

REGIONAL COOPERATION AND INTEGRATION ASSESSMENT (SUMMARY)

1. Regional cooperation and integration (RCI) is an important part of Timor-Leste's development strategy. Membership of the Association of Southeast Asian Nations (ASEAN) is Timor-Leste's principal RCI objective and would support integration with the dynamic economies of East and Southeast Asia. Timor-Leste can also benefit from, and contribute to, knowledge sharing with the Pacific island nations with which it shares important characteristics such as size and fragility. ADB can support Timor-Leste's RCI through investments in improved transport connectivity, targeted technical assistance to address constraints to regional integration, and support for knowledge sharing.

A. Background and National Strategy

2. **Geography.** Timor-Leste's location and ethno-linguistic heritage place it within Southeast Asia. It is situated at the Eastern tip of the Malay Archipelago and comprises the Eastern half of the island of Timor, the Oecusse-Ambeno enclave in the Western part of Timor, and the islands of Atauro and Jaco. It has 228 km of land borders with Indonesia and shares maritime borders with Indonesia to the North and East and West, and Australia to the South. Timor-Leste has important historical and cultural ties to Portugal and other Portuguese speaking countries and has also forged links with neighboring countries in the Pacific region by participating in Pacific regional fora.

3. **International Relations.** After achieving independence in 2002, Timor-Leste became a member of the United Nations and acceded to key UN treaties and conventions. Since then, it has established diplomatic relations with more than 100 countries and developed consulates and embassies in each of the countries in Southeast Asia as well as major economies and historical allies outside the region. Timor-Leste is a founding member of the g7+ group of fragile states and continues to fund the group and host its secretariat. The g7+ was instrumental in the development of the New Deal for Engagement in Fragile States and continues to advocate for more appropriate and country-led responses to fragility. Timor-Leste has also assumed leadership of the Community of Portuguese Language Speaking Countries (CPLP). As chair of this group from 2014-2016 it is using its position to broaden the scope of cooperation between CPLP member countries to include economic policy and investment.

4. **Foreign Policy Objectives.** Timor-Leste's constitution establishes friendship and cooperation as key objectives of its international relations and gives special priority to relations with neighboring countries, countries within the region, and Portuguese speaking countries. Timor-Leste's Strategic Development Plan 2011-2030 (SDP) expands on the constitution by committing to an outward looking, collaborative approach to foreign policy that promotes stronger cultural and economic linkages that can support the country's development. Timor-Leste has identified itself as a potential nexus for cooperation and exchanges between Southeast Asia, the Pacific, and the countries of the CPLP.¹

B. Priority Initiatives

i. Demarcation and Management of International Borders and Boundaries

5. **Indonesia.** Indonesia is Timor-Leste's largest trading partner and the two countries have established cooperation on healthcare, environmental management, agriculture, security,

¹ Government of Timor-Leste. 2011. *Timor-Leste Strategic Development Plan, 2011-2030*. Dili.

defense, and petroleum development. There has been good progress in demarcating the land borders between the two countries, with 97% of the border now demarcated. Efficient border management can help to facilitate a smooth flow of goods and people between the countries. This is particularly relevant given the close historical and cultural ties, the physical separation of the Oecusse-Ambeno exclave from the rest of Timor-Leste, and the potential for significant gains from trade. Formal border posts have been established at Batugade, Saleni, Sacato, and Boboneto and in recent years the entry of foreign citizens via these land borders has been comparable to total international arrivals by airplane. The border post at Batugade, currently accounts for the majority of recorded flows of goods and people although the proportion of total bilateral trade that is routed through the land border is not clear. Priorities for border management include completion of border demarcation; improved protocols for communication between government and security officials involved in border management; introduction of a border pass system for citizens of both countries living close to the border; and harmonization of arrangements for customs clearance and quarantine.

6. **Australia.** Timor-Leste and Australia share a maritime boundary in the Timor Sea. The location of this boundary has not been demarcated but interim arrangements for management of the boundary area were established through the Timor Sea Treaty (TST) in 2002.² The TST demarcated a Joint Petroleum Development Area (JPDA) and defined a legal and regulatory regime for regulating petroleum production within the JPDA. In 2006 Australia and Timor-Leste signed the Treaty on Certain Maritime Arrangements in the Timor Sea (CMATS) in 2006.³ CMATS has an agreed duration of fifty years and its signature also extended the validity of the TST so that it will remain in force until CMATS ends. Under CMATS, Timor-Leste's prospective share of revenues from the undeveloped Greater Sunrise gas field rose from 20.1% to 50%. However, CMATS also included a moratorium on the pursuit of sovereign rights or jurisdictional control of the maritime boundaries. There has been a prolonged and complex disagreement relating to the way in which CMATS was negotiated and the implications that the treaty would have for the development of petroleum resources and the distribution of benefits. In 2013, Timor-Leste initiated legal proceedings in the International Court of Justice (ICJ) to have the CMATS Treaty revoked. In addition to pursuing a claim in the ICJ, Timor-Leste has also maintained bilateral dialogue with Australia on the issue. In 2015 Timor-Leste established a Maritime Council that is chaired by the Prime Minister to pursue a final delineation of its maritime boundaries with Australia.⁴ Resolution of the current disagreements would pave the way for development of the Greater Sunrise oil and gas field.

ii. **The Association of Southeast Asian Nations (ASEAN)**

7. **Commitment to membership.** ASEAN membership has been a priority for Timor-Leste's leaders since independence. Timor-Leste joined the ASEAN Regional Forum in 2005 and acceded to the Treaty of Amity and Cooperation in Southeast Asia in 2007. The SDP aims for Timor-Leste to have become a key ASEAN member by 2020 with recognized expertise in economic development, small-nation management, good governance and aid effectiveness.

8. **The pathway to membership.** The ASEAN Charter establishes four conditions that prospective members must meet: i) location within Southeast Asia; ii) recognition by all ASEAN

² The Government of East Timor and the Government of Australia. 2002. *Timor Sea treaty between the Government of East Timor and the Government of Australia.* Dili.

³ The Government of Australia and the Government of the Democratic Republic of Timor-Leste. 2006. *Treaty between Australia and the Democratic Republic of Timor-Leste on Certain Maritime Arrangements in the Timor Sea.* Sydney.

⁴ Government of Timor-Leste. 2015. *Decree Law No. 2/2015.* Dili

Member States; iii) agreement to be bound and to abide by the ASEAN Charter; and iv) ability and willingness to carry out the obligations of membership.⁵ Timor-Leste has already met the first three conditions but meeting the fourth condition will be challenging. ASEAN's move towards deeper cooperation and integration means that accession is more technically demanding now than when Cambodia, Laos PDR, Viet Nam, and Myanmar joined in the 1990s. At present a new ASEAN member would be required to accede to 64 substantive legal agreements and make the necessary changes to domestic legislation to ensure consistency.⁶ A new member must also show commitment to the various ASEAN's non-binding policy objectives and develop the capacity to participate meaningfully in ASEAN's technical working meetings.

9. **Preparations for accession.** Timor-Leste formally applied to join ASEAN in 2011 with strong support from key ASEAN members including Indonesia. This application remains under consideration by the ASEAN Coordinating Council and a specially formed working group. In the meantime, Timor-Leste has taken steps to prepare for membership. It hosted a meeting of the ASEAN Regional Forum in Dili in 2011 and received an official visit from the ASEAN Secretary General in 2012. The Government has strengthened its diplomatic and economic relations with ASEAN member countries, established a system of ASEAN focal points in relevant line ministries, and carried out public awareness programs. The government has also requested technical assistance from ADB and other development partners to support training and capacity building, analysis of the economic implications of ASEAN accession, and mapping of the domestic legal and institutional reforms needed to comply with ASEAN requirements. Initial preparations have highlighted that accession to ASEAN will be a major undertaking that requires the implementation of substantial legal reforms and close coordination across a wide range of government departments and agencies.

10. **Impact of membership.** A joint ADB and Timor-Leste Ministry of Finance study on the economic implications of Timor-Leste's accession to ASEAN suggests that the short run first-order impacts will be positive but modest.⁷ Timor-Leste already has a relatively liberal and open trade policy so there will be no dramatic changes due to trade liberalization. Joining ASEAN would send a clear signal that Timor-Leste will maintain relatively open and liberal policies for trade and investment and this may help to encourage investors who would otherwise be deterred by uncertainty about future policies. The corollary of this is that accession to ASEAN will reduce the policy space of future governments since they will not be free to pursue policies that breach Timor-Leste's ASEAN treaty commitments. The longer term impacts of ASEAN membership are largely dependent on the Government of Timor-Leste's ability to address critical constraints to business activity within the country.⁸ This points to the importance of linking ASEAN accession with the government's broader program of economic reforms.

iii. Timor-Leste-Indonesia-Australia Growth Triangle (TIA-GT)

11. Timor-Leste has been the leading proponent of trilateral integration with certain sub-regions of Australia and Indonesia. The TIA-GT was first proposed in 2010 and is intended to include the Indonesian province of East Nusa Tenggara (ENT), and the Northern Territories of Australia. The premise of the growth triangle is that additional efforts to enhance physical, institutional and social connectivity will help to accelerate development of the three regions. The

⁵ Association of Southeast Asian Nations. 2007. *Charter of the Association of Southeast Asian Nations*. Singapore.

⁶ Association of Southeast Asian Nations. 2016. *ASEAN Legal Instruments*. Jakarta.

⁷ ADB and Government of Timor-Leste. Forthcoming. *The Economic Implications of Timor-Leste's accession to ASEAN*. Dili.

⁸ See: Private Sector Assessment (Summary); Finance Sector Assessment (Summary); and Economic Analysis (Summary). Available from the list of linked documents in Appendix 2 of the country partnership strategy.

Government of Timor-Leste has established a Mission Unit to work with officials from Indonesia and Australia to develop a concept for the growth triangle.⁹ ADB's experience supporting other sub-regional integration initiatives is highly relevant to the proposed TIA-GT. A preliminary study by Charles Darwin University provided seven recommendations: (i) that the governments engage the private sector in planning and implementation of the growth triangle; (ii) that the governments support increased people to people links through sporting and cultural events; (iii) that Australia and Indonesia support Timor-Leste's preparations for ASEAN membership; (iv) that each government continue to improve their regulatory environment for business and trade and investment facilitation; (v) that the three governments develop a regional brand and support potential growth industries such as cultural and environmental tourism, and cattle production; (vi) that Australia expand the access granted to migrant workers from Timor-Leste and ENT; and (vii) that the three governments establish mechanisms to share knowledge on aquaculture and fisheries management.¹⁰

iv. Pacific Regional Forums

12. Timor-Leste has been an observer at the Pacific Islands Forum since 2002 and applied for membership in 2014 following a change in Forum rules to allow non-regional members. It is also a member of the Pacific Islands Development Forum, which was established in 2013, and has been an observer at the Melanesian Spearhead Group since 2011.¹¹ Timor-Leste shares some of the development challenges faced by Pacific Island states related to size and fragility and there is scope for mutually beneficial knowledge sharing on issues such as governance, capacity development, economic policy, and natural resource management.

v. The World Trade Organization (WTO)

Timor-Leste's Strategic Development Plan does not target WTO membership. However, WTO membership would complement the current policy objective of ASEAN membership. All ASEAN members are WTO members, and for many ASEAN agreements WTO obligations represent the agreed baseline. For example, several elements of the ASEAN Economic Community (e.g. on non-tariff barriers to trade) are explicitly based on WTO commitments. WTO membership provides a clear signal that a country abides by world trade law, and expects its trading partners to do the same. Membership also provides access to the dispute settlement mechanism if another WTO member is not respecting its WTO commitments. Normally WTO members abide by the rules but the dispute settlement mechanism has been used successfully by small countries. A more common benefit of WTO membership is that it would signal to would-be investors and trading partners that Timor-Leste is committed to abide by world trade law. ASEAN can be seen as WTO-plus with respect to international trade, and ASEAN accession without WTO membership would involve many of the commitments of WTO membership without the corresponding benefits.

C. ADB Experience and Assistance

13. The Asian Development Bank's RCI Strategy identifies 4 pillars for ADB support: i) cross border infrastructure and related infrastructure; ii) trade and investment cooperation and

⁹ Government of Timor-Leste. 2013. *Government Resolution No. 20/2013*. Dili

¹⁰ Charles Darwin University. 2015. *Trilateral Cooperation between Australia, Indonesia, and Timor-Leste Study – Interim Report*. Darwin.

¹¹ J. Santos. 2015. Acting West, Looking East: Timor-Leste's Growing Engagement with the Pacific Islands Region. In R. Azizian, and C. Cramer, eds. *Regionalism, Security & Cooperation in Oceania*. Daniel K. Inouye Asia-Pacific Center for Security Studies. Honolulu

integration; iii) monetary and financial cooperation and integration; and iv) cooperation in regional public goods. ADB's experience and support strategy under each of these pillars is discussed below:

14. **Cross border infrastructure.** ADB has provided grant and loan financing to upgrade the road connecting Dili to the Batugade border post.¹² When completed, these upgrades will reduce the time required to travel between Dili and the border by one third. ADB will continue to support improved transport connectivity from 2016-2020. A loan to finance part of the cost of a new international seaport is programmed for 2017 and further investments in domestic road links are planned.

15. **Trade and investment cooperation and integration.** ADB has provided technical assistance to support regional economic integration with a particular focus on ASEAN membership. This has supported analysis of the legal and institutional reforms that Timor-Leste will need to complete in order to comply with the requirements of the ASEAN Economic Community and establishment of a National Trade Facilitation Committee. ADB is also providing training and capacity building to government officials, and helping the government to analyze and understand the impacts of ASEAN accession and possible linkages with WTO membership. Technical assistance to help the Government of Timor-Leste to prepare for ASEAN accession will continue during the new CPS period. This will include support to build public sector capacity to plan and implement the reforms required for ASEAN accession and participate in ASEAN meetings.

16. ADB's support for ASEAN accession and other trade and investment cooperation will emphasize close coordination to ensure that Timor-Leste leverages the opportunities arising from regional integration. ADB's experience in supporting sub-regional integration initiatives within ASEAN and in Central and South Asia has direct relevance to the plans for trilateral cooperation through the TIA-GT and ADB will ensure that this experience is available to Timor-Leste and its partners. If the Government of Timor-Leste decides to seek WTO membership then ADB will ensure that its support for ASEAN accession and sub-regional integration is also aligned to, and supports, this goal.

17. **Monetary and financial cooperation and integration.** ADB support for activities in this area has been limited due to the relative underdevelopment of Timor-Leste's financial sector.¹³ Moving forwards, ADB will facilitate knowledge sharing with relevant partners in Asia-Pacific as part of its support for financial sector development in Timor-Leste.

18. **Cooperation in regional public goods.** ADB's support for ASEAN accession provides indirect support to Timor-Leste's cooperation in the regional public goods that are organized through ASEAN. ADB has also included Timor-Leste in regional technical assistance projects that support regional cooperation on public goods such as the conservation efforts under the Coral Triangle Initiative. ADB will continue to include Timor-Leste in regional projects that address public good provision and will support Timor-Leste's growing cooperation with countries in both Southeast Asia and the Pacific region.

¹² ADB. 2009. *Democratic Republic of Timor-Leste: Road Network Development Sector Project*. Manila (Sovereign Project 43322-012, \$46.00 million Asian Development Fund grant, approved on 20 November 2009); ADB. 2012. *Democratic Republic of Timor-Leste: Road Network Upgrading Project*. Manila. (Sovereign Project 45094-001, \$30.85 million Ordinary capital resources loan and \$9.15 million Asian Development Fund loan, approved in 30 March 2012)

¹³ Finance Sector Assessment (Summary). Available from the list of linked documents in Appendix 2 of the country partnership strategy.