in health and nutrition for the Timorese population. The Ministry of Health (MoH) has developed a new Health Sector Strategic Plan (HSSP) and a Medium Term Expenditure Framework (MTEF) for the health sector, which will replace the earlier Sector Investment Plan (SIP). These will need to be translated into annual action plans and budgets, with an increased focus on monitoring.

Key Issues

- ***Improving supply of essential drugs.*** One of the chief complaints of health care staff and community members is lack of availability of drugs. Strengthening oversight and monitoring the performance of the national drug procurement agency (SAMES) will help address delayed and erratic supply.
- ***Enhancing distribution and performance of health workers.*** Some areas have an insufficient number of health workers. Motivation and job performance could be improved overall. In the short-term, incentive schemes to encourage service in rural areas and to deliver better quality services could be tested. Such pilots could include improved housing, additional salary or benefits for staff in rural areas, or pilots to provide salary bonuses to staff based on performance in providing services.
- ***Piloting conditional cash transfers and other approaches to strengthen demand for health services.*** Low use of health services contributes to poor health and nutrition. The MoH plans to pilot a Family Health Promoter program. Additionally, conditional cash transfers, whereby cash payments are provided to poor families to promote healthy behaviors, such as vaccination of children or birth at health facilities, have been effective in other countries and could be tested in Timor-Leste.
- ***Addressing administrative blockages to service delivery.*** Shortages in the districts of essential supplies, such as fuel, have at times affected service delivery. Government may wish to consider further deconcentrating spending to the MoH, and from central MoH to health districts and hospitals. This includes for procurement and budgetary commitment authority.

The Sector

Child and maternal mortality, child malnutrition, and fertility indicators for Timor-Leste remain among the highest in the region. In 2003, the child mortality rate was 83 per 1,000 children, and nearly two-thirds of children under five were underweight. Malnutrition contributes to high mortality and low school achievement. Fertility rates are among the highest in the world, with women having an average of 7.7 children. High fertility and low rate of attendance by skilled health personnel during childbirth contributes to high maternal mortality rates, estimated at 660 per 100,000 births. Communicable diseases such as diarrhea, tuberculosis (TB), and malaria are prevalent.

The quality of health care is often inadequate, compounded among many families by low use of health services. Vaccination rates have improved, but only 18% of children were fully immunized in 2003, and only 18% of births were attended by skilled personnel. Low utilization is due to both inadequate coverage and quality of health services, as well as low “demand” by some for use of basic health services. Quality of health services is compromised by continued shortages of essential drugs, laboratory supplies, or fuel for field outreach services. Certain household behavioral practices contribute to poor health and nutrition outcomes, such as inappropriate weaning practices for infants or low use of impregnated bednets. While some nongovernmental organizations have local level community health or demand-generating activities, the scale of these activities could be broadened.

The number of health workers is approaching norms for the region, but Timor-Leste needs better distributed, trained, and supervised health personnel. The 300 doctors from Cuba have helped reduce shortages of medical personnel. But health workers are unevenly distributed and supervision could be strengthened. The Institute of Health Sciences (IHS) trains nurses but has limited capacity. A Health Workforce Plan lays out planning for the staffing of the sector but requires updating. While geographic coverage has improved, access remains difficult in some rural areas. In seeking to improve access, Government could consider a systematic strategy for coverage with mobile clinics.

The MoH is among the best performing ministries in terms of budget execution, but centralized procedures continue to constrain service delivery. The former Ministry of Planning and Finance (MoPF) took some steps to decentralize some procedures. MoH now manages procurement for contracts up to \$100,000 and has petty cash accounts at the district level, permitting staff to more easily procure essentials like fuel directly from suppliers. Raising the procurement threshold to \$250,000 would expedite implementation of capital projects. But such steps will need to be accompanied by further capacity building in procurement and financial management. The performance of SAMES in procurement, financial management, and distribution needs to be strengthened. Legislation calls for the now MoF to establish a financial oversight committee for SAMES, and consideration could be given to establishing an independent board of directors.

The planning and budgeting process could be improved by ensuring that district health plans are clearly linked to the budget. The MoH, districts, and hospitals also all need to start using the information they collect to monitor progress and to improve performance. This will require

strengthened supervision and technical support for district teams. With respect to donor coordination, the MoH wishes to continue progress towards a more sectorwide approach (SWAP), including through joint donor missions and harmonized implementation arrangements.

Facts and Figures

Health Infrastructure and staffing	
Number of health posts	155
Number of Community Health Centers (CHCs)	66
Regional Hospitals	5
National Referral Hospital (Guido Valadares)	1
Total health staff (Government)⁸	1,718
Doctors	
Timorese	17
Cuban	300+
Nurses	763
Midwives	255
Laboratory/other technician	33/103
Logistics/support	241
Administration	248
Key Service and coverage indicators	
% of pregnant women receiving at least one antenatal visits	61
% of children (6-59 months) receiving vitamin A supplements	36
% of children sleeping under treated mosquito nets (any net)	8 %
% married or cohabitating women using modern contraceptives	10
Percentage of malaria cases treated according to recommended protocols	30
% of infants (0-6 months) exclusively breastfed	31%
Child outpatient attendance rate (U5, annual visits per capita)	1.4 (2006)
Case fatality rate for children treated for severe malaria at health facilities	10%
Total fertility rate (average # children per woman)	7.7
% married or cohabitating women using modern contraceptives	10
Annual Population growth rate	3.2%

2. Progress on MDGs/key indicators

	2001/2	2006	MDG target	MDG Global target
Infant mortality rate	88 per 1000 births			½ of 1990
% children vaccination against				
DPT3	56%	63%	90%+	90%+
Measles	47%	61%	90%+	90%+
% children underweight	45%		31%	½ of 1990
Access to drinkable water (rural)	51%		75%	Double 1990
Access to sanitation (rural)	10%		40%	Double 1990
Maternal mortality ratio	800 per 100,000 live births			Reduce 1990 levels by 70%
% of births attended by skilled health personnel	24%		90%	90%
% of population taking effective malaria treatment	30%			90%
% of Tuberculosis cases treated successfully	80% of detected cases cured under DOTS			90%
Number of persons infected with HIV	Estimated HIV prevalence 0.35%			Maintain same low level prevalence

⁸ From 2005 MoH database

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9. Sector Note: Petroleum

Overview

Timor-Leste's petroleum revenues and savings arrangements will ensure the country's economic future. The savings arrangements allow for sufficient and sustainable funds to be used each year to fund the state budget, but to date Government has had trouble spending the annual budget. Timor-Leste's petroleum revenues amounted to USD1.2 billion as of March 31, 2007, and are increasing at a pace of USD 100 million/month since January 2007. While providing resources for the country's development, petroleum revenues also pose economic and governance challenges. International experience shows that countries rich in natural resources often experience more wasteful spending and corruption than other countries. To avoid this "resource curse," Timor-Leste adopted arrangements for good management of petroleum revenues for the benefit of current and future generations.

Key Issues

- ***Maintaining petroleum revenue management arrangements.*** These arrangements provide the basis for good governance of petroleum revenues. Saving for the future is important because petroleum resources will not last forever. At the same time effective spending from these revenues is necessary to develop and grow the non-petroleum economy, provide services, and reduce poverty.
- ***Developing Greater Sunrise.*** Through the Treaty on Certain Maritime Arrangements in the Timor Sea (CMATS), which entered into force in February 2007, Timor-Leste and Australia agreed to share 50/50 the revenues from the Greater Sunrise gas field. However, an agreement on how to develop the field has not yet been reached. This is largely due to discussions regarding where a pipeline from the field will go. Timor-Leste should establish an informed, consensus position on Sunrise development in preparation for such discussions. Commercial, social, and economic aspects should be taken into account.
- ***Reorganizing the Sector.*** In April 2007 the Oil and Gas Directorate put out for public comment draft legislation on a successor agency to the Timor Sea Designated Authority. Draft legislation on the creation of a national oil company was also put out. In line with the process followed for Timor-Leste's overall petroleum legislation, broader consultation and engagement with sector legal experts on scope and governance arrangements for these entities are warranted.

The Sector

All petroleum revenues that come to Timor-Leste are deposited in a Petroleum Fund managed by the Banking and Payments Authority (BPA). The Fund is governed by the Petroleum Fund Law, which spells out the formula for calculating the amount of "estimated sustainable income" that can be transferred from the Fund each year to finance the state budget.

Estimated sustainable income is the amount that can be withdrawn from the Fund in perpetuity without decreasing the country's petroleum wealth. Each year the amount of sustainable income is verified by an independent auditor. If the country follows this savings rule, it will have money available to finance its budget forever. Money from the Fund can only be transferred after approval of the annual budget by the Parliament and can only go to the budget..

Timor-Leste's petroleum management arrangements are designed to maintain transparency and accountability. The BPA issues quarterly reports on the Petroleum Fund, including its balance, any transfers, and its investments. These are publicly available. According to the law, an internationally recognized auditor must complete an independent, external audit of money received by the Fund each fiscal year. The auditor's report must be published. Made publicly available in July 2007, the first Annual Report, including the Fund's audited financial statements, and the quarterly reports are available from the BPA or at www.bancocentral.tl/PF/Reports.asp. An Investment Advisory Board advises the Government on the investment strategy and management of the Fund. An independent Consultative Council, including civil society and private sector representatives, advises Parliament on the Fund.

The former Ministry of Natural Resources, Minerals and Energy Policy (MNRMEP) and now possibly the Secretary of State for Natural Resources is responsible for petroleum resources in Timor-Leste's territory. The TSDA, a joint Timorese/Australian agency, is responsible for petroleum resources in the Joint Petroleum Development Area (JPDA) in the Timor Sea. The JPDA is governed by the 2002 Timor Sea Treaty (TST), under which Timor-Leste and Australia agreed to split JPDA revenue 90/10 in favor of Timor-Leste. According to the 2002 Timor Sea Treaty after three years the TSDA would be folded into an Oil and Gas Directorate or become a different Timorese agency.

In developing Greater Sunrise, Timor-Leste has favored the pipeline coming to its south coast along with the establishment of an LNG plant. Woodside, the main operator of the field, and Australia have favored the pipeline going to Darwin (where there is an existing LNG plant). Woodside and its joint venture (JV) partners (ConocoPhillips, Shell, and Osaka Gas) aim to prepare a preliminary development plan for Sunrise by September 2007. The plan will require agreement by the Governments of Timor-Leste and Australia. If Timor-Leste insists on a development concept that differs from what the JV believes to be in the JV's commercial interest, the JV may require compensation from Timor-Leste.

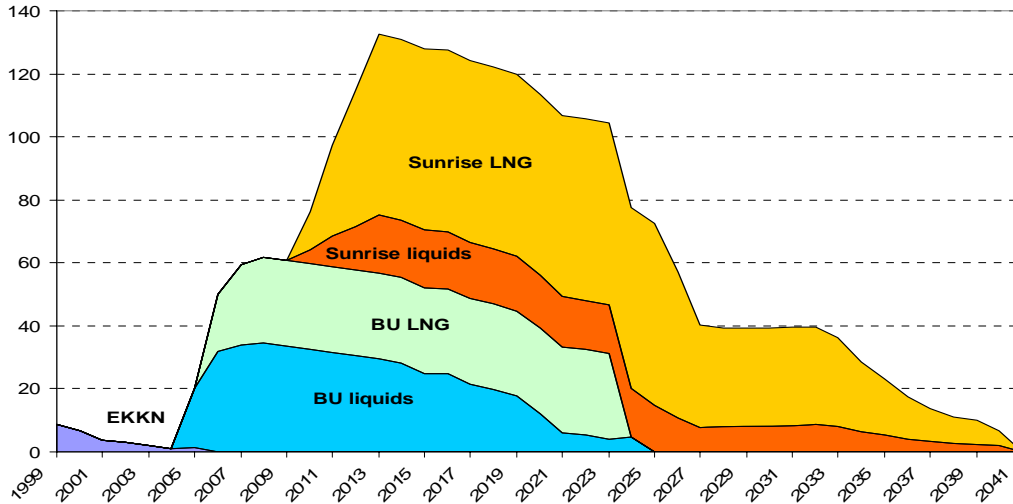
In addition to the Petroleum Fund Law, a Petroleum Law, Model Production Sharing Contract (PSC), and Petroleum Tax Law were adopted in 2005. This completes the legal framework governing the exploration and development of petroleum resources in Timor-Leste's territory. These laws are in line with international good practice. Timor-Leste is also implementing the Extractive Industries Transparency Initiative (EITI).

Timor-Leste's petroleum production is currently primarily from the Bayu Undan gas field in the JPDA. Bayu Undan is estimated to generate about USD9.4 billion in accumulated revenue for Timor-Leste over the next 15-20 years. Greater Sunrise is estimated, on a very preliminary basis, to generate around USD24 billion in revenues over the life of the field, half of which would go to Timor-Leste. As Sunrise is not under production its revenue projections are not yet

included in sustainable income estimates now produced for the budget. Exploration rights in Timor-Leste’s territory were awarded in 2006 to ENI and Reliance. While this could be another source of petroleum revenue, a commercial discovery must first be found and development concepts agreed before production starts/revenue flows. This is likely to take several years.

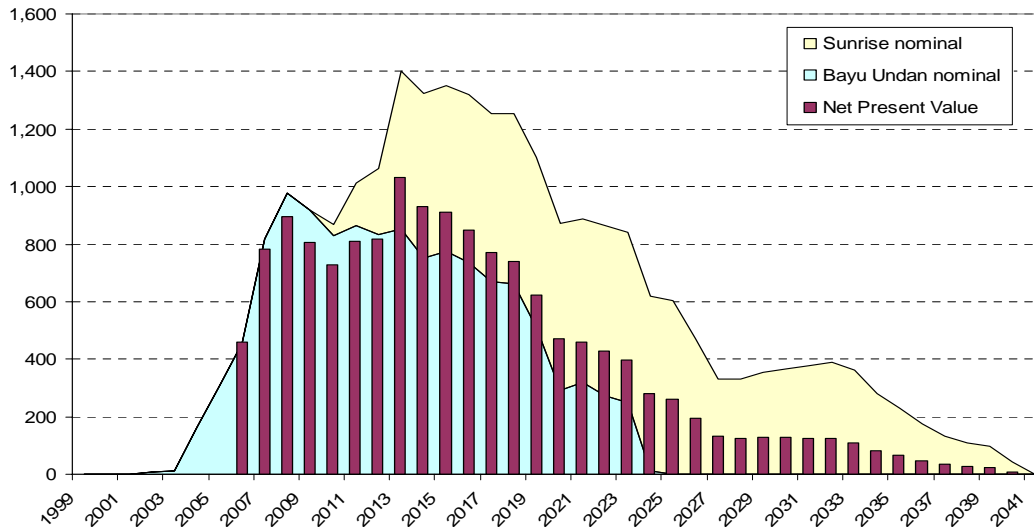
Facts and Figures

Timor-Leste Production Profile, 1999-2041 (million barrels of oil equivalent)*



*At this stage, Sunrise profiles should be considered as very broadly indicative only.

Timor-Leste Projected Petroleum Revenue Profile, 1999-2041 (USD million)**



**Projections are extremely sensitive to oil price assumptions, to which LNG prices are linked

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10. Sector Note: Power

Overview

Since 2002 significant progress has been made in improving power supply services. However, the quantity and quality of power supply services have deteriorated following the 2006 crisis. With the operation of a new generator at the Comoro Power Station started in April 2007, the reliability of the power generation system is expected to improve significantly. Nevertheless, much more needs to be done to improve power supply services, strengthen institutional capacity, enhance financial sustainability, and increase rural electrification. Timely and effective implementation of planned and ongoing initiatives is a challenge, but central to achieving results in the short term.

Key Issues

- ***Increasing reliability of Dili power supply.*** Implementing planned emergency repair of the Comoro power plant, rehabilitation of the power distribution system and ensure quality of fuels at the station in Dili will increase reliability.
- ***Improving supervision of management contractor.*** The appointment of the new management contractor, Manitoba Hydro, a Canadian company, will contribute to improve the performance of Electricidade de Timor-Leste (EdTL), the national power utility. However experience of the first management contract with Companhia de Electricidade de Macau (CEM) shows that Government needs to provide the management contractor with the necessary autonomy, while also ensuring adequate supervision. Supervision will ideally encompass a board with clear responsibilities and accountabilities, as well as systems to ensure regular reporting of performance and compliance with contract conditions.
- ***Implementing planned actions toward greater financial sustainability.*** Increasingly widespread illegal tapping of electricity is a major issue. This drives up the cost of electricity, contributing to the sharp increase in Government subsidies to cover cash deficits in EdTL in FY07. Planned actions to address illegal connections and improve revenue collection include action by the contractor with support from the sector ministry to address non-payment by customers and reinstallation of prepaid meters based on appropriate theft proofing standards.

The Sector

Timor-Leste has a small and fragmented power system. Currently, about 43,500 households have access to electricity, amounting to an overall electrification rate of around 22%. The Comoro Power Station in Dili serves about 26,500 customers in Dili and surrounding area, with

an electrification rate of about 85%. However, only 5% of rural households have access to electricity.

Power generation in the country has depended entirely on imported diesel fuel, resulting in one of the most costly electricity supply systems in the world. The current electricity price covers only a fraction of the total power generation cost, requiring significant subsidization from Government. Key to addressing this high cost is continuing plans toward diversification of power generation beyond diesel fuel as well as improved revenue collection and reduction of illegal consumption. The ongoing Gas Seep Harvesting Project and the planned Ira Lalaro Hydropower Project will, if successful, reduce the cost of power generation sharply.

Access to electricity in rural areas is very limited, but plans are in place to improve rural electrification. District capitals are currently served by some 60 isolated small power sub-systems administered by community management. The recently completed Rural Electrification Master Plan and experience gained from the ongoing Gas Seep Harvesting Project will help lay the groundwork for scaling-up rural electrification over the medium and longer term. The pilot Gas Seep Harvesting Project will supply electricity to about 1,000 households currently connected to the power system and about 2,000 new households and commercial customers in Aliambata, Babulo and Borolalo.

EdTL is legally part of the Government, but it is not financially autonomous. EdTL operates under the Government budget and receives subsidies to cover cash deficits for both operations and capital expenditures. For fiscal year 2007, the Government budget for EdTL amounted to US\$12.4 million, including about US\$8.4 million for imported fuels and the balance of US\$4 million for capital expenditures. In addition, US\$1.4 million of Government budget will cover the fees of the management contractor at EdTL.

Since 2002, the installed power generation capacity has been restored close to pre-1999 levels. System restoration efforts have shifted from rebuilding of power stations to repair and rehabilitation of damaged distribution networks. The engagement of a management contractor, CEM, increased the commercial orientation of EdTL. However, a review of the performance of this management contract by a consultant of the line ministry indicated that on the Government's side, the Supervisory Committee that was appointed to supervise the work of CEM did not fulfill its functions adequately or provide the requisite degree of direction, encouragement or assistance to the contractor. This highlighted the importance of providing a new contractor the requisite degree of management autonomy if history is not to repeat itself at the expense of the state.

Since the crisis in 2006, operational and maintenance field work of EdTL has been disrupted. Moreover, the contract with CEM was terminated in November 2006, although mobilization of a new contractor has been delayed. Consequently, CEM has been retained under a temporary contract, with reduced managerial staff. These adverse developments contributed to poor and/or disrupted maintenance, sub-optimal operation, and the lack of spare parts, resulting in a breakdown of power-generating units. Currently, the operating generating capacity at Comoro Plant Station is only about 15 MW, as compared with 29 MW of name-plate capacity. The poor quality of power services and the security crisis have contributed to a

sharp increase in bypassing of prepaid meters by users who use the electricity for free. This in turn has encouraged energy waste, exacerbating the current power supply shortfall during peak hours. Broad-based stakeholder consultations in February 2007, with representatives of the local government of Dili, NGOs, women’s association, a business group and local residents, confirmed the high priority of the Government to reverse the deterioration of power services, including halting illegal tapping of power, which is prone to cause fires and accidents.

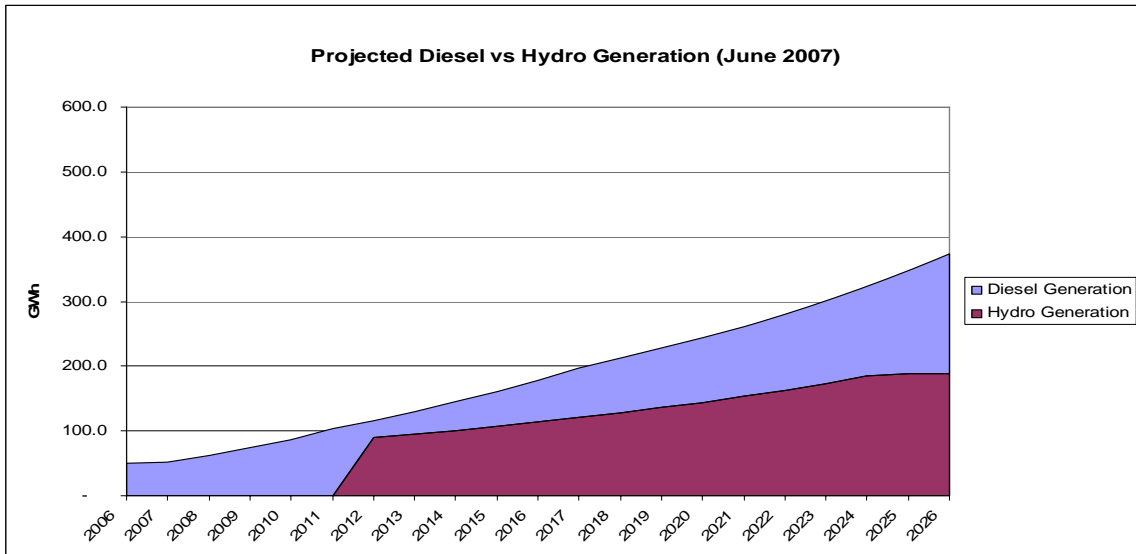
Facts and Figures

Power Generation Capacity in Dili with Operating Ratings in June 2007)

	Make	Year Installed	Nameplate Capacity (KW)	as of June 2007 operating ratings (KW)
1	Mak 1	1985	2,650	1,200
2	Mak 2	1985	2,650	1,200
3	Mak 3	1994	2,940	2,000
4	Niigata 1	1988	4,240	0
5	Niigata 2	2005	4,167	4,000
6	Cummins 8 units	2002	8,040	2,100
7	Caterpillar	2007	4,700	4,600
	TOTAL		29,387	15,100

Ira Lalaro Hydropower Plant

Ira Lalaro is expected to have a nominally-rated capacity of 28 MW, while firm capacity is estimated in at 12.9 MW. If implemented successfully, it is projected to bring down the cost of power generation substantially over the medium and longer term for the country.



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11. Sector Note: Private Sector Development

Overview

Improving Timor-Leste's climate for business is critical to economic growth and creating jobs in the private sector. Currently Timor-Leste ranks second worst in the world for ease of doing business – 174 out of 175 countries surveyed in the World Bank/International Finance Corporation's *Doing Business*. There are several reasons for this. Many administrative procedures are burdensome and expensive. Overloaded courts mean that resolving contract and labor disputes is nearly impossible. Infrastructure is highly under-developed and business input costs are high – electricity is among the most costly in the world for commercial users and phone calls cost around four times more than in Indonesia. Wages are several times higher than in the rest of the region. Supporting business services such as accounting, auditing and private law practices are nearly non-existent. A credit registry, which will help establish the credit worthiness of borrowers, has yet to be established. To address this situation, the challenge will be for the public and private sectors to work together to simplify unnecessarily complex regulation and to put in place efficient, clear administrative procedures. These measures need to be accompanied by an increase in public administrative capacity and promotion of a service attitude toward business in the public sector.

Key Issues

- ***Approving the land law.*** A functioning market for land is critical for strong private sector development. Passing the pending land law, drafted in 2005, will be the first step toward resolving Timor-Leste's difficult land situation. In the meantime, the Directorate for Land and Property at the Ministry of Justice can commence work on building a cadastre, the register of land ownership, and mapping out of plots, though this will require additional staff with appropriate technical skills.
- ***Accelerating reform of the business environment to stimulate investment and job creation.*** Amending those laws that are inconsistent and overly complex will reduce unnecessary bureaucracy. Examples include the Commercial Societies Act (company law), the Commercial Registry Code (business registration) and the investment laws.
- ***Easing business start-up procedures.*** A proposal to ease business start-up procedures, including predominantly the abolition or significant reduction of the required \$5,000 minimum start up capital for limited companies (more than 10 times the average annual income), was considered by the Council of Ministers at the end of 2006, but was not implemented.
- ***Enabling microfinance.*** The financial sector has grown rapidly with the establishment of three private banks and several microfinance providers. Government can play an important

role in creating a supportive environment for specialized agencies to provide microfinance and credit services to the population. Concrete measures could include provisions for safely transferring cash around the country. Adopting appropriate regulations for the establishment of a credit registry and exploring options for providing insurance can also help. On the other hand, Government should avoid providing credit guarantees or establishing new banks. Access to investment capital is needed, but is best served by established banks and microfinance agencies with the technical capacity to assess clients.

The Sector

There is a need to address deficiencies in the regulatory framework for the private sector. Timor-Leste has made progress in passing laws in a range of relevant areas, including foreign and domestic investment, tax and customs, companies and registration, border control and immigration, notaries, insurance, banking, payments and foreign exchange, and fisheries. However there are quality concerns with some of the existing legislation and in some areas necessary legislation has yet to be passed. Consultation with the private sector and others during the development of this legislation has been inadequate. As a consequence much of it is overly complex and does not take into account the limited implementation capacity of the public administration. Addressing these deficiencies in the legislative framework is becoming increasingly urgent. For example, there is an urgent case for deciding if registration should take place in the Ministry of Development and Economy or Ministry of Justice and set it out in regulations that are implemented. For the private sector it is of less consequence where registration takes place, but it is vital that the process is actually legal and simple: the current practice is an interim arrangement and is not, in fact, legal.

A much simplified investment framework would contribute to making Timor-Leste more attractive for both foreign and domestic investment. There are currently two investment laws, one for domestic and a second for foreign investment. These could be merged into one, simplified law. They are nearly identical, but both laws detail many exemptions that are difficult to administer. The implementing autonomous Government agencies, TradeInvest Timor-Leste (TITL) and Institute for Entrepreneurial Support (IADE), could be merged by amending their establishing decree-laws. Government can also make use of the planned Public Private Dialogue to guide the process of creating a better environment for business.

Land registration and titling is one of the key areas requiring attention. At present, some parts of a land legislation structure have been put into place: (a) leasing between private parties, and (b) leasing of state property. A good legal and regulatory environment for land should provide clarity on access to land, security of land title or use rights and the development of land. A functioning land administration system is likely to lead to: (i) improved security of tenure which facilitates transfer of land; (ii) a more developed credit market since it will facilitate use of land as collateral; (iii) a developed market for land; and (iv) increased investment, business development and economic growth.

There is large unmet demand for savings services and to a smaller degree for credit in the rural areas. To address the unmet demand for deposit services, Government could lift the current cap on savings of up to one million dollars in IMfTL (Instituto de Microfinancas de

Timor-Leste). IMfTL has reached the cap and cannot take more savings from clients. The national budget for 06/07 included a budget line for rural credit, with which it was intended to set up a bank. It is unlikely that a Government supported bank would achieve adequate levels of repayment, which could disrupt the financial sector. For rural outreach, there is one microfinance network that works well, Moris Rasik, with clients across the country, achieving high rates of repayment. Global experience supports that development of sustainable extension of credit is more effective if done by specialized microfinance providers, rather than Government.

There is a Private Sector Development SIP, called “Private Sector Development” which was updated in July 2007.

Facts and Figures

- Timor-Leste’s business community is largely made up of small family firms – 80% of the workforce is engaged in family farms.
- 72% of formal enterprises employ less than 10 workers.
- 33% of the population operates entirely outside the cash economy.
- 16,000 people enter the workforce annually whereas there are only 40,000 paid workers in the private sector.
- most firms obtain start-up capital from personal or family resources and not banks.
- 45% of formal and nearly 90% of informal urban firms have a turnover of less than US\$ 5,000 per year.
- foreign investors have shown interest in Timor-Leste but so far only a few investments have materialized and some early entrants have ceased operations.

Timor-Leste

Region: East Asia & Pacific

Population: 975,539

GNI per capita (US\$): 750.00

Country laws: see our [Law Library](#)



Ease of...	2006 rank	2005 rank	Change in rank
<i>Doing Business</i>	174	174	0
Starting a Business	160	158	-2
Dealing with Licenses	173	173	0
Employing Workers	115	114	-1
Registering Property	172	172	0
Getting Credit	159	160	+1
Protecting Investors	142	141	-1
Paying Taxes	124	119	-5
Trading Across Borders	73	66	-7
Enforcing Contracts	175	175	0
Closing a Business	151	151	0

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12. Sector Note: Public Financial Management

Overview

Timor-Leste's central financial management challenge is spending its annual budget. By the end of the third quarter of FY06/07, on a cash-basis only \$80.8 million had been spent from a central government budget of \$320 million, with another \$15.2 million of expenditure relating to carry-over from previous budgets. Execution of the capital budget is particularly weak. The surge in oil revenues has failed to translate into economic growth due to the inability of the Government to spend the income from the petroleum fund through the budget. Weak capital budget execution has also adversely affected the ability of Government to provide goods and services, undertake development projects, and jump-start economic growth and contribute to acceleration of job creation. Nonetheless, since independence Timor-Leste has made some progress in establishing an institutional framework for public financial management (PFM), although implementation of this framework remains in its infancy. PFM in Timor-Leste is characterized by inadequate implementation of rules and regulations, shortages in the number of qualified staff and limited familiarity with PFM systems and processes, both in MoPF and line ministries, have constrained public spending. The system remains heavily dependent on international advisers.

Key Issues

- ***Executing the budget.*** Immediate steps to improve budget execution could include: (i) the established Budget Execution Committee under the Council of Ministers should be made to work; (ii) re-introduction of petty cash accounts in line ministries, agencies, and districts; and (iii) timely issuing expenditure authorization notices to cover annual appropriations.⁹
- ***Improving capacity to execute the new procurement delegation.*** Government passed a decree in 2006 revising the threshold for delegating public procurement to qualifying ministries from \$10,000 to \$100,000. Eight line ministries have now have delegated procurement authority but have limited procurement and financial management capacities. This constrains the effectiveness of the delegation in improving budget execution. More coaching from the Ministry of Finance (MoF), and access to the computerized financial management information system, Freebalance, would help address this problem.
- ***Delegation of internal controls.*** In the past, there has been a reluctance to delegate internal controls, for example the separation of preparation and verification of CPVs, in public spending due to concerns of possible fiscal leakages. Overly centralized processes delay spending. Government may wish to balance delegation of internal controls with strengthened internal and external accountability, including legislative oversight.

⁹ World Bank Aide Memoire of July 26, 2006.

Procurement and commitment authority may be delegated to line ministries, while payments remain centralized.

The Sector

Timor-Leste has made some progress in several areas of public financial management. These include budget comprehensiveness in terms of including all Government revenues and expenditures and progress in implementation and upgrading of the financial management information system (FMIS) called Freebalance. Arrangements for the maintenance of aggregate fiscal discipline are in place. Expenditures are financed by the combined source budget which includes domestic non-oil revenues, oil revenues, and grants from the international community. Non-oil revenues, which began to recover in 2005, were set back by the recent crisis. However, high world oil-and-gas prices and increased output have raised projected oil revenue. The petroleum fund is integrated into the Government budget, and managed transparently.

The Government budget is comprehensive and policy-based, linked to national development goals. However, weaknesses in budget formulation processes reduce the accuracy of budgeted expenditures. The budget process requires estimates to be based on the annual action plans (AAPs) which are based on the national development plan (NDP) and sector investment plans (SIP). However, accuracy of budget estimates is reduced due to lack of expenditure planning, weak capacity and limited technical knowledge in project costing. Budget was appropriated on a commitment basis and total project cost, which spanning several years and front-loaded in single year appropriations. These practices overstated planned expenditures in a given fiscal year, skew budget execution rates and will benefit from significant reform. Government is now in the process of moving towards a cash based system, which is encouraged.

While the recurrent budget, salaries and wages, is mostly being executed as planned, the expenditure rates on a cash-basis for capital development projects has been particularly low. Recurrent budget execution progressed as planned at 75.2% by the end of the third quarter of FY06/07. By the end of the third quarter of FY06/07, Government had spent only 2.6% of its capital budget on a cash basis, when calculated as a percentage of appropriations. In FY05/06, only 6.9% of the capital budget was spent on a cash basis.

Practices in transaction recording, accounting and reporting provide an inaccurate picture of budget execution. Financial information is often recorded outside Freebalance in excel spreadsheets and statements are often prepared in excel spreadsheets instead of being produced automatically from Freebalance. Government may wish to keep more detailed track of expenditures from past budgets on a cash-basis so as to increase accuracy of the Government's financial position. Government could also ensure all financial officers within delegated line ministries have 'read' access to Freebalance.

Facts and Figures

Table 1. Timor-Leste: Finances of Central Government

(In millions of US dollars, unless otherwise noted)

	2002/03	2003/04	2004/05	2005/06	2006/07 (Q1-Q3)
Budget a/	74.27 b/	74.1 b/	78.67 b/	131.05 c/	320.64 c/
Recurrent Expenditure (commitment basis)	..	..	..	87.45	192.05
Capital Expenditures (commitment basis)	..	..	..	43.60	128.59
Current year expenditure on a commitment basis					
Expenditure	..	69.2	73.5	119.2	210.9
Recurrent Expenditure	..	59.5	61.5	77.3	114.6
Wages and salaries	..	23.8	25.1	25.7	24.2
Goods and services	..	29.2	31.2	45.6	66.3
Current transfers	..	0.0	0.0	0.0	11.6
Subsidies to agencies	..	6.6	5.3	6.0	12.4
Capital Expenditure	..	9.7	12.0	41.9	96.4
Minor capital	..	..	2.3	6.6	14.3
Capital and development	..	..	9.0	24.8	77.1
Capital transfers	..	0.4	0.4	10.5	0.0
Subsidies to agencies	..	0.0	0.2	0.0	4.9
Current year expenditure on a cash basis					
Expenditure	68.5	66.9	70.7	93.1	99.7
Expenditure from current budget	58	55.5	59.1	81.8	80.8
Recurrent Expenditure	53.3	53.1	56.4	66.1	75.2
Wages and salaries	21.6	23.8	25.1	25.7	24.2
Goods and services	25.3	22.8	26.0	34.4	35.3
Current transfers	0.0	0.0	0.0	0.0	3.9
Subsidies to agencies	6.4	6.6	5.3	6.0	11.8
Capital Expenditure	4.7	2.4	2.8	15.6	5.6
Minor capital	..	..	..	3.4	2.9
Capital and development	..	..	..	1.7	2.7
Capital transfers	..	0.4	0.4	10.5	0.0
Subsidies to agencies	..	0.0	0.2	0.0	0.0
Expenditure from past budgets	10.5	11.4	11.5	11.3	15.2

a = Budgets are appropriated on a commitment basis

b = Source for FY 02-03 to FY04-05 is the annual financial reports and accounts, GoTL

c = Source IMF, 2007

Source for statistical annex: IMF, 2007; References: World Bank Aide Memoirs July 2006, October 2006, February 2007; PEFA assessment report, IMF Staff report, article IV, 2006.

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13. Sector Note: Public Sector Administration

Overview

Development of an effective, accountable, and transparent public service is crucial for effective delivery of services and programs, and securing public confidence in state institutions. The public service has inexperienced managers, few rules, and limited capability. Performance will be improved through clear management and reporting, merit-based career structures, workforce planning, and opportunities for further training. The Civil Service Statute (2004) creates a good legal basis for the service but implementing regulations remain to be passed. Further laws on pay and career structure and staff assessments are in draft but require thorough evaluation to ensure that their impact will be positive. Leadership is critical, as is motivating staff and building a service delivery culture. It will be important to dispel public suspicions of politicization of the service, and for Ministers and senior civil servants to model responsible behavior and practices. Government should avoid any immediate sweeping changes so as not to cripple an already weak administration.

Key Issues

- ***Explore ways to improve local service delivery in the short term to secure and maintain public confidence.*** Strengthening existing local financial and other delivery systems will help get results. The new decentralization proposals require further work, and would need to be carefully handled in order to avoid further disruption to services.
- ***Develop leadership and management ability*** to (i) focus on results, (ii) set benchmarks for task delivery, (iii) institute simple, regular reporting, (iv) set standards for team behavior, (v) reward staff for good performance and enable their further study and training, (vi) reprimand staff for poor work and absenteeism.
- ***Implement the Civil Service Statute 2004.*** This can equip managers with the necessary tools to manage their staff appropriately. However, the draft implementing regulations, and more recent Decree Laws on a Career Regime and salary structure, need review and amendment before implementation to ensure that they are simple, clear, consistent and free from politicization.
- ***Complete workforce planning.*** Clear workforce planning is required to support the emergence of an effective civil service. The Capacity Development Coordination Unit (CDCU) is estimating the numbers of staff required in different skill categories, and identifying shortfalls, over-staffing, and ways of providing needed skills and improving the productivity of international advisers.
- ***Interim allowances for civil servants.*** The one-off cost-of-living subsidy paid to civil servants stopped at the end of FY07. Interim provisions could be made in the next six month and calendar year budgets to prevent salaries falling until decisions are made on the permanent pay structure.

The Sector

The public service, including staff of autonomous agencies, consists of 25,631 public servants, including: 17,471 permanent staff, 4,034 temporary staff, and 4,126 casuals.¹⁰ The budget for salaries and wages in FY 2006/2007 represented 12.8% of a total state budget. Civil servants are often unclear about the goals or core functions of the agency in which they operate, they are delegated limited responsibilities, and have few non-financial incentives to improve their performance. Absenteeism and poor time-keeping are frequent. High priorities include development of clear communication between ministers and civil servants, development of able and committed managers, clear service-wide rules, transparent processes for decision-making, recruitment, promotion, and management control.

Development of leadership and management ability is necessary for results. Improved service delivery and effective public administration can only be achieved through leadership, a sense of direction, and clear communication of expectations. Managers must be encouraged to focus on results and set benchmarks for delivery that can be monitored by a simple and regular system of reporting. Informing staff of the Civil Service Code of Conduct and setting standards for behavior would also yield improved results. It is also important to strengthen the usefulness of the several hundred foreign and national advisers by defining advisers' roles, standards of behavior, and ensuring accountability for results.

The Civil Service Statute 2004 provides a constructive framework for civil service development, management, and human resource management. An immediate priority is to implement this statute to provide managers the tools including – recruitment, promotion, performance evaluation and non-financial reward structures - to manage their staff appropriately. Proposed implementing laws would benefit from evaluation and amendment before implementation. These include: a Decree Law (January 2007) establishing a career regime and salary structure that would result in a 38% increase in public service pay. This decree and recent draft decrees on recruitment and promotion and performance evaluation might helpfully be reviewed to ensure that they are feasible, consistent and fair. In many countries, independent Public Services Commissions are charged with ensuring accountability, transparency and impartiality in the application of regulations. They also insulate ministers from decisions concerning civil servants. The opportunity exists to create a Public Services Commission for Timor-Leste. The Provedor can also be instrumental in providing civil servants and citizens with an impartial way of raising concerns of maladministration. Publicity of the complaints process and results would create motivation to improve.

Plans to upgrade the National Institute of Public Administration (INAP) are needed but will take time to implement. Meanwhile, extensive donor efforts to up-skill civil servants have had mixed results due to over-reliance on substitution by international advisers and off-site training. Greater emphasis on training within workplace systems is necessary. Workforce planning is also needed to deliver the right number and type of personnel with the needed administrative and technical skills to deliver services to the public. The CDCU workforce planning initiative aims to address this challenge. In parallel, a Public Management Information System (PMIS) that will provide the essential baseline data needed to manage staff and overall workforce planning and performance is being developed

¹⁰ MSA stats at July 2007.

Facts and Figures - Staff profile¹¹

<i>Sovereign institutions</i>	<i>Permanent staff</i>	<i>Temporary</i>	<i>Casuals</i>	<i>Intl. Advisers</i>	<i>Total (Excl. intl.)</i>
Office of the President	111	40	-	6	151
National Parliament	43	30	-	6	73
Tribunals	66	68	-		134
Sub-total					358

Government agencies

Office of the Prime Minister and President of the Council of Ministers	73	97	27	17	197
Ministry of Defense	18	-	-	-	18
Office of the Secretariat of State for the Council of Ministers	21	3	20		44
Ministry of State Administration (incl. district admin.)	414	98	1300	7	1812
Ministry of Interior (incl. PNTL admin)	661	55	339	15	1055
Ministry of Development	57	65	62	2	184
Secretary of State for Youth and Sport	35	21	2	-	58
Ministry of Justice	477	18	107	15	602
Ministry of Agriculture, Forest and Fisheries	316	187	250	21	753
Ministry of Education and Culture	6831	1220	1190	4	9241
Ministry of Health	1760	602	-	4	2362
Ministry of State for Labor and Community Reinsertion	105	-	157	5	262
Ministry of Foreign Affairs and Cooperation	64	66	-	1	130
Ministry of Planning and Finance	511	62	205	29	778
Ministry of Transport and Communications	140	93	101	2	334
Ministry of Natural Resources, Minerals and Energy Policy	190	27	-	7	217
Ministry of Public Works	189	88	78	6	355
F-FDTL	1435	-	-		1435
PNTL	3500	3	40		3543
Sub-total					23,380

Independent agencies:

INAP	29	16	-		45
Public Prosecution Office	29	17	8	11	54
Ombudsman for Human Rights and Justice	12	4	30	3	46
Tertiary Institutions or Universities	-	1006	-		1006
Sub-total					1,151

Autonomous agencies:

STAE				1(?)	
Directorate for Materials	26	14	146	-	186
EDTL	260	15	0	-	275
Directorate for Civil Aviation Service	84	4	44	-	132
Port Authority	44	-	20	-	64
Banking and Payments	67	-	-	3	67
Autonomous Medical Supplies	-	-	-	-	0
Public Broadcasting Service of Timor-Leste	-	135	-	2	135
Sub-total					859
TOTAL	17,568	4,054	4,126	166	25,748

¹¹ MoPF Budget Paper No 1, 2006-2007 refers.

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14. Sector Note: Telecommunications

Overview

Access to Telecommunications Infrastructure and Services in Timor-Leste is limited and expensive. Only 5% of Timorese citizens, most of them in Dili, have access to basic telephone or data services.¹² Internet access is costly and limited in capacity. Improving access to affordable, reliable, and readily-available telecommunications infrastructure and services could benefit the entire economy and society. Benefits include lower costs for Government, businesses, and households. Improved access to information is another benefit. This can help farmers seeking information about prices and availability of goods and services or small businesses communicating with suppliers. Better telecommunications technology can generate new economic opportunities, such as those offered by mobile phone-enabled financial services and internet cafes, as well as direct and indirect job creation. Further, Government can derive increased revenue from a more diversified telecoms sector than from a single operator. Currently, Timor-Leste is not reaping any of these benefits. Many governments, including in the Pacific region, are addressing similar challenges. Telecommunications reform can have high political visibility due to its direct impact on the population. With strong leadership, and technical support from development partners there is potential for quick wins, though the institutional changes will take some more time.

Key Issues

- ***Promoting a pro-poor/pro-rural business strategy.*** As a shareholder and regulator, Government can strongly encourage Timor Telecom to adopt a more pro-poor/pro-rural business strategy. Immediate measures could include introduction of lower-denomination credit recharge cards and electronic recharge, reducing the cost of text messaging (SMS), introducing low-cost handsets, and starting a “village phone” program to provide public access in rural areas.
- ***Increasing competition.*** Government can introduce competition in telecommunications, in particular mobile telephone and internet services. The recommended approach is through renegotiation of the Concession contract (BOT) with the current provider. This will involve first preparation and adoption of a new telecommunication and information technology policy. This can be followed by formation of a Government Steering Committee, preparation of a negotiating strategy, and formal legal agreement with Timor Telecom.
- ***Updating the legal framework.*** Telecommunications laws could be revised and modernized. It will also be important to develop new regulations in specific areas, such as tariffs, spectrum, and interconnection. Review and development of regulation will ideally

¹² Fixed lines=2,300. Mobile subscribers=63,000. Internet subscribers are about 650.

focus on consumer/user rather than operator interests, and empower the regulatory authority (ARCOM) to enforce them.

- ***Investing in a domestic high-speed "backbone"***. Improvement in the communications infrastructure could increase the overall capacity of the telecoms network. Two important measures are building of a domestic “backbone” to ensure access to services across the whole territory and lower-cost international links. At the same time, it will be necessary to put in place regulatory safeguards to allow for use of such infrastructure on fair and transparent terms.

The Sector

The telecommunications market structure in Timor-Leste is restrictive, deterring new investment. The telecommunications operator, Timor Telecom (TT), holds a 15 year monopoly in the form of a “build operate transfer” (BOT) concession contract. This is an unusual legal instrument for telecommunications service provision. Current laws and regulations favor the operator's interests. They also restrict the role of the regulatory authority and offer little or no protection to consumers. These factors have limited further development of the sector. For example internet services are very limited and expensive. Slow dial-up service is available where there are fixed lines, mostly in Dili. “Dedicated” or leased line service is available to large users, but very expensive. Broadband or “high-speed” internet is not available.

The BOT Concession Agreement gives a broadly defined exclusivity over most telecommunications services. However obligations relating to quality of service are weak. The concession is long-term in nature, and lacks reasonable termination provisions. The concessionaire is exempt from paying for the use of frequencies until the end of the concession, but gets to “own” numbers, which may be considered scarce public resources. The nature of the BOT arrangement, in which the provider is required to transfer assets to the Government at the end of the concession period, is a disincentive to long-term investment. It encourages the operator to maximize short-term profits.

Decree laws numbers 11 and 12/2003 do not adequately empower the relevant institutions. Although telecommunications legislation has been passed it has not been fully enforced. Moreover, the organic law for the sector ministry which establishes the organizational structure, functions and processes of the ministry has not yet been approved. Absent the organic law, it is difficult to apply the telecommunications laws, organize, or delegate authority. With regard to the legislation itself, while reflecting good regulatory practice in many areas, it falls short in others such as licensing, universal service obligations, tariffs, radio spectrum, media, and numbering. In addition, the laws were passed after the BOT concession was granted and are geared towards a monopolistic market.

Institutions currently lack enforcement capacity. The sector ministry acts as policymaker and the sector regulator, ARCOM, is attached to the Ministry. However, regulatory capacity suffers from shortages of skills and lack of financing, e.g. from radio spectrum usage, number allocation and license fees that regulators typically collect.

There is real potential for improved access by means of new, particularly mobile and internet technologies, and through a more competitive market. The cost of access to telecommunications has come down worldwide, and new, particularly mobile/internet technologies, bring information and communications tools closer to rural populations. Benchmarking suggests that, with competition, particularly for mobile services, the number of mobile subscribers could reach at least 200,000 within 2-3 years, up from less than 70,000 today. In other countries, even the *threat of competition* has prompted monopoly operators to lower costs and increase the variety and quality of services.

Facts and Figures

Comparative Data (sources, ITU 2005, plus latest available operator data).

Market structure: M=monopoly, C=competition, PC=partial competition (ISPs cannot set up own infrastructure).

<i>Country</i>	<i>Population</i>	<i>Fixed lines/100</i>	<i>F</i>	<i>Mobile/100</i>	<i>M</i>	<i>Internet/100</i>	<i>Market structure</i>
Timor-Leste	1,100,000	<0.5	M	5.0	M	<0.5	PC
Samoa	185,000	11.0	M	46.0	C*	4.0	C
Vanuatu	212,000	3.5	M	11.5	M*	3.8	M
Solomon Is	478,000	<0.5	M	1.5	M	<0.5	M
Fiji	848,000	14.0	M	35.0	M*	7.7	C
PNG	6,000,000	<1.0	M	3.0	M	<0.5	PC

Note: Competition in mobile communications likely to be introduced in Vanuatu and Fiji in 2007. Samoa introduced mobile competition in 2006.

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15. Sector Note: Transport

Overview

Road, aviation, and maritime transport sector investments have the potential to quickly deliver important social and economic development benefits. However, the state of the road network has become a bottleneck to development rather than a platform for growth. The condition of the road network is generally poor, and sections fail regularly during the rainy season, resulting in rural populations in particular having limited access to towns and markets. Vehicle operating costs are high by regional standards, travel is slow, and the nation is fragmented economically. However there has been ample transport strategic planning and Timor-Leste has a high quality, detailed 10-year road sector investment plan¹³ that underpins the Transport Sector Investment Program (SIP). The SIP is currently being updated and provisionally includes increased transport (land, air, sea) investments proposed under the Program for Accelerated National Development (PAND)¹⁴. The works defined in the PAND transport program will generate much needed employment and provide an opportunity to institutionalize quality design and construction procedures. Important road, aviation, and maritime projects await budget commitment. Whether or not to commit to PAND is a key issue facing the transport sector, especially roads and bridges.

Key Issues

- ***Accelerating national development.*** The most important short-term decision facing the Government, for the road sector, is whether to continue with the 10-year national road rehabilitation program (the first year is currently being implemented) or to ramp the program up to include widespread road improvement (not just rehabilitation; and including new bridges). The Ministry of Infrastructure already has four requests for proposals for consulting services to prepare preliminary designs and feasibility studies (based on a standard national road pavement width of seven meters where feasible). The Government is in a position, if it chooses, to recruit consultants for this work within 2 months.
- ***Improving budget execution and quality of works.*** Although the former Ministries of Public Works (MoPW), and Transport and Communications significantly improved capital program execution during the latter part of FY07, it will be impossible to significantly increase the pace of public works and harness their job creation potential without improved budget execution.
- ***Outsourcing, period contracts, large contracts, and other models to leverage ministry resources.*** There is little experience of feasibility study, engineering design, and civil works

¹³ Prepared with the help of ADB TA 3731-TIM, the feasibility study for the Road Sector Investment Project

¹⁴ Refer NADP project breakdown included in Table 1.

outsourcing to private firms in Timor-Leste. This is changing, and the Infrastructure Ministry should take full advantage of outside project management support being offered.

- ***Labor intensive approaches.*** There is already one ongoing and two planned labor intensive road maintenance programs, including some road improvement. These can directly benefit thousands of local people, particularly in rural areas, and should be quickly rolled out.

The Sector

The former MoPW obligated over 50 consultant services and civil works contracts worth a total of \$28 million prior to the end of FY07. However urgent challenges remain: (a) capital works are typically included in annual budgets without proper programming and project definition; (b) this leaves ministry staff with the impossible task of preparing and managing preliminary design contracts, detailed design contracts, and civil works contracts – all in one year; (c) because of “spend it or lose it” rules, ministries prepare and tender or sole-source very crude contracts that expose the government to financial loss and poor quality civil works; and (d) even then, actual disbursements remain low and carried forward amounts continue to accumulate. Capital works items should not be budgeted until after the preliminary design/feasibility study stage. In seeking to remedy this, the Infrastructure Ministry could take full advantage of outside project management support being offered.

Greater use could be made of “period” contracts, especially for road maintenance, as a model for leveraging Ministry resources. Period contracts could be easily prepared, tendered, awarded, and managed, covering an entire city, town, or district/s for a defined period of time. Packages can also be consolidated, for instance all bridges of a particular type and scale could be awarded as a single contract. This would not jeopardize local firms who would always be subcontracted in order to reduce costs. Other models should be trialed, for instance road maintenance outputs-based aid (OBA) contracts.

Rural and feeder roads rehabilitation program. Strategic planning, programming and investments have focused so far on national and some district roads. Systematic rehabilitation of rural feeder roads is now urgent.

Facts and Figures (2005)

Surface area (sq km)	14,870
Length of Existing National Road network	1,412 km, with 400 bridges
Length of Road Network in Poor or Very Poor Condition	1,200-1,300 km
Original pavement widths	3.2-4.5 m

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16. Sector Note: Veterans

Overview

Recognition and assistance for veterans of the resistance has been an area of strong progress since 2002. Commissions under the Office of the President registered a total of 75,143 veterans, in a transparent and participatory process. A reliable database of registered veterans has been produced. The veterans law, the Estatuto dos Combatentes da Libertação Nacional (ECLN), passed in 2006, is fundamentally sound, but could be strengthened through amendment. Payment of veterans pensions and other benefits has been delayed, awaiting approval of the relevant decree laws. However Government has prepared relevant administrative procedures, manuals, plans, and a pension database. Pensions can be rolled out quickly once the decrees are approved.

Key Issues

- ***Transferring the database.*** Currently the veterans database is with the Comissão de Homenagem, Supervisão de Registo, e Recurso (CHSRR). Transfer of the database to the Secretário de Estado para os Assuntos dos Antigos Combatentes de Libertação Nacional (SEAACLN) is necessary for Government to start processing pensions.
- ***Approving decree laws.*** The two decree laws laying out the legal framework for payment of pensions have been drafted. The laws need to be approved in order for Government to start paying pensions.¹⁵
- ***Institutional strengthening.*** Currently, 17 out of 22 of the Direcção Nacional dos Antigos Combatentes de Libertação Nacional (DNACLN) staff are on temporary contracts, leading to insufficient investment in training and risk of losing qualified staff. Moving qualified staff to permanent contracts will strengthen the department
- ***Amending the veterans law.*** Consideration could be given to a strengthening of veterans' pension scheme through amendments to the law.

The Sector

A total of 12,002 people have been awarded medals in ceremonies of recognition since November 2006. The ceremonies were organized by the CHSRR. Of these 11,367 were awarded to survivors of the deceased, while 635 were awarded to the living. Additional ceremonies are planned for late 2007. Supported by the Government budget, the CHSRR is

¹⁵ (i) Decree-law on pensions and subsidies to combatants of national liberation and their families and
(ii) Government decree establishing financial benefits under the Statute of the Combatants of National Liberation.

mandated by the ECLN to organize and oversee the ceremonies. The CHSRR includes members appointed by Parliament (3), Government (3), the President (3), and F-FDTL (1). The CHSRR was established in September 2006 and can run for a total of two years. According to the law, a final registration opportunity must be opened for one year, currently planned to start in January 2008. The registration will be implemented by Government but overseen by the CHSRR.

The data from the registrations carried out by the Comissão para os Assuntos dos Antigos Combatentes - Comissão para os Assuntos dos Veteranos das Falintil (CAAC-CAVF) and Comissão para os Assuntos dos Quadros da Resistencia (CAQR) has been corrected and verified several times by the Comissão Consolidação de Dados (CCD), which closed in May 2006. The data is sound. However, there are 10,338 pending cases for which data is missing or incomplete. There are also 859 "denunciados" cases in which claims have been lodged against individuals, disputing their eligibility to be recognized as veterans. By law, both categories for cases must be resolved by the CHSRR.

The veterans law foresees four pensions: Subvenção por Dedicção Exclusive, Pensão Especial de Subsistência, Pensão Especial de Reforma, and Pensão de Sobrevivência. The law has to date been interpreted such that only full-time participation in the resistance, in practice the armed struggle or prison, counts for the purpose of receiving a pension. A change whereby time in the clandestine front was also counted would greatly increase the pool of beneficiaries and budget implications of the law. In 2005, 38 long-serving veterans started receiving subsidies of between \$100 and \$123 a month. This will cease once the pension system starts.

Currently only 350¹⁶ living veterans are eligible for monthly pensions. Those who served between one and eight years are only eligible for the *Subvenção por Dedicção Exclusive*, a one-off payment. Those who served 8-14 years will only receive a pension after they turn 55. By contrast up to 11,829 survivors of deceased veterans could receive pensions, with no age limit applied. Consideration could be given to lowering the years of participation required, eliminating the 55 year age limit, and/or making the levels of payment more equitable.

Government has undertaken significant preparations for paying veterans pensions. The public attendance unit, pensions and benefits units, and database unit have been established. The public attendance unit will have offices in each of the 13 districts to receive pension applications. A site in Dili for the public attendance unit has been obtained and is awaiting rehabilitation, although the funds were not obligated. \$10 million was included in the FY07 budget for veterans pensions, but these funds cannot be accessed while Government is operating without a new budget.

Beneficiaries have been identified and construction is underway for 100 houses for veterans who served 15 to 24 years, are disabled for work, and currently lack housing. The first stage of the Garden of Heroes memorial near the Metinaro F-FDTL base has been completed. A second stage is planned and consultation on design is underway.

¹⁶ All figures from the Comissão Consolidação de Dados, November 2006 via SEAVAC/DNACLN.

Facts and Figures

Total Registered Veterans:	75,143
CAAC-CAVF (Frente Armada):	38,337
CAQR (Frente Clandestina):	36,806
Pending:	10,338
Living:	56,627
Deceased:	18,516
Martyrs (Died as a result of participation, survivors eligible for pension.):	11,829
Excluded – less than three years participation:	7,848
3 – 8 years participation (both armed and clandestine struggle):	27,983
3 – 5 years in armed struggle:	7,901
6 – 8 years in armed struggle:	181
8 or more years participation (right to medal under law):	11,223
8 – 14 years in armed struggle:	193
15 or more years in armed struggle:	157
24 years in armed struggle:	28

Veterans Pensions as Defined by Estatuto dos Combatentes da Libertacao Nacional, Law No. 3/2006

<u>Pension Title</u>	<u>Category as Defined by Law</u>	<u>Beneficiaries*</u>	<u>Payment Range</u>
Pensão Especial de Reforma (Art. 25)	15 or more years	157	\$254 - \$407 per month
Pensão Especial de Subsistência (Art. 24)	8 - 14 years, once over 55 years of age	193 currently 53 are over 55	\$85 - \$159
Pensão Especial de Subsistência (Art. 24)	Disabled veterans	Disabled veterans unknown, pending development of criteria	\$85/month
Subvenção por Dedicção Exclusiva (Art. 23)	Veterans who did not join the public service – in practice those who served 1 – 8 years	approx. 17,905	One-off payment of \$200 per year served
Pensão de Sobrevivência (Art. 26)	Widows, orphans, parents, or siblings of those who died due to participation in the struggle. One pension beneficiary per deceased	11,829	\$85/month

(Data source: CCD via DNACLN, November 2006)

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17. Sector Note: Water Supply and Sanitation

Overview

Globally, the Water Supply and Sanitation (WSS) sector, both rural and urban, is problematic. Data on WSS coverage and levels of service is unreliable, and the 2004 national census had no questions relating to WSS. Nation-wide, only about 13% of families have house connections and 16% are served by community taps. Best estimates for rural water supply are 30% coverage (2004). Urban water supply estimates vary greatly according to definitions: for instance, if access to 24-hour continuous piped safe water is the benchmark, then only about 25% of Dili households are adequately served. There are problems with willingness to pay, willingness to charge, technical difficulties in maintaining systems, and water utility governance. Rural sanitation coverage estimate for 2004 was 19%. As in many countries, in Timor-Leste the effective demand for improved sanitation is typically lower than demand for improved water supplies. Changes in knowledge, attitudes, and practices are needed to lock-in health benefits from improved water and sanitation. Inadequate funding, sub-optimal investment strategies, and lack of human resources are the most important development constraints.

Key Issues

- ***Increasing human resources.*** Timor-Leste does not yet have sufficient qualified, trained, and experienced WSS planners, engineers, and technicians to deliver on NDP and MDG targets. This could take 10-15 years, and in the meantime outside experts, contracted by the Government, are needed if targets are to be achieved.
- ***Maintaining WSS services.*** Urban as well as rural WSS services are difficult to maintain. Part of the problem is that piped water supply systems are difficult to manage and maintain, especially in rural areas. Part of the solution is to define clear and *appropriate* service standards - levels of service - for specific geographical and community situations. Service levels policy has been prepared and can now be disseminated and applied. More involvement by Government in rural WSS, providing technical, financial, and authority backup to community system managers, could also help solve these problems.
- ***Increasing financial sustainability.*** Urban water operations are losing more money than ever before. The National Development Plan, and global experience, make clear that costs should be recovered from customers. This is difficult in the current situation and full cost recovery is 10 or more years away. But the decline in urban water supply revenues should be reversed by increasing billings and collections. The necessary legislation already exists. In 2004 – 2005, the Government prepared a National Water Resources Policy in 2004/2005 but it was never approved by the Council of Ministers.

The Sector

The National Directorate of Water and Sanitation (DNAS) is responsible for developing and providing WSS services throughout Timor-Leste. DNAS has 164 allocated permanent staff positions, supplemented by 137 temporary contract positions. Most staff and resources are assigned to urban water supply activities. DNAS is a designated revenue collection agency but is not a ‘Revenue Retention Agency’ (such as EDTL, Ports, and Aviation authorities) and must return collections to the Banking and Payments Authority. The new Corporate Services Directorate (CSD) within the former MoNRMEP is responsible for advising the Minister on WSS policy. There are currently no donor-funded international advisors working within CSD, further constraining capacity. CSD is also responsible for procurement of government-funded WS projects. The WSS sector in Timor-Leste lacks certain legislation and policy, but these are not major development constraints.

DNAS urban WSS operations cover Dili and all 12 remaining district centers. The DNAS urban water supply infrastructure asset base is estimated at around \$50 million. \$30 million has been spent on the Dili water system since 2000. Urban waste water management is almost entirely a private responsibility; there is no sewerage system or Government owned and managed communal septic tanks, only the septage treatment facility at Tacitolo. DNAS manages the collection and disposal of solid waste in Dili. No urban water supply system in Timor-Leste is complete. Most rehabilitation, including for Dili, has focused on water production (water source development, transmission, treatment, storage) and primary and secondary distribution. Tertiary distribution (reticulation) has received little attention and in Dili, for instance, 50% of water is lost through leaks and pilferage.

Reducing water losses and non-revenue water is essential. This can be achieved by concentrating investments using a “zonal approach” to system improvement rather than spreading investments thinly. A zonal approach focuses rehabilitation works on single defined hydraulic zones, one or a few at a time. When reliable water supplies are completely restored in a zone and customers are satisfied, the investment program moves to the next zone/s. The program is stepped around the city until the entire network is functioning properly. The first zonal approach project for Dili is being prepared.

It is estimated that less than a quarter of rural households in Timor-Leste have access to safe water, while an even lower proportion (19%) have access to adequate or effective sanitation facilities (some data suggests that this figure may even be lower, at 13%). There is also a widespread lack of awareness of health and sanitation issues among the rural population. The most common diseases among children are acute respiratory infections and diarrheal diseases, also common among adults. It is estimated that large numbers of rural children under the age of five die because of the lack of potable water, poor sanitary environment and sanitation practices. Mountainous geography, poor road infrastructure and annual cycles of drought further compound problems of access in rural areas. Women are generally the primary collectors, transporters, and end users of water. Currently, there is limited Government capacity to plan, manage, and deliver rural water supply and sanitation services.

The National Development Plan includes seven Water Supply and Sanitation (WSS) objectives and 15 performance indicators, including (i) 80% of urban population with access to safe piped water, and (ii) 80% of rural population with access to safe local water supply. Timor-Leste has also signed on to the Millennium Development Goals (MDGs), which means increasing the proportion of people with improved access to water from 44% to 78%, and the proportion of people with improved sanitation 19% to 46% - see below for actual WSS coverage. Government and donor-supported WSS programs are guided by the WSS Sector Investment Program (SIP) that provides an itemized five-year rolling investment program. The WSS SIP is currently being updated.

Rehabilitation and improvement of WSS facilities and services since 2000 have been mostly funded by donors. The Government's own WSS capital works program for FY2007 totaled \$1.79 million, around \$1.00 million for rural water supply and the remainder for urban water supply. 65% of this budget allocation has been obligated, meaning contracts awarded.

Facts and Figures

The specific targets set by Government for access to adequate rural water supply and sanitation are detailed below. These targets are based on the Government's desire to achieve the Millennium Development Goal (MDG) for provision of safe water and sanitation.

Targets for Access to Rural Water Supply and Sanitation

Indicator	2004 Target	2010 Target	2015 Target	2020 Target
Access to safe drinking water, Rural population (%)	30%	60%	80%	80%
Access to safe drinking water, Rural population (total)	215,528	506,362	759,293	850,867
Access to sanitation, rural population (%)	19%	50%	80%	80%
Access to sanitation, Rural population (total)	136,501	421,968	759,293	850,867

Economic and Social Development Brief

18. Sector Note: Youth

Overview

Despite its potential, the youth sector can most appropriately be described as *in crisis*. It is therefore essential that the Government and the international community make a concerted, comprehensive and strategic investment in the youth sector in order to stem youth involvement in violence and lawlessness, and to capitalize on the potential of this generation. Youth constitute a significant and growing percentage of the population. Youth development, however, has received little attention from the Government or the international community since independence. Youth involvement in the crisis of 2006 and more recent violent episodes have highlighted the dangers of neglecting this sector.

Key Issues

- ***Keeping youth in school.*** Despite the current generation being the most educated of the Timorese, many do not finish school. Numerous benefits accrue to both the individual and society when youth stay in school.
- ***Increasing youth employment opportunities.*** Unemployment amongst youth is staggeringly high. Without regular work youth are susceptible to manipulation and involvement in violence and other risky behavior.
- ***Connecting youth with community.*** Many youth feel disconnected from family, community and society. This is the result of massive social change and a weakening of social structures over the past 35 years.
- ***Empowering youth to participate in nation-building.*** Amongst today's youth there are strong feelings of disillusionment with the government and marginalization from the nation-building process.
- ***Strengthening formal and informal controls on youth*** is crucial to preventing their involvement in violence and other risky behavior.

The Sector

Youth aged 15-29 constitute almost one-quarter of the population. This number is expected to increase to 37 % in 2010. Today's youth are the most educated generation of Timorese, but many do not complete school. 77% complete *some* primary education, but only 34% complete junior secondary and 27% complete senior secondary school. The quality of education is also generally low. Literacy remains high at 77%, but many young people leave school without the skills and information needed to find work and escape poverty. Indeed, youth unemployment is

currently estimated at approximately 43% nationally and a staggering 58% in Dili. See the annex for a summary of these figures.

In addition to economic and education factors, social, political and legal factors contribute to the current youth crisis. Many young people suffer from domestic violence, feel disconnected from community and school, drink heavily, and are perceived negatively by society. The youth of today feel marginalized and disillusioned. They distrust the authorities and the older generation. They lack necessary civic education and opportunities to engage meaningfully in the nation-building process. Furthermore, the breakdown in social control mechanisms has encouraged youth to act with impunity and participate in opportunistic activities, including crime and vigilantism. It is therefore unsurprising that youth quickly became implicated in the ongoing crisis.

Past Government programming in the youth sector has recorded some notable wins. The response of the Government and the international community to the current crisis has been swift and commendable. The former Ministry of Labor and Community Reinsertion (MOLCR) drafted a National Action Plan on youth employment 2007-10. The Secretariat of State for Youth prepared a draft national youth policy, and the Government's post-crisis Compact includes youth employment and skills development as one of its themes. More programmatically, the Government and the international community launched a number of cash-for-work programs that mostly benefited youth. The MOLCR/ILO program, for example, ran from April to December 2006 and generated over 465,000 workdays, and provided employment to 37,000 people, 44% were youth, for 15 days each. Since independence, and prior to the current crisis, the Government and international community established a number of youth centers as well as vocational training centers. Several international organizations have been providing school lunch programs in order to encourage participation, and the Government is envisaging a similar program of its own.

Although these initiatives have been generally positive, three inter-related challenges have consistently beleaguered the youth sector: scope, scale and sustainability. Youth involvement in the recent violence and social unrest has highlighted the need to expand the *scope* of programming in the youth sector to address social, political, legal, as well as economic aspects of the current youth crisis. Related, the sheer number of youth and the depth of the current crisis have underlined the critical need to expand the *scale* of programming in the youth sector. Finally, ensuring the *sustainability* of initiatives in the youth sector has proved illusive. For example, many youth centers stopped functioning once donor funds finished. *These challenges are due to a number of factors, including weak leadership and coordination of the youth sector, a lack of dedicated and sufficient funds, as well as implementation capacity constraints.*

Only a comprehensive approach—one that understands the problem holistically, combines local and international experience, and commits to a long-term strategy—can address the current challenges and overcome the current youth crisis. The rapid expansion of recent labor-intensive youth employment programs is of particular importance.

Facts and Figures

Population Profile

Youth make up a large and increasing percentage of the population.

Total Population	924,642
Youth (Total)	225,300 (24%)
Youth (15-19)	94,300 (10%)
Youth (20-29)	131,000 (14%)

Note: There are slight differences in age categories used in figures and graph

Education

Today's youth are the most educated generation of Timorese, but many do not complete school. Poor-Non-poor differences are higher than male-female differences

	All
Some primary school	77%
Junior secondary school	34%
Senior high school	17%
Post-secondary	2%

Literacy

Illiteracy remains high despite high levels of primary school completion.

Youth literacy	77%
Youth literacy (female)	76%
Youth literacy (male)	79%
Comparison (Philippines)	97%

Employment

Unemployment is extremely high, particularly in the urban centers Dili and Baucau.

Youth Unemployment (Total)	43%
Youth Unemployment (Dili/Baucau)	59%
Youth Unemployment (Rural)	15%

Note: %age for Dili/Baucau and Rural based on the 15-19 youth age group.

School-to-Work Transition

The school-to-work transition takes men on average five years, and many take even longer

Transition age	17 years
Transition time (poor)	5 years
Transition time (better-off)	7 years

Figure 1: Youth (12-29) share of population (1995-2015)

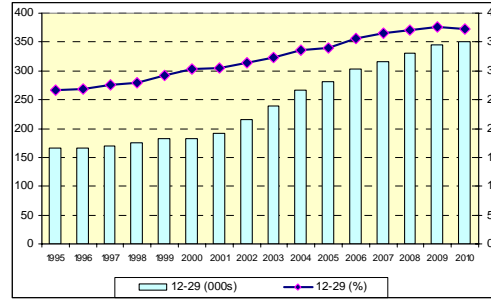


Figure 2: Education attainment by population group

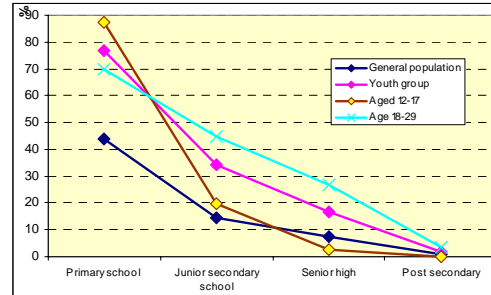


Figure 3: Youth literacy rate

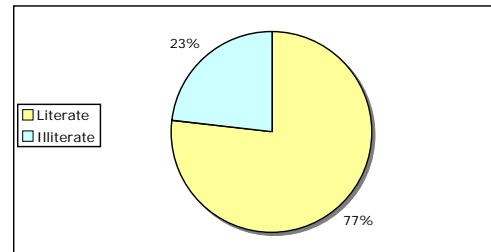


Figure 4: Unemployment by age group and geography

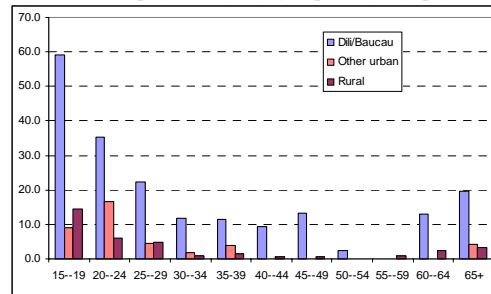


Figure 5: School-to-work transition

