

CONTINUED RELEVANCE OF THE TIMOR-LESTE – ADB COUNTRY PARTNERSHIP STRATEGY 2016-2020

I. INTRODUCTION

1. The Timor-Leste – Asian Development Bank (ADB) Country Partnership Strategy 2016–2020 (the CPS) was approved in May 2016.¹ The strategy was designed to support economic growth and diversification by removing infrastructure bottlenecks and institutional constraints, and by investing in human capital. Knowledge solutions were integrated into sector operations and coordinated through a country knowledge plan, and sector programs were designed to leverage private sector expertise. The CPS was prepared and approved during a period of political stability and relatively good economic performance. Subsequently, starting 2017, the implementation was impacted by a prolonged period of political instability, of approximately two years, and the current COVID-19 pandemic that delayed progress.

2. The CPS envisaged a scaling up of ADB lending, with indicative lending approvals of \$82 million per annum during 2016–2019 compared to average approvals of \$40.6 million per annum during 2011–2015. However, ADB approvals declined to an average of \$42.4 million per annum during 2016–2019. Considering the delays in CPS implementation, the Government of Timor-Leste agreed to extend the strategic priorities of CPS to 2023 to allow additional time for successful implementation.² This assessment of the relevance of the CPS been prepared as an input into the enhanced COBP 2021–2023. The enhanced COBP 2021-2023 will extend the CPS strategic priorities until the new CPS 2023-2027 is prepared.

II. ALIGNMENT TO GOVERNMENT PRIORITIES AND ADB’S STRATEGIC AGENDA

3. The CPS was designed under the VI Government of Timor-Leste, aligned to the country’s *Strategic Development Plan 2011-2030* (SDP).³ Infrastructure development is a core pillar of the SDP. Some progress was made in the development of road networks, but overall Timor-Leste did not meet any of the SDP’s 2020 objectives on infrastructure such as completing the rehabilitation of all national and regional roads and having all government schools connected to clean piped water. Non-oil economic growth remains heavily driven by the public sector, and additional institutional reforms and investments in human and physical capital are necessary to carry the diversification of the economy and eradicate poverty. The CPS also aligns with the program of the VIII Government of Timor-Leste which is in the continuity of the two previous Governments. Given this continuity, the country context, and the limited developments since 2017, the focus of the CPS remains appropriate.

4. The priority areas in the CPS continue to provide good guidance for ADB planning as it is aligned with ADB’s Strategy 2030 and its operation priorities, in particular on addressing remaining poverty and reducing inequalities (OP1), accelerating progress in gender equality (OP2), making cities more livable (OP4), strengthening governance and institutional capacity (OP6), and fostering regional cooperation and integration (OP7).⁴

¹ ADB. 2016. [Timor-Leste: Country Partnership Strategy 2016-2020](#). Dili.

² Letter from Vice Minister and Interim Minister of Finance, No. 421/GVMF/VIII/2019-11, dated 18 November 2019. Implementation of the CPS progressed was delayed due to three different presidential and parliamentary elections in 2017 and 2018.

³ Government of Timor-Leste. 2011. [Timor-Leste Strategic Development Plan, 2011–2030](#). Dili.

⁴ ADB. 2018. [Strategy 2030: Achieving a Prosperous, Inclusive, Resilient, and Sustainable Asia and the Pacific](#). Manila; and ADB. 2008. [Strategy 2020: Working for an Asia and Pacific Free of Poverty](#). Manila. The CPS was also aligned to ADB’s Strategy 2020 and the strategic agenda of inclusive economic growth.

III. IMPLEMENTATION OF THE CPS

5. The CPS identified three objectives: more inclusive and sustainable growth; improved human capital; and a more diversified and productive economy. ADB's lending during the CPS period focused largely in the road transport sector, and grants financing allocated to projects in water and urban services, education, energy. A summary of the progress in the CPS priority areas is provided below. Related outcomes indicators and outputs remain relevant and are in the process of being realized. Knowledge has been consistently used as a tool to accelerate progress on the CPS objectives. The use of regional TA facilitated cross-learnings and access to international experiences. TAs were systematically attached to projects, as required by the Timorese legislation. Several knowledge gaps were addressed fully or partially, although some areas require additional support and capacity building.

6. **More Inclusive and Sustainable Growth.** There has been good progress on the outcome indicators showing reduced time and cost to transport goods and people by road, improved coverage and reliability of electricity services, and increased access to improved water and sanitation. PPP options are being explored. O&M and climate resilience are being incorporated into ADB-supported project designs.

7. *Inclusive and sustainable infrastructure services.* ADB supported policy and planning in selected infrastructure services e.g. transport sector masterplan; masterplans for water supply systems in Dili and four municipal capitals; and strengthening quality of public investment management by closing gaps in sector policies and plans in energy, transport and water and urban infrastructure and services. Some aspects related to contractors' capacity, PPP-management, financial literacy, and sectoral planning were not fully tackled during this implementation period.

8. For road transport, disbursements for the period 2016-2020 was \$232.8 million through two grants and seven loans. A multi-donor project management unit (PMU) was created to manage all ADB, World Bank and JICA projects. Delays occurred in approvals related to safeguards measures (resettlements and environmental licensing) and political instability, and in implementation related to contractual, payment and financial issues.

9. Timor-Leste aims to improve air connectivity through the expansion of Dili airport to increase the existing capacity of 150,000 passengers to one million people per year. ADB is supporting the assessment of the Dili airport runway upgradation and ancillary facilities.

10. *Leveraging private sector expertise for infrastructure management.* Use of PPP for infrastructure has been an area of interest of the Government for several years, but the capacity to develop and manage PPPs remains limited. ADB projects integrate capacity building in the private sector and technical advice to the Government. Two performance-based maintenance pilot contracts were awarded after completion of the ADB Road Network Development Sector Project. The only PPP in Timor-Leste - the Tibar-Bay Port PPP concession contract – was supported by ADB in 2016.

11. The Government has initiated assessments in other areas, such as solid waste management, with ADB support since 2018, and transitioning management responsibility for the electricity supply agency EDTL to a PPP arrangement.⁵ ADB has helped prepare masterplans for water supply systems in Dili and four municipal capitals, review tariff policy in Dili, and has contributed to the development of water resource policies. A TA is on-going with the aim to

⁵ ADB. [Timor-Leste: Power Distribution Modernization Project.](#)

strengthen the quality of public investment management, by closing remaining gaps in sector policies and plans in energy, transport and water and urban infrastructure and services.

12. Long-term fiscal sustainability. Key issues highlighted in the CPS remain valid, including risk to infrastructure sustainability due to limited maintenance capacity. The new Transport Sector Master Plan highlights effective road maintenance is still under-budgeted and most of the maintenance budget is spent on emergency work. ADB has incorporated a minimum of two years of post-construction O&M into its road investment projects and is working with the government to establish appropriate O&M systems in all infrastructure sectors.

13. Despite progress over the last 10 years, several communities have no access to electricity and existing networks need modernization and replacement of ageing assets. Government action to reduce technical losses has been limited. ADB's most recent estimate is that technical system losses and non-technical issues due to unmetered and unbilled consumptions account for over half the electricity lost. Reducing the heavy subsidization of the electricity sector is also essential for long-term fiscal sustainability. In 2016, ADB provided \$1 million TA to EDTL.⁶ The distribution network is planned for upgradation through the Power Modernization Project in 2021. ADB is also supporting institutional reforms including transformation plans for electricity and water services departments into two state owned enterprises (SOEs) in 2020.⁷ Continued support will be needed to ensure successful transition in line with the current CPS strategy.

14. Successive governments have regularly emphasized the need to increase domestic revenues to alleviate the pressure on the rapidly-depleting Petroleum Fund. A Fiscal Reform Commission (FRC) was created in 2015 and ADB supported the process.⁸ Although the FRC was dissolved in 2019, the government has emphasized the importance of continued work toward fiscal reforms.

15. Environmental sustainability. Significant efforts toward climate resilience proofing in infrastructure projects has been made. However, Timor-Leste's terrestrial and marine biodiversity face serious challenges. There are gaps in legislation and poor understanding of existing regulations. The capacity for implementation, administration and oversight is weak within the National Directorate of Pollution Control and Environmental Impact (NDPCEI) and implementing agencies. ADB has supported capacity development of NDPECEI for licensing activities and review of the legal framework and preparation of amendments.⁹

16. There is lack of legislation regarding fisheries and the protection of marine biota, currently covered by a 2004 law. Illegal fishing is rising in the southern sea region. ADB has assisted the government through a regional TA to prepare a strategy plan for the development of the fishery sector as well as to assist in the establishment of marine protected areas both managed by the government and the community.¹⁰

17. **Improved Human Capital.** The outcome indicators are on track and show increase in technicians with secondary and post-secondary qualifications as well as increased access among

⁶ ADB. 2019. [Timor-Leste: Energy System Strengthening and Sustainability Project \(TA 9802\)](#). Manila.

⁷ ADB. 2016. [Finding Balance 2016. Benchmarking the Performance of State-Owned Enterprises in Island Economies](#). Manila. Supported through [Timor-Leste: Implementing Reforms for Growth and Competitiveness \(TA 9932\)](#) to address the departments' lack of capacity and autonomy in decision making and the low level of service delivery. International experience has shown that restructuring public utilities as SOEs can help improve efficiency and quality, but this is contingent upon good corporate governance.

⁸ ADB. 2016. [Timor-Leste: Fiscal Policy for Improved Service Delivery \(TA 9122\)](#). Manila.

⁹ ADB. 2017. [Timor-Leste: Policy and Planning Development for Public Investments, Subproject 1 \(TA 9495\)](#). Manila.

¹⁰ ADB. 2010. [Regional Strengthening Coastal and Marine Resources Management in the Coral Triangle of the Pacific, Phase 2 \(TA 7753\)](#). Manila.

urban households to reliable water supply. Progress is being made to improve sanitation to realize 100% coverage by 2030.

18. Technical Education. The limited availability of skilled staff is a major obstacle to Timor-Leste's economic diversification. In 2016, the secondary technical system counted 7,938 students, an increase of 7% from the previous year. Budget allocations to Technical-Vocational Education Training (TVET) followed an upward trend and collaborative efforts were made to unify course curriculums, create training manuals, and assess professional skills. Further strengthening of the connection between the TVET and the labour market is needed. Between 2010 and 2016, the ratio of skill mismatch in the employed population rose from 4.8% to 12.2%, attesting employment of people in occupations below their educational attainment and reflecting a misalignment between the education system and workforce skills requirements. An updated Education Sector Plan 2020-2030 includes revised objectives and costings for TVET.

19. Urban water supply and other services. The Dili Urban Water Supply Project, completed in 2018, provides important lessons on institutional capacity and O&M support.¹¹ The project design overestimated government capacity to guide policy development and project implementation. The water sector has inadequate expertise for design and project supervision, lacks institutional structure and incentives, provides poor water quality and service to customers, and fails to maintain the system and undertake repairs. Consequently, the project suffered significant delays and several outputs could not be completed. Inclusion of an O&M capacity building component in future water projects is required to ensure sustainability of water systems.

20. **A more diversified and productive economy**. There has been some progress on the output indicators, including compliance with ASEAN legal agreements, improved availability and efficiency of financial services, and increase in FDI from ASEAN+6 countries.

21. Business enabling environment. Timor-Leste's efforts to build a stronger business-enabling environment have showed limited results. Business development requires a multi-faceted intervention to tackle a limited financial sector, lack of skilled labour, administrative constraints, and legal and governance weaknesses relating to contract enforcement, commercial dispute resolution, and land rights. Timor-Leste's export promotion agency TradeInvest Timor-Leste IP aims to facilitate international partnerships and encourage investments in non-oil sectors of the economy but FDI inflows remain low and dropped to their lowest in 2016-2017, before making a recovery in 2018-2019. Core to improving the business environment is reviewing Timor-Leste's legal framework. A revised Private Investment Law was passed in 2017, but more adjustments are needed.

22. Opportunities for ADB's non-sovereign operations are constrained by the slow development of the private sector. ADB focus on engagement in nontraditional sectors can have a highly catalytic impact. In 2017, ADB approved its first private sector operation as part of a regional project whereby a \$4 million loan was approved to the global agro-firm Olam to fund coffee processing equipment and permanent working capital along with \$1.2 million TA grant for providing training regarding improved production and climate-smart agriculture to 4,200 farm households.¹² Additionally, a grant project approved in 2020 will support implementation of Timor-Leste's Coffee Sector Development Plan and pilot a new training model for farm households.¹³

¹¹ ADB. 2018. [Timor-Leste: Dili Urban Water Supply Sector Project \(Grant 0100\)](#). Manila.

¹² ADB. 2018. [Olam International Limited: Inclusive, Sustainable, and Connected Coffee Value Chain, Subproject 2. \(TA 9521\)](#). Covering Indonesia, Timor-Leste, Viet Nam, and Papua New Guinea. Manila.

¹³ ADB. 2020. [Timor-Leste: Coffee and Agroforestry Livelihood Improvement Project \(Grant 9209\)](#). Manila.

23. *Financial sector development.* The finance sector of Timor-Leste is stable and profitable, The payment system is being modernized and the Central Bank is implementing the National Financial Inclusion Strategy 2017-2022. However, critical constraints remain. Expanding credit access necessitates addressing institutional barriers, improving the diversity of available financial products, and improving the regulatory framework. ADB's support for governance reforms at BNCTL, the state-owned national commercial bank, is an example of good corporate governance that can guide management of other SOEs in the country.¹⁴

24. *RCI.* Fostering RCI is an important element of Timor-Leste's strategy towards building a more diversified and productive economy. Substantial efforts are needed to achieve compliance with ASEAN and WTO. In addition to support for ASEAN membership, ADB is working on strengthening Timor-Leste's ties with its geographic neighbors. Following assessment of border cooperation opportunities, ADB is supporting fostering of cross border trade in livestock and tourism cooperation between Timor-Leste and Indonesia's West Timor.¹⁵

25. Review of Timor-Leste's legal framework is also key to ASEAN accession. Compliance with binding and non-binding ASEAN requirements is being finalized and a TA is also assisting the development of an ASEAN focal point system across different ministries.¹⁶ In addition, ADB is supporting Timor-Leste's application process to WTO.

IV. CONCLUSION

26. In 2019, the Government of Timor-Leste launched a new Foreign Aid Policy which aims to reinforce the use of country systems by integrating the portfolio of donor funded projects in the national planning and budgeting system and better align activities of development partners to the Government's priorities. Education, health, malnutrition, youth and gender, agriculture and rural development, tourism, infrastructure for growth, connectivity and accessibility, water and sanitation, RCI, private sector development and public sector management are listed as priority areas for external support, which confirms the relevance of the CPS in its alignment with Government priorities.

27. ADB's cumulative support in 2020 covers eight areas including transport, water and other urban infrastructure and services, education, energy, agriculture, natural resources and rural development, RCI and public sector management. In 2019, the Government provided a list of sectors which could be financed partly through borrowing. This represents an opportunity for ADB to diversify its existing investment portfolio. Indicative lending for water and urban sanitation, ICT development, energy and education are expected to be approved in 2021. In non-lending, ADB will continue on-going support to transport, energy, urban and water development, fiscal sustainability, agriculture, finance development, and RCI. ADB is also working to provide high-quality, demand-driven, and responsive knowledge support.

28. The proposed timeframe for the extension of the strategic priorities of the current CPS is end-2022. This would enable ADB to make further progress and complete the projects under implementation which has been delayed due to political issues and the current COVID-19 pandemic.

¹⁴ ADB. 2014. [Timor-Leste: Expansion of Financial Services \(TA 8762\)](#). Manila.

¹⁵ ADB. 2019. [Regional: Cross-Border Trade and Cooperation between Indonesia and Timor-Leste \(TA 9767\)](#). Manila

¹⁶ ADB. 2020. [Timor-Leste: Capacity for Multilateral and Regional Economic Integration \(TA 6542\)](#). Manila.