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SPEECH AT THE EXTRAORDINARY PLENARY SESSION OF THE NATIONAL PARLIAMENT ON

THE RE-ASSESSMENT OF THE NATIONAL PARLIAMENT DECREE No.20/III - GSB FOR 2016

National Parliament
January 8th, 2016

Your Excellency President of the National Parliament,

Your Excellencies Vice-Presidents of the National Parliament,

Honourable Members of Parliament,

Fellow Members of Government,

Ladies and Gentlemen,

People of Timor-Leste.

Still in the spirit of the New Year's festivities, I wish you a good start to this year.

It is with great humility that we come here today, once again, to present the point of view of the Sixth Constitutional Government on the policy that was the foundation to the annual action plan and to the General State Budget (GSB) for 2016, especially on the points of view related with the message delivered by His Excellency the President of the Republic, – addressed to the National Parliament, on December 28th, 2015, requesting the re-assessment of Decree No. 20/III - General State Budget for 2016.

Before presenting the perspective of the Sixth Constitutional Government, with regards to the most prominent points in the veto message of His Excellency the President of the Republic, I wish to remind you that within the context of separation of powers, enshrined in the Constitution of the Republic, the Government is the sovereign body responsible for leading and executing the general policy of the country (Article 103), after obtaining approval from the National Parliament (point a, no. 1, of Article 115). Based on this constitutional mandate, all governments, since the First Constitutional Government, have defined their own guidelines to conduct policy in the country, through their own Programmes, which, after being submitted to this Great House, are implemented through the respective action plans and annual budgets. The Government's responsibility in preparing the plan and the GSB and its implementation after the approval by the National Parliament is defined explicitly in point d, no. 1, of article 115 of the Constitution of the Republic.

Specifically, regarding the Sixth Government, on the one hand, we still remember that the Government Programme was appraised and approved by the National Parliament in March 2015, and that the programme itself represents a continuation of the Fifth Government (though giving emphasis to different aspects of the Fifth Government), and that this programme also attempts to implement a Strategic Development Plan approved in 2011 by the National Parliament itself, to serve as a guide for Timor-Leste's socio-economic development from the year 2011 to 2030. According to the Strategic Development Plan, from 2016 to 2020 Timor-Leste shall enter into the second phase of implementation, which involves three very important lines of action: (1) continuing infrastructure development, (2) consolidating Human Resources; and (3) developing Timor-Leste's economic competitiveness.

On the other hand, these three lines of action, already highlighted in the Strategic Development Plan for the period 2016-2020, have already been incorporated in the Sixth Government's programme and we strive to implement them through the action plan and the annual budget, also reflected in the GSB for 2016. It is precisely the reflection of these three lines of action that determines the priority and the budgetary allocation for 2016.

Mr. President, distinguished Members of Parliament, people of Timor-Leste.

Considering the message of His Excellency the President of the Republic regarding the veto to the GSB for 2016,

First of all, the Sixth Constitutional Government is aware that *the investments that we have currently decided to carry out, must not impair development in the future.* However, the Government believes that there will be no development in the future, if there is no investment today.

The Government understands this concern about the unsustainability of its expenditures, namely due to (1) the oil price continuing to fall and that the projection for the year 2016, according to observers, is based on USD 50/barrel, while the reference price set by the Government in the GSB, for 2016, is higher, amounting to USD 64,70; (2) the GSB having always surpassed the sustainable income, exceeding 100%, and (3) the non-oil revenue having remainedlow for some time now, or "almost stagnant".

It is true that the price of oil varies regularly, however, we must not forget that 90% of the oil wealth of which we know of has already been transformed into financial resources/assets, and that such financial resources, based on the current Government investment policy, attracts annual profits in favour of the Petroleum Fund.

To consider the sustainability of our use of the Petroleum Fund, we also need to take into account the income from oil and gas and the additional income resulting from the investment by the Petroleum Fund, and then comparing them to the amount withdrawn by us, annually, to sustain the GSB. From 2005 to 2014, the funds that entered the Petroleum Fund (coming from the income extracted from oil and gas and adding the profit extracted from investment) were higher than the amount withdrawn to finance the GSB. The existing data shows that we managed to save more than 70%, following the increase in the price of oil. In 2015, on the occasion of the presentation of the Central Bank's report on the income from the investment of the Petroleum Fund and up to the month of December, the amount withdrawn from the Petroleum Fund to finance the GSB was USD 200 million higher than the amount that entered the Petroleum Fund, even though this amount may vary. For 2016, if we use USD 50/barrel as a basis for the estimation (as His Excellency the President of the Republic suggests), such estimate shows that the Petroleum Fund for 2016 will have a total income of USD 1.321 billion (USD 453.5 million from the yield of oil and gas, and USD 867.7 million from the profit of the investment of the Petroleum Fund).

It is true that we have passed the Sustainable Estimated Revenue to the extent that we needed additional financial resources to invest in the areas defined by the Strategic Development Plan, as mentioned above. On the one hand, since 2011 the Government has adopted a policy of '*frontloading*', i.e. anticipate now the expenditure on capital investment, so that, at the beginning of 2020, these will create adequate tax revenues to reduce Timor-Leste's dependency on the Petroleum Fund. To finance such a '*frontloading*' policy, we have to withdraw some of the money from the Petroleum Fund and resort to loans made available by partners – with lower interest rates ~~lower~~ than the interests gained by the financial investments we have made from the Petroleum Fund.

On the other hand, when we analyze the data of non-petroleum revenue, we see that such revenues are not stagnant as, since 2011, for example, and until 2015, the non-petroleum revenue increased from USD 111.7 million to USD 170 million, i.e. in five years there was an increase of 52.1%. This progress is still not the best we can achieve, but demonstrates that the non-petroleum revenue assumes a high potential to become an additional source and significant contribution to finance the socio-economic development of Timor-Leste, provided that there is a serious investment in our economy. The economic and fiscal reforms currently under execution by the Government attempt to (1) further diversify the type of non-petroleum taxes; (2) extend the tax base, i.e. the range of contributing taxpayers; and (3) render a more efficient administration.

Mr. President, distinguished Members of Parliament, people of Timor-Leste.

Another important concern expressed by His Excellency the President of the Republic, in the message to veto the GSB for 2016, focuses on the sustainability of Timor-Leste's development in the future. Such concern was transmitted through a syllogism, or a reasoning model based on deduction, with two premises geared towards a conclusion. The syllogism regarding the sustainability of Timor-Leste's future development is written on page 3 of the message of His Excellency the President of the Republic. I quote:

> *''In a GSB where:*
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> *a) the current State expenditure corresponds to more than two thirds of the total expenditure, and in which*
> *b) nearly half (47%) of the overall financing of the budget is done above the ESI, means that the withdrawals above the ESI are not intended to safeguard the interests of Timor-Leste's future and of the Timorese, but to finance the current functioning of the state machinery.''*

When we look at this deductive thought superficially, we may get the impression that the conclusion is correct, that the GSB proposal for 2016 only safeguards the State machinery and not the future interest of Timor-Leste and of the Timorese, since the Government has proposed the use of 75% of 2016's GSB to sustain the State machinery.

However, if we carefully analyse the Budget Books 1 to 6, we note that:

(1) The Recurrent State Expenditure (i.e. the total amount allocated in the GSB for 2016 intended to sustain the state machinery, namely wages and salaries, part of goods and services, and part of minor capital) does not exceed 29% of the total GSB for 2016. This means that the budget intended to support the State machinery for 2016 is only USD 453.862 million.
(2) The Capital Expenditures and Public Transfers allocated in the GSB represent 71%, i.e. USD 1,108.371 million.
(3) The Estimated Sustainable Income for 2016 is USD 544.8 million, and the estimated non-petroleum revenue for 2016 is USD 171.4 million. These together amount to USD 716.2 million. This means that the Recurrent State Expenditure does not exceed the total Estimated Sustainable Income in conjunction with non-petroleum revenues.

Based on the facts presented beforehand we can conclude that the syllogism, i.e. the deductive reasoning above-mentioned, is not correct, or becomes what is called a "fallacy" in philosophical logic. This means that, when we do not analyze in detail the information contained in Books 1 to 6, the concern with the sustainability of Timor-Leste's development in the future, expressed by the syllogism above, may seem correct, but after a detailed analysis becomes unfounded.

Mr. President, distinguished Members of Parliament, people of Timor-Leste,

His Excellency the President of the Republic also expresses concerns on the way in which we define national priorities and how we invest our resources, which are limited, especially when, according to the perception of His Excellency the President of the Republic, the GSB for 2016 (1) added 24% to infrastructures, particularly in the ZEESM and in the Tasi Mane project, which "allegedly" do not offer guaranteed returns; (2) markedly reduced the budget for health, education and agriculture, and (3) that there is the need to maintain a balance in the development of rural areas.

The Government is aware of such concerns, but would like to clarify the following points:

(1) The increase in the budget for infrastructure is based in the context of a commitment that the State has taken in order to diversify the economy in Timor-Leste. If Timor-Leste does not continue to invest in infrastructure, as a means to invest in the socio-economic investment process, how can we diversify our economy and thus reduce the dependence on the Petroleum Fund?

(2) As was already explained during the debate of the GSB for 2016, in general terms and of each individual section, the return of public investment is not similar to that of private investment. All investments, both public and private, face the dilemma between risk and return, and the decision to invest is usually made on the basis of a good balance between risk and return. A smaller risk is usually associated with a smaller return, and a larger risk is associated with a larger return. A Portuguese popular saying states that: "Nothing ventured, nothing gained", i.e. those who do not want to take the risk will not get the "treat", i.e. will not enjoy the good results. Which risks may affect public investment? Let me mention just three important risks: *inefficiency, wastefulness and corruption.* Are we ready, or not, to face such risks? Good planning will reduce the risk of inefficiency, and good control mechanisms will reduce the risk of wastefulness and corruption. Regarding return, the greatest return on public investment is social return, immediately followed by the economic and fiscal returns, and finally the financial returns. However, in all investments, public and private, it is difficult to predict the scale of the return, in particular financial return. Even with a variety of feasibility studies and methodologies, it is still very difficult to predict an exact financial return.

(3) In what regards the ZEESM, the initial feasibility study carried out before the adoption of Law No. 3/2014 says that the Special Economic Zone in Oecusse-Ambeno (at the time, the social component was not yet included) will need an investment of USD 4 billion during fifteen years, intended for a special economic zone with an area of 170 hectares (within the area of Pante Macassar, including Padiai and Tono). Of this amount, the estimate for private investment is 75%, public investment 25%, and the objective of this public investment is to create adequate conditions regarding roads, electricity, drinking water, port, airport and other infrastructure to attract Foreign Direct Investment. Economic activities within the 170 hectares can also generate, in addition to the social, economic and tax return, from 2030 onwards, a **20% financial perpetuity/year**, or in other words, the assets generated from the investment of USD 4

billion will generate a fixed income of about USD 800 million/year. However, we must update this feasibility study in that it needs to also account for the concept of "social market economy". This means that it should also include the Oecusse-Ambeno territory (with an area of 850 km^2). The spatial planning for the SAROA will be concluded this month and on the basis of this plan, the Strategic Development Plan for ZEESM will be prepared, including Ataúro as a complementary pole of development. This Strategic Plan will identify specific economic investment projects and will carry out feasibility studies for each project. Regarding Ataúro, the spatial plan is ready, and at the beginning of this year, the public investment allocated to Ataúro will concentrate on infrastructure, especially drinking water, electricity and the port. When the spatial plan is approved by the Council of Ministers, it will also serve as the basis for developing a part of the Strategic Development Plan for ZEESM regarding Ataúro, and then feasibility studies will be carried out for each economic activity project already identified in the Strategic Plan.

(4) Regarding the Tasi Mane project, the estimates made by previous governments reveal that public investment, in the next 7 years, will need to reach USD 2 billion, in particular for the construction of the Suai supply base, the highway and the airport, all aimed at attracting foreign direct investment totalling USD 15 billion, for the construction of the LNG plant, refinery, and industrial zone for other complementary industries. Such investments, in addition to the social, economic and tax returns, as per the estimates, create the potential to accumulate income for the State, beginning in the next twenty years, of up to USD 40 billion, through the extraction and processing of oil and gas industries.

(5) If we consider only Timor-Leste's Consolidated Fund, it is correct to say that the budget for 2016 suffered a reduction in health, education and agriculture, compared to 2015. However, if we include the expenditure for the capital allocated to PIMD (previously known as IDDP), the Infrastructure Fund and the Human Capital Development Fund, we can see that for health there is an amount of USD 65.6 million for the year 2016 (while in 2015, USD 67 million were allocated in the Consolidated Fund, where only USD 63 million have been executed); for agriculture, for 2016, the amount is USD 28.1 million (while in 2015 USD 27 million were allocated in the Consolidated Fund, having only executed USD 26 million) and for education, for 2016, USD 112 million were allocated (while in 2015 USD 103 million were allocated in the Consolidated Fund, only USD 102 million have been executed). Under the Government's perspective, the amount or percentage of the amount allocated to such sectors alone should not serve as a single standard in relation to our act of giving, or not, priority to such sectors. The amount allocated should also meet the capacity to execute the allocated funds and to implement the programmes or projects with quality.

(6) The GSB for 2016 allocates 49.8%, or USD 453.8 million in the category of capital expenditure and public transfers to the 13 municipalities. Although this does not ensure, by itself, the balance in the development between the rural and the urban areas, it reveals at least that the allocation of the GSB for 2016 is not concentrated just on the national projects.

Mr. President, distinguished Members of Parliament, people of Timor-Leste,

Another concern transmitted by His Excellency the President of the Republic in its veto message is the elimination of the then Infrastructure Fund, as a special fund, and the creation of the Infrastructure Fund as an autonomous fund. According to the veto message, the creation of this fund does not abide by the legal framework that defines the rules for the transparent functioning of special funds.

The Government understands the concern about the legality and transparency regarding the establishment of the autonomous infrastructure fund, but would like to express its point of view in the following:

(1) The Infrastructure Fund that Decree no. 20/III, The General State Budget, proposes to create **is not a special fund as defined in Article 32 of Law No. 13/2009, of October 21st,** but an autonomous fund, with legal personality, and administrative and financial autonomy.

(2) The importance in creating the autonomous fund, in substitution of the special fund, is that through this autonomous fund we do not need to, annually, re-appropriate the amounts whose execution were not completed until the end of the year. Such a mechanism offers two important benefits: (a) the payment process intended for infrastructure projects can be performed even if we have reached the end of the year and even if the budget has still not been approved and promulgated, a situation that we currently face. It also solves liquidity problems for companies, a common cause for the delay in the implementation of works accross the country; (b) this mechanism will open fiscal space, allowing for budget allocation for areas that require investment. Because every year we have to re-appropriate the amounts whose implementation were not completed before the end of the year, such re-appropriation occupies a "fiscal" space, removing flexibility in budgetary allocation process each year. A concrete example: in 2016, we alocated USD 1 million for the construction and supervision of an irrigation scheme in Larisula. If, by the end of December 2016, the work is only completed up to the amount of USD 600 thousand, we will not need to re-appropriate the remaining USD 400 thousand in the GSB for 2017 to complete this work because the autonomous infrastructure fund will already retain the amount of USD 400 thousand to complete the work. Thus, one may continue to pay the invoices from the company executing the work, even if we were in December 31st, and the start of GSB implementation for 2017 cannot occur in January, a situation that we face today.

(3) Regarding the legality of the establishment of the autonomous infrastructure fund, the Government is of the opinion that: (a) the most appropriate legal instrument to create an autonomous fund is the General State Budget Law, in so far as this autonomous fund represents a financial figure with budgetary impact, and the GSB Law constitutes a more appropriate legislative instrument to define rules and financial and budgetary impacts, also respecting the principle of universality or unity, as in the provisions of article 4 of Law no. 13/2009; (b) the proposal for the creation of this autonomous fund does not contradict Law no. 13/2009 because the proposal complies with the principle of transparency, and the specification of the revenue and expenditure is clearly described in the purpose of the autonomous fund and its global revenues and expenditures are described in Annex II and Annex III, in the part relating to the "Autonomous Services and Funds", according to what is stipulated in the Law no. 13/2009 in article 27; (c) the proposal for the creation of this autonomous fund also ensures its subjection to international accounting standards, and also to the inspection and monitoring budgetary implementation by other sovereign bodies, as per the provisions of Law no. 13/2009, in articles 52 and 53.

Mr. President, distinguished Members of Parliament, people of Timor-Leste, After having presented the Government's position, and with all due respect to the concerns of His Excellency the President of the Republic, expressed through his veto message, I would like to, in the name of the Government, point out that **the budget proposed by the Government for 2016 seeks to use our limited resources toward the sustainable development of our country and improve the living conditions of our population.**

The Government does not dispute the need to invest more in favor of the Timorese, through education and health, as tools for well-being, but the Government is also of the opinion that "more investment" does not just mean an "increase in funds" where, in practice, the institutions responsible for planning, management and implementation of the budget will not be able to absorb and use in a context of implementation with quality.

Lastly, it is true that after thirteen years of the restoration of our independence, together, we can improve and we can do even more, provided that each one of us, abide by the rules as defined in the Constitution.

Let's move forward with confidence, because together we can build the nation from the bottom to bring change to the lives of our people!!!

Thank you for your attention!

Dr. Rui Maria de Araujo
January 8th, 2016