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East Timor Is Going For Broke As Oil Runs Out

Protesters holding a protest banner chant slogans as they march towards the Australian Embassy building in Jakarta, Indonesia, Thursday, March 24, 2016. Dozens of people staged the rally supporting East Timor in the dispute over maritime boundaries and resource revenue sharing agreements. Credit: AP

East Timor could be bankrupt within a decade unless it takes urgent action to diversify its economy and reassess its fixation with mega-petroleum projects

East Timor was once seen as the poster child for developing nations. It had natural resources, a comprehensive legal framework governing their extraction and an oil fund. But without new sources of income the Southeast Asian state could be bankrupt as early as 2027 , research from Dili-based thinktank La'o Hamutuk shows.

The government's finance ministry is more optimistic, forecasting that its sovereign wealth fund, derived from oil money, will stretch until 2032. But there seems to be some confusion among high-level ministers, including the Prime Minister, Rui Maria de Araújo, about the timelines, as Guteriano Neves, a Timorese post-graduate student at the Crawford School of Public Policy in Australia, highlights in his post Are We The Victims Of Our Own Fantasies?

Significantly, the fledgling nation is almost entirely dependent on petroleum revenues. But its oil and gas income peaked in 2012 and continues to fall. The ConocoPhillips-operated Bayu-Undan project – East Timor's only producing field – has provided about $20 billion over the past 10 years, but the oil money has all but dried up as output is expected to stop sometime between 2020 and 2022.

Still East Timor's government, which hopes to be reelected in 2017, recently issued a press release East Timor's Economic Outlook Positive As Reforms Begin To Show Results and published a similar article East Timor Approaching 2017 Elections With Confidence.

But "the articles, which draw on government, World Bank and IMF sources, portray a rosy outlook for the future of East Timor's economy. Unfortunately, by quoting out of context and ignoring key underlying realities, they paint – like Salvador Dali – a surrealist image very different from the reality facing East Timor as our oil revenues end, investments produce limited income, and planned state spending threatens to exhaust our savings in 10-12 years," La'o Hamutuk said in its article Spinning Straw Into Gold

As La'o Hamutuk highlights, the government press release cherry picked the most flattering aspects of the World Bank and IMF reports, omitting dire warnings about urgently-needed economic diversification in the medium term, unsustainable spending patterns in the state budgets, and the need to analyze large infrastructure projects more carefully.

Indeed, East Timor has moved from dependence on revenues from selling petroleum to dependence on revenues from its Petroleum Fund investments. But the balance in the Fund continues to fall, as the withdrawals are larger than the income.

The proposed 2017 budget of $1.39 billion will require a withdrawal of over $1 billion from the fund, and the government plans to take out almost four times the estimated sustainable income every year between 2018 and 2021, by which time the sovereign wealth fund's balance will have fallen by at least $3 billion, to $13 billion, the NGO warned in a submission to parliament in early November.

Nevertheless, the state budget proposes spending almost $2 billion by 2021 on grandiose plans for a mega-petroleum project, which most experts believe is economically unviable. The whole scheme is dependent on commercializing the Woodside-operated Greater Sunrise oil and gas fields in the Timor Sea. But development of East Timor's last known major oil and gas field, which straddles Australia's seabed, remains indefinitely stalled. A dispute over maritime boundaries with Australia and the treaties that govern the joint development of Greater Sunrise means Perth-based Woodside – and its partners ConocoPhillips, Shell and Osaka Gas – has shelved plans to develop the gas.

Yet the government continues to throw money at its petroleum development fantasies and other dubious infrastructure projects. The amount of money allocated to these projects is much higher than small-scale economic and social spending, in a country where 42% of the people still live in poverty .

"The new sources of income that East Timor desperately needs will not come from unsustainable extractive projects like Greater Sunrise, but from a productive, diverse economy based on East Timor's human and renewable resources," Charlie Scheiner, an analyst at the NGO told me.

La'o Hamutuk's main point, and the goal of its recommendations to cancel unproductive mega-projects, including the petroleum development known as Tasi Mane, is for the focus to shift towards health, education, agriculture, sanitation and water, as well as other sectors that will lay the foundation for a sustainable economy.

"East Timor's response to pressure caused by the imminent end of oil revenues should be to diversify its economy and spend more wisely," adds Scheiner.

Making a quick deal on Greater Sunrise, which could be competitively developed using the existing facilities at Bayu-Undan as production is exhausted, "is not an effective or logical response," said Scheiner.

Jeffrey Feynman, a physics and economics specialist that has consulted on various energy projects in the region, estimates that Greater Sunrise would at best bring in $8.5 billion worth of revenues for East Timor over the 30-year production life of the project, and perhaps less than zero if it were ever developed on East Timor's southern shores, which the government has been striving for . Most experts agree that building a new gas export plant in East Timor is uneconomic and that reusing the existing facilities from the ageing Bayu-Undan fields is far more compelling.

Still, "if current government spending trends continue, $8.5 billion in the 2020s and 2030s could pay for two to five years of state spending, hardly a long-term solution. It's less than half of the amount the country has received from Bayu-Undan, and won't go as far after inflation, population growth and the need to maintain infrastructure and provide services," added Scheiner.

Yet, minister of state and government spokesperson, Agio Pereira, told me that East Timor "is striving for the delimitation of maritime boundaries [..and that] every decision is attached to the process". The government hopes that by shifting its maritime boundary it will take control of Greater Sunrise and realize its vision of processing the oil and gas at home, despite the huge risks involved , rather than using the existing facilities from Bayu-Undan in northern Australia.

Still, there is hope that East Timor's government heeds the IMF's advice that "public investment should be better prioritized, focusing on projects with higher returns determined by rigorous investment appraisal". The World Bank echoes the IMF's warning saying that "East Timor must employ its finite resource effectively and implement key reforms to support a more diversified economy…a combination of marginal investments and high costs also raise important questions of the quality and prioritization of the [infrastructure] programme."

If it does not, then it's hard to avoid the conclusion that East Timor will be a failed state within the next decade.