República Democrática de Timor-Leste

State Budget 2021

Budget Overview

Book 1

Book 1 – Budget Overview

Preface

The Organic Law of the Ministry of Finance specifies the responsibility of the National Directorate of Budget to collect and manage financial information relating to the public sector and publish the statistical results.

In accordance with this provision and to promote the transparency of the public finances, the Ministry of Finance is publishing the final version of the documents relating to the 2021 State Budget, following the approval of the Council of Ministers.

The documentation for the 2021 State Budget consists of the Budget Law, plus various supporting budget books:

Book 1	**: Budget Overview**
Book 2	: Annual Action Plan
Book 3A	: Infrastructure Fund
Book 3B	: Municipalities
Book 3C	: RAEOA & ZEESM
Book 4a and 4b	: Budget Line Items
Book 5	: Development Partners
Book 6	: Special Fund - FDCH

Book 1 *Budget Overview* describes the overall budget strategy of the Government. It provides information on the international and domestic economic outlook, expected domestic and oil based revenue including expected sustainable income, and overall expenditure in the medium term and the main new initiatives in the coming year.

Budget documentation is available on the website of the Ministry of the Finance, www.mof.gov.tl. Inquiries relating to this publication should be directed to the General Directorate of Planning and Budget on email jgama@mof.gov.tl telp.+67077852000, syaquim@mof.gov.tl – telp.+67077305809 and spmartins@mof.gov.tl – telp.+67077879183.

I consider that this document will increase awareness and understanding of the Government's finances and help people to become good citizens and heroes to our nation by providing them with relevant information on the 2021 State Budget.

GABINETE DA VICE-MINISTRA
MINISTÉRIO DAS FINANÇAS

Sara Lobo Brites
Acting Minister of Finance

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2.1 Executive Summary

Government Policy

Government policies are organized around four pillars of the Strategic Development Plan: Institutional Framework, Social Capital, Economic Development and Infrastructure Development, where the last three have been designated as priorities in the VIII Constitutional Government's mandate. The proposed 2021 Budget allocates the largest share to the Social Capital Sector, followed by Infrastructure Development, Institutional Framework and Economic Development. The combined source budget for 2021 is set at $2,050.1 million, with $1,895.0 million from government expenditure. The rest is sourced from Development Partners commitments. The different sources of budget expenditure are set out in the table below.

Table 1: Combined Source Budget 2019-2025, $million

	2019 Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Combined Source Budget	**1,405.6**	**1,681.0**	**2,050.1**	**2,499.9**	**2,382.7**	**2,044.5**	**2,167.7**
Government Expenditures by Fund	**1,243.8**	**1,497.0**	**1,895.0**	**2,433.4**	**2,370.7**	**2,035.7**	**2,159.0**
CFTL (excl. loans, inc. EU, inc. social security)	**1,169.6**	**1,426.3**	**1,811.3**	**2,366.0**	**2,310.8**	**1,987.3**	**2,066.8**
Social Security	*35.1*	*41.5*	***42.7***	*44.4*	*46.2*	*48.0*	*50.0*
European Union (Budget Support)	*6.7*	*10.6*	***9.1***	*9.0*	*5.0*	*2.8*	*3.8*
HCDF	17.8	**10.7**	**13.0**	13.5	14.1	14.6	15.2
Borrowing/Loans (disbursements)	49.8	**60.0**	70.7	53.9	45.9	33.8	77.0
Development Partner Commitments	161.8	184.0	155.1	66.5	12.0	8.7	8.7

Source: Ministry of Finance, 2020.

Impact of COVID-19 on Timor-Leste

Timor-Leste recorded its first COVID-19 case on 21st March 2020. There has since been a total of 29 recorded cases in the country, all of which have so far recovered with no deaths. There has been no evidence of community transmission and the last active case was announced on 20th August.

Following the first confirmed case, President of Republic declared a State of Emergency to run from 28th March to 27th April 2020, and this was subsequently extended until now. The first two State of Emergencies aimed to limit public movement through the suspension of public transport and banned large group meet-ups (5 or more people) including religious services, festivals, sporting events, cultural activities and the running of schools/universities. With no local contamination, the subsequent state of emergencies aim to limit movements across border, especially the land border and all returning from overseas have to complete a mandatory 14-day quarantine upon arrival in a quarantine centre. Anyone experiencing COVID symptoms had to self-isolate and submit for testing and international commercial flighs are suspended until now.

The National Parliament approved a total amount of 536.3 million extra-ordinary withdrawal from the Petroleum Fund, with $219.5 million to be set aside for an autonomous COVID-19 Fund where its planning and allocation is coordinated by the Integrated Crisis Management Centre (CIGC), while the Inter-ministerial Committee approved the measures to prevent and combat COVID-19 before it's proceed to final execution approval by the Council of Management for COVID-19. The bill set out broad spending programs and sub-programs level, including $198.3 million for prevention and combating COVID-19. This was focused on the acquisition of essential medical equipment and goods, the creation and maintenance of isolation centres and training for key staff. $4.95 million was used to improve sustainable production and productivity and $17.0 million to provide access to food and non-food services. The remainder of the extra-ordinary withdrawal totalled $316.6 million is used to reinforce the Treasury account during the duo-decimal.

On 17 April, the government announced a 19-measure economic stimulus and response package, including deferral tax payments; a universal cash transfer provided a monthly basic income of $100 to households earning less than $500/month for up to 2 months. So far, 298,495 families have been supported by the scheme; Private sector employees unable to work owing to the state of emergency still received 60% of their salary provided by the government; All electricity consumers (over 160,000 individuals) received a $15 credit per month during the state of emergency; Payment of water bills; social security contributions (workers and employers) and rent of government properties was be suspended; over 4,200 Timorese students currently abroad, unable to return to the country, received a stipend and students unable to attend school in Timor received an internet subsidy to allow them to study online; a 3-month emergency supply of rice was be purchased; and movement of food supplies across the country was subsidized, especially to more remote areas. The package also included the creation of new credit opportunities and a reduction in interest payments. Businesses were provided access to emergency loans to prevent bankruptcy and those importing essential goods were given credit guarantees.

In 2021, the COVID-19 Fund will receive $31.0 million to focus on risk mitigation and recovery measures. $23.9 million will be allocated to Goods and Services, $3.5 million to Public Transfers and $3.6 million to Capital development.

Petroleum Fund Revenue

The Petroleum Fund remains the main source of funding for the state budget. The amount withdrawn is categorised into the ESI amount and any excess withdrawal that is justified by the Government to be in the long-term interests of Timor-Leste. Calculating the ESI requires projecting the Fund's value at the beginning of the budget year along with the present value of future petroleum revenue. The assumptions for Budget Book 2021 are largely the same as Budget Book 2020, although investment returns and petroleum revenue for 2020 are now higher to reflect the year to date figures. As a result, the expected value of the Fund at the end of the year has risen and the ESI for 2021 is $547.9 million, an increase of $12.3 million. Withdrawals to fund the 2021 Budget are projected to be $1,377.6 million or 7.6% of Petroleum Wealth, exceeding the 2021 ESI by $829.7 million.

The Fund's balance was $18,469.5 million as at September 2020. Investment income for the year until September was $906.5 million, which translates into a return of 5.2%. Petroleum receipts until September are $290.4 million. The Fund is expected to end 2020 at $18,065.7 million, However, The end of year balance is uncertain and depends largely on the performance of equity markets and withdrawals to finance government expenditure in the final quarter.The Fund's value is expected to continue to decline over the budget projection period and beyond.

Petroleum receipts will be very low compared to previous years as Bayu-Undan's reserves deplete further and investment returns are not expected to offset withdrawals.

Economic Growth

Becoming an upper middle income country by 2030 requires strong, high-quality non-oil economic growth. Public investment seen from 2008 to 2018 through the frontloading fiscal policy has driven growth in the non-oil economy, averaging at 4.7% per year. This was aimed at providing necessary foundations for long-term sustainable private sector led development. . Preliminary GDP projections for 2019 indicate that GDP was positive, recovering from the recent previous 2 years of contraction, indicating growth at around 2.0%.

Economic growth is expected to contract by -6.0% in 2020 due to COVID-19 and the delayed budget, but is expected to return to positive growth of 3.9% in 2021. This return to growth is driven by an end to political uncertainty and return to strong government expenditure. Meanwhile, inflation is expected to remain low and stable at 0.7% 2020 and 2.1% in 2021.

Expenditure

Total expenditure in the 2021 budget is $1,895.0 million (excluding donor funded activities of $155.1 million). The total 2021 State Budget (excluding donor funded activities) is 27.0% higher than that allocated for 2020.

Table 2: Fiscal Table, $millions

	2019 Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Total Expenditure (incl. loans)	**1,243.8**	**1,497.0**	**1,895.0**	**2,477.8**	**2,416.9**	**2,083.8**	**2,209.0**
Total (excl. loans)	**1,194.0**	**1,437.0**	**1,824.3**	**2,423.9**	**2,371.0**	**2,050.0**	**2,132.0**
Recurrent	922.6	1,274.7	**1,359.9**	1,414.3	1,470.9	1,529.7	1,590.9
Salary and Wages	203.0	206.7	**239.3**	248.8	258.8	269.1	279.9
Goods and Services (incl. HCDF)	380.4	499.3	**421.5**	438.3	455.9	474.1	493.1
Public Transfers (incl. social security)	339.3	568.7	**699.1**	727.1	756.2	786.4	817.9
Capital	314.6	222.3	**535.1**	1,019.1	899.9	506.0	568.1
Minor Capital	27.8	8.9	**61.2**	63.6	66.1	68.8	71.5
Capital and Development (including loans)	286.8	213.4	**474.0**	955.5	833.7	437.2	496.6
Revenue	**727.6**	**716.7**	**738.5**	**728.7**	**691.1**	**650.0**	**620.8**
Domestic Revenue	198.6	172.3	**190.6**	202.1	212.1	218.7	229.0
Estimated Sustainable Income (ESI)	529.0	544.4	**547.9**	526.6	478.9	431.3	391.8
Fiscal Balance	**(516.2)**	**(780.3)**	**(1,156.5)**	**(1,749.1)**	**(1,725.9)**	**(1,433.7)**	**(1,588.2)**

	2019 Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Financing	**529.9**	**780.3**	**1,156.5**	**1,749.1**	**1,725.9**	**1,433.7**	**1,588.2**
Excess Withdrawals from the PF	440.0	419.5	**829.7**	1,686.2	1,675.0	1,397.1	1,507.4
Use of Cash Balance	33.4	290.1	**247.0**	-	-	-	-
Cash Balance of Treasury	33.4	214.1	**150.0**	-	-	-	-
Cash Balance of RAEOA/ZEESM	-	76.0	**97.0**	-	-	-	-
Borrowing/Loans (disbursements)	49.8	60.0	**70.7**	53.9	45.9	33.8	77.0
European Union (DBS)	6.7	10.6	**9.1**	9.0	5.0	2.8	3.8

Source: Ministry of Finance, 2020.

Fiscal Sustainability Analysis

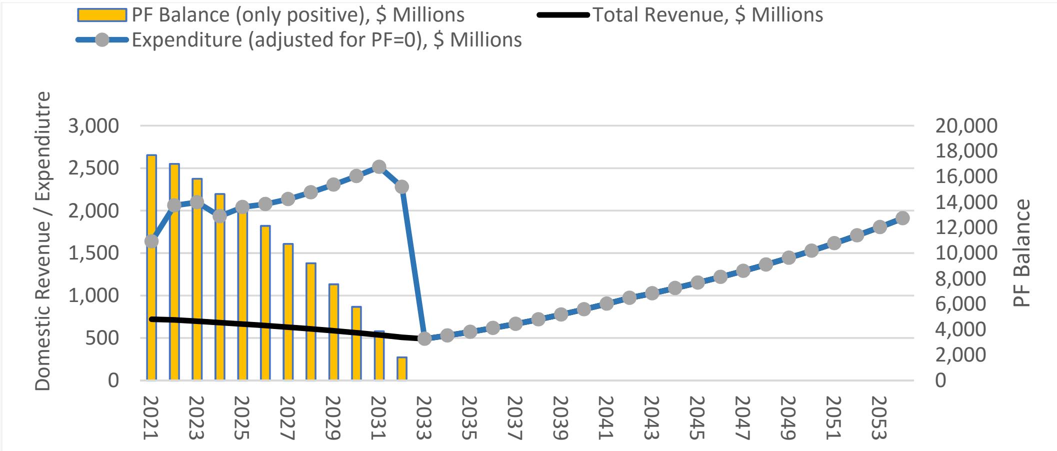
The economy of Timor-Leste is currently highly dependent on the Petroleum Fund for financing the fiscal deficit. The current government policy is one of front-loading expenditure, running high government budgets in the short run to finance capital spending for Human Development and key infrastructure, with the aim to encourage development of the private sector, increase diversification and grow the overall economy. A stronger non-government Timorese economy would require less funding from the Petroleum Fund in the future as the fiscal deficit would be smaller due to higher non-oil domestic revenues and a lower need for government spending to boost the economy in normal times.

The Ministry of Finance conducts a fiscal sustainability analysis for the budget ceiling chosen each budget cycle. Through the use of modelling, the impact of the selected budget ceiling on the long term sustainability of Timor-Leste can be estimated, specifically the overall balance of the Petroleum Fund. The model used mainly focuses on the impact of capital spending on longer-term GDP and domestic revenues and their bearing on the Petroleum Fund reserves.

Under the expenditure scenario set out in this budget book (see Table 1), the growth rate of all appropriation categories grows at 4%. The only expectation is Capital and Development which is estimated to adjust following requested amounts set out by the Infrastructure Fund in the years 2021-2025 and a long term growth rate linked to inflation after that.

Under this fiscal ceiling, as well as the selected assumptions, the model estimates that the Petroleum Fund would run out in 2033, 13 years away.

Figure 1: Expenditures, Revenues and Petroleum Fund Balance Forecasts 4% Growth Scenario 2021-2040, $millions



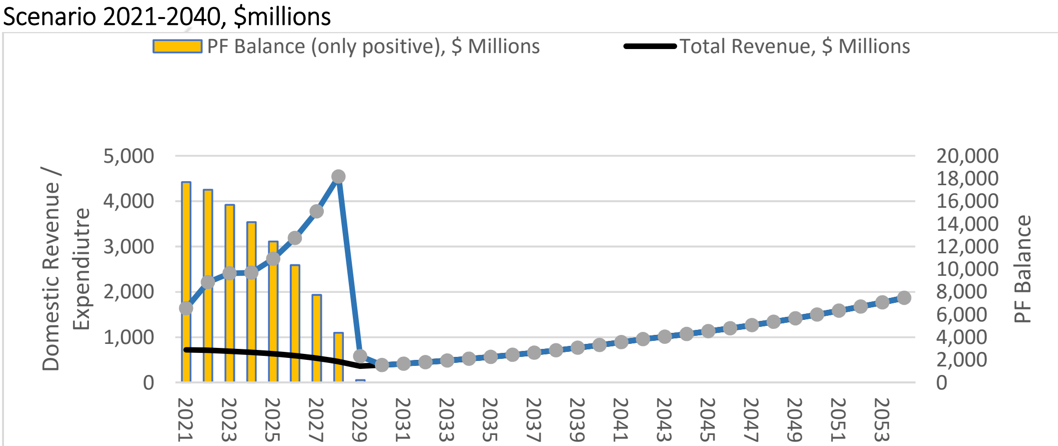
Source: Ministry of Finance, 2020.

As the Fund begins to get close to zero, expenditure would have to fall rapidly in order to match domestic revenues as that would be the only source of income (excluding external debt). The model estimates this would be mean an 80% fall in expenditure in two years (2031-2033), falling from $2.5 billion to $491 million (when expenditure must equal domestic revenue).

If revenues do not rise as quickly as the model forecasts, the fall in expenditure would have to be even greater. Therefore it is vital that mobilisation of domestic revenues is a key focus of the government over the coming years.

However the growth in spending has often been higher than 4%. The average growth rate of approved budget spending (not adjusted for execution) across all appropriation categories (including loans but excluding contingency expenditure) between 2010 and 2019 was 20.9% per year. This masks significant variation between categories with Minor Capital seeing the largest annual growth (46.7%) and Goods and Services the smallest (7.9%). Using the historic growth rates, rather than the 4% assumption, the model estimates that the Petroleum Fund would run out in 2030, 10 years away. This is 3 years earlier than the previous scenario.

Figure 2: Expenditures, Revenues and Petroleum Fund Balance Forecasts Historic Growth Scenario 2021-2040, $millions



Source: Ministry of Finance, 2020.

The model estimates this would be mean a 92% fall in expenditure in two years (2028-2030), falling from $4.5 billion to $386 million (when expenditure must equal domestic revenue).

It is important to state that the model does not factor in any effect to GDP when the Petroleum Fund balance hits zero, or close to it. This seems unlikely as the associated fall in expenditure would likely cause an economic downturn, with a fall in consumer and private sector spending and a decline in GDP. This downturn would also have an effect on domestic revenues, further decreasing possible expenditure.

Domestic Revenues

The forecast for 2021 see domestic revenues totalling $190.6m including RAEOA-ZEESM taxes by the end of the year and $187.3m excluding RAEOA-ZEESM. This is a near return to 2019 collections which were $191.7m. Non-oil receipts are set to grow year-on-year from 2021 nearing $230m by 2025, provided that macro-economic conditions hold. The implementation of new fiscal policy reforms would boost this forecast even higher.

It should be noted that from 2021 EDTL will be classified as a Public Enterprise, this will allow it greater autonomy and therefore their revenues will no longer be part of the General Government Account. However, we will continue to forecast revenues for public enterprises to better compare revenues between years. For 2021 EDTL represents around 17% of domestic revenue, excluding EDTL domestic revenues are forecast to stand at $157.5m. The impact of this restructure is discussed further in section 2.4.1.6.

Financing

The fiscal deficit is equal to revenue minus expenditure. The Government uses excess withdrawals from the Petroleum Fund (PF), loans, the cash balance of Treasury and RAEOA/ZEESM and Budget Support from European Union to finance the deficit in 2021. The total amount of excess withdrawals to be taken from the PF (i.e. the amount withdrawn exceeding the ESI) in 2021 is $829.7 million.

Loans are becoming an increasingly important tool for financing in the Government of Timor-Leste. The current loans contracted by the Government of Timor-Leste are used to finance key infrastructure projects and have relatively low rates of interest and significant grace periods. Total loan financing for 2021 is $70.7 million.

The total use of the cash balance for 2021 State Budget is $247.0 million, of which from the Consolidated Fund of Timor-Leste (CFTL) is $150.0 million and from RAEOA/ZEESM is $97.0 million.

Total Budget Support from European Union for 2021 State Budget is $9.1 million. This is a new source of financing introduced independently for Budget 2020. It is included as its own line item as the support will be used directly by Governmental institutions.

Loans and Public Private Partnerships (PPPs)

At present, external loans are provided by international multilateral banks such as the Asian Development Bank and the World Bank, with one bilateral loan from JICA. These have a considerable degree of concessionality and compare favorably to the opportunity cost of withdrawing funds from the petroleum fund.

At the end of 2019, debt stock increased to $192.2m. Considering the COVID-19 outbreak, fall in disbursement is expected in 2020 as construction projects may suffer delays. At the end of Q3 2020, loan disbursements were $213.4m. This is expected to rise again in 2021 as the country recovers from the COVID-19 economic downturn. There are currently 15 ongoing road projects funded by concessional loans of which 8 projects had already been completed. Other projects that are most likely to be concluded by 2020/2021 bringing the total numbers of projects completed to nearly 70%.

Infrastructure development is expected to continue playing a key role in the country's economic development in the medium to long term. Strategic sectors such as water, education, telecommunication, and air transports should receive concessional financing. This would help unleash the growth potential of other key economic activities, leading to inclusive economic growth and poverty reduction. The Government is therefore proposing an estimated ceiling of $400m for new concessional foreign loans to be negotiated in 2021.

There are a number of PPPs projects that are currently ongoing. These are the Tibar Bay Port PPP which is in the Implementation and Operation Stage, the Medical Diagnostic PPP which is in the procurement and negotiation stage and the Affordable Housing PPP, Cristo Rei PPP and Presidente Nicolau Lobato International Airport which are in Feasibility Stage.

Note: The 2021 Budget draft law includes a proposal for a US $20 million celling for the possible issuance of public debt bonds, in addition to the US $400 million celling of concessional loans, for a combined public debt ceiling of US $420 million, depending on the approval of the Government bonds legal framework during 2021.

Development Partners

Development Partners' support is forecast to experience a 15.7% decrease in 2021, as compared to 2020 planned disbursements, with a forecast total of $155.1m. This fall is due to a significant increase in 2020 as development partners increased their backing to aid Timor-Leste in its quick and effective response to COVID-19.

2.2 Economic Overview

2.2.1 Summary

Table 3: Economic Indicators, 2020-2022, %

Summary	**Forecast**		
	2020	**2021**	**2022**
Real GDP (non-oil)	-6.0%	3.9%	2.5%
Inflation CPI	0.7%	2.1%	2.7%

Source: Ministry of Finance, 2020. [1]

- Real non-oil GDP growth is expected to contract by 6% in 2020 due the combined effect of the Budget being delayed, political uncertainty, COVID-19 and the State of Emergency.
- 2021 is due to see GDP return to positive growth of 3.9% as a result of a rebound in private investment and household consumption.

[1] *Please note GDP forecast will be updated to reflect updated National Accounts 2019 data when released*

- Inflation is expected to remain low and stable at 0.7% in 2020 and 2.1% in 2021. This will positively contribute to increasing Timor-Leste's competiveness, with inflation expected to be lower than the regional average.
- Between August 2019 and August 2020 the US dollar appreciated slightly by 0.3% against a weighted basket of currencies of Timor-Leste's trading partners (the nominal effective exchange rate, NEER). There has been a small overall appreciation in the last few years which has reduced the price of imports, placing downward pressure on domestic inflation, benefiting Timorese consumers. However, this appreciation also makes Timorese non-oil exports more expensive in international markets constraining the development of the country's exports.
- The exchange rate forecast suggests a small depreciation with Timor-Leste's trading partners in the medium term, 2021 to 2024, which should provide a boost to competitiveness.

2.2.2 Macroeconomic Trends

2.2.2.1 Growth

Table 4: Real GDP 2010 - 2018

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Real GDP ($m)	1294.8	1370.0	1452.4	1483.3	1549.3	1596.7	1653.3	1590.5	1578.1
Real GDP Growth (%)	9.5	5.8	6.0	2.1	4.5	3.1	3.6	-3.8	-0.8

Source: Ministry of Finance, 2020. [2]

Timor-Leste

In 2018, non-oil real GDP in Timor-Leste decreased by -3.8% to $1,578.1m. National Accounts data exist up to 2018, which is the latest year of GDP data available without forecasting.

Timor-Leste experienced GDP growth, averaging 3.3% per year over 2010-2018. These growth rates have been driven by increases in government expenditure associated with the government's economic strategy to ensure that Timor-Leste has the necessary infrastructure to allow the private sector to flourish in the long-run. The Government's economic strategy uses loan financing and excess withdrawals from the Petroleum Fund to finance high quality investment in infrastructure and human capital development. As outlined in Timor-Leste's Strategic Development Plan, the Government's high return investments will provide the necessary foundations for long-term sustainable private sector led development. Government investment has enabled a significant upgrade to road and electricity coverage throughout Timor-Leste, which has helped to improve both living standards and the business environment.

Non-oil GDP growth in 2019 shows signs of recovery from the recent episodes of negative growth (-3.8% in 2017 and -0.8% in 2018). The contraction was a consequence of declines in government expenditure, private sector investment, and lower exports. Political uncertainty also led to lower development partner spending and reduced business activity. coffee harvest,

2 NA 2000-2018 correct as of October 15th 2020. Historical GDP figures will be updated when National Accounts 2019 are published.

3 EIA's Short-Term Energy Outlook, released on September 9, 2020. www.eai.gov.

the main source of exports, was affected by a poor season. The preliminary forecast for 2019 indicates a return to growth of around 2.0%. This is largely due to political stability, boosting business activity and household consumption. In 2020, the impact of the State of Emergency due to the global COVID-19 pandemic, coupled with the delayed budget has led to GDP forecast of a contraction of -6.0%.

International

Table 5: Growth Indicators, 2018-2021, %

Country	Actual		Forecast	
	2018	2019	2020	2021
World	3.6%	2.9%	-4.9%	5.4%
Advanced Economies	2.2%	1.7%	-8.0%	4.8%
Emerging and Developing Economies	4.5%	3.7%	-3.0%	5.9%
Emerging and Developing Asia	6.3%	5.5%	-0.8%	7.4%
China	6.8%	6.1%	1.0%	8.2%

Source: IMF World Economic Outlook, 2020.

Global growth outlook is projected to contract by –4.9% in 2020, this is more pessimistic than the -3.0% forecast in April 2020. Advanced economies are now forecast to shrink the most by -8.0%, while growth for emerging markets and developing economies is forecast to fall -3.0%. The fall in global growth was driven mostly by the outbreak of COVID-19. The U.S. economy is projected to contract this year by -8.0%. However, China will maintain positive growth of 1.0% in 2020.

Global growth is expected to rebound to 5.4% in 2021, the advanced economy group is forecast to grow at 4.8%, while growth for the emerging market and developing economy group is forecast at 5.9%. However, the rebound in 2021 is uncertain and depends on how fast the pandemic will fade. A lot of effort have been done in accommodating the public health requirements around the world to prevent the spread of the virus, nonetheless this policy limited the economic activity and the financial system which is contributed to the decline in growth in 2020. Nevertheless high levels of growth, especially in Asia, still provides a solid foundation for Timorese exporters and economic development. The international environment provides favourable conditions for Timor-Leste to take advantage of in 2020 and beyond.

2.2.2.2 Prices and Inflation

Table 6: Global and Regional Inflation Rates, 2018-2021, %

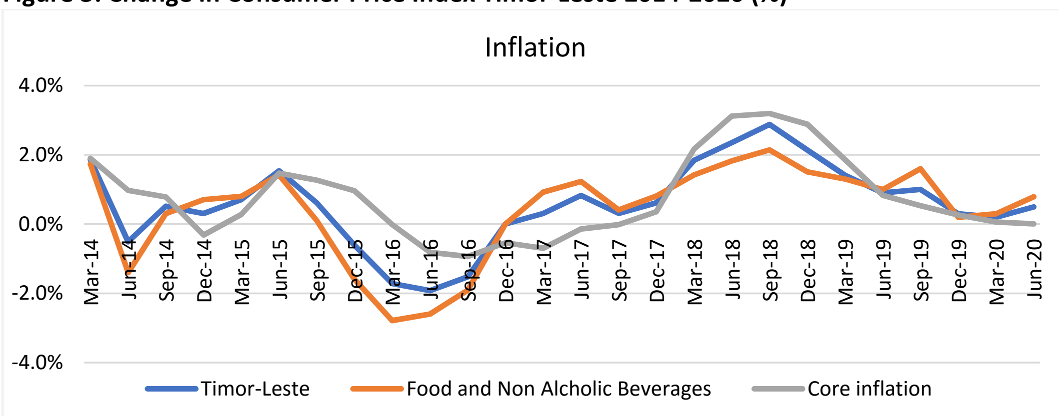
Country	Actual		Forecast	
	2018	2019	2020	2021
World	3.6%	3.6%	3.0%	3.3%
Advanced Economies	2.0%	1.4%	0.5%	1.5%
Emerging and Developing Economies	4.8%	5.0%	4.6%	4.5%
Emerging and Developing Asia	2.6%	3.2%	3.0%	2.9%
Timor-Leste*	2.3%	0.9%	0.7%	2.1%

*Source: IMF World Economic Outlook, April 2020. *Ministry of Finance forecast, 2020.*

Timor-Leste

With year on year inflation in August 2020 of 0.6%, Timor-Leste still enjoys a low level of inflation. Due to the significant weight of food and non-alcoholic beverages in the CPI basket and the high proportion of food imported into Timor-Leste every year, international food prices remain one of the key drivers of the overall CPI rate, and the MoF continues to monitor price levels. The World Bank (WB) food price index has remained stable between May 2019 and May 2020 increasing just 0.5%. Domestic food prices have also been muted seeing a small increase of just 0.8% in the same timeframe. It is expected that the current world food prices will fall slightly in 2020 and then experience a small uptick in 2021 but remain stable. Rice specifically is a staple part of the Timorese diet. The benchmark Thai 5% rice is expected to increase 8% in between 2019 and 2020 and 2% between 2020 and 2021, this will have a negative effect on poorer households where basic foods make up the majority of their spending and this will leave them with less disposable income. Coffee prices (both Arabica and Robusta) are expected to decrease 3% and 7% respectively in 2020 but increase by 2% and 3% respectively in 2021 compared to 2020. This will positively affect those families who rely on coffee production in Timor-Leste.

Figure 3: Change in Consumer Price Index Timor-Leste 2014-2020 (%)



Source: Ministry of Finance, 2020.

International

Global inflation forecast at 3.0% by the IMF in 2020. The decline in the commodity prices especially lower oil prices have contributed to the sharp falls in consumer price inflation in the advanced economies. However, the inflation is projected to soften in the coming years. For the emerging market economies, inflation has been rising reflecting the impact of currency depreciation and higher commodity prices, but it is projected to moderate as the impact of tighter monetary policy and recent declines in oil prices. Low inflation in Timor-Leste in this context will tend to help improve competitiveness.

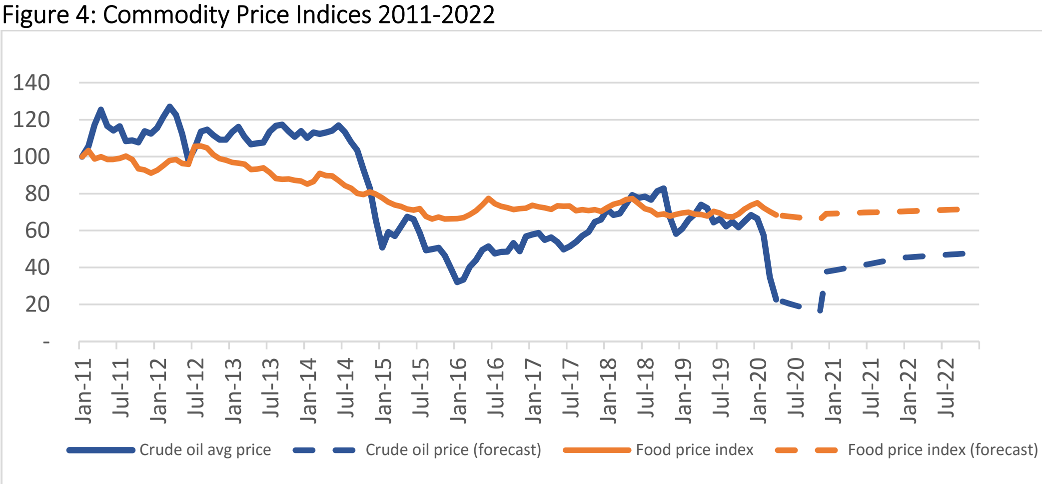
Oil prices

Oil prices are important to Timor-Leste both for consumers, through consumer prices, and as an oil exporting country. The average international price of Brent oil has witnessed dramatic declines since June 2014 from highs of $112 per barrel to lows of $32.2 per barrel in January 2016. The decline in oil prices was driven by the increased global supply during a period of low global demand. Following this prices had started to recover with oil prices for 2019 averaging at $64 per barrel. However, global demand for oil has drastically declined since the onset of the COVID-19 pandemic. Since the beginning of January 2020, many governments' around the world imposed restrictions on travel and temporary business closures to stem outbreak. Oil prices fell to $21/barrel in April 2020, however, the average is expected to be slightly above $40/barrel for 2020, down 33% from 2019. Prices are expected to rise to $50/b in 2021.

Agricultural Commodity Prices

A significant portion of the food consumed in Timor-Leste is imported and thus changes in international food prices can have a significant impact on both the rate of inflation and standard of living. According to the World Bank Commodities Price Index, international food prices have continued to decline from a high of 105.8 in August 2012, though prices had been stable averaging at 73 and 70 in 2018 and 2019 respectively. The World Bank is forecasting that food prices will fall marginally in 2020 and then recover in 2021 and 2022, however the increase is small, and overall food prices are expected to remain stable. Rice specifically is a staple part of the Timorese diet. The benchmark Thai 5% rice is expected to increase 8% in between 2019 and 2020 with a further increase of 2% in between 2020 and 2021, from $86/mt in 2020 to $88.mt in 2021, this will have a negative effect on poorer. Coffee prices (both Arabica and Robusta) are expected to decrease 3% and 7% respectively in 2020 but will experience a slight rebound with an increase of 2% and 3% respectively in 2021 compared to 2020 (Arabica from $2.8/kg to $2.85/kg, Robusta from $1.5/kg in to $1.54/kg) . This will positively affect those families who rely on coffee production in Timor-Leste.

Figure 4: Commodity Price Indices 2011-2022



Source: Ministry of Finance, 2020.

2.2.2.3 Exchange Rates and Competitiveness

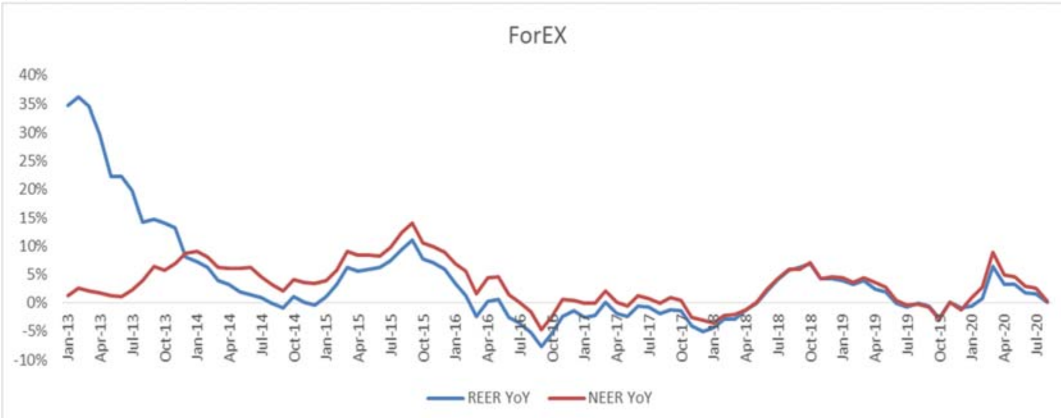
Between August 2019 and August 2020 the US dollar appreciated by 0.3% against a weighted basket of currencies of Timor-Leste's trading partners (the nominal effective exchange rate, NEER). There has been a small overall appreciation in the last few years which has reduced the price of imports, placing downward pressure on domestic inflation, benefiting Timorese consumers. However, this appreciation makes Timorese non-oil exports more expensive in international markets constraining the development of the country's exports sector.

An inflation-adjusted measure of the exchange rate, the real effective exchange rate (REER), is a better measure of competitiveness. If inflation in Timor-Leste is lower than in other countries, this can help mitigate exchange rate appreciation. In fact, the REER appreciated just 0.1 %

between August 2019 and August 2020, driven by the exchange rate changes captured in the NEER and lower inflation in Timor-Leste compared to its neighbours over the last year.

The inflation rate in Timor-Leste is expected to be lower than its neighbours in the near future, and so Timor-Leste can expect an improvement in competitiveness. This will help the Timorese export market be well-placed in the international market. While this is to be welcomed, the government is not complacent about the issue of competitiveness. A key priority is improving the business environment to encourage improved competitiveness, and the inflation target policy is a part of meeting the priority.

Figure 5: Exchange Rate Indices 2013-2020 (%)



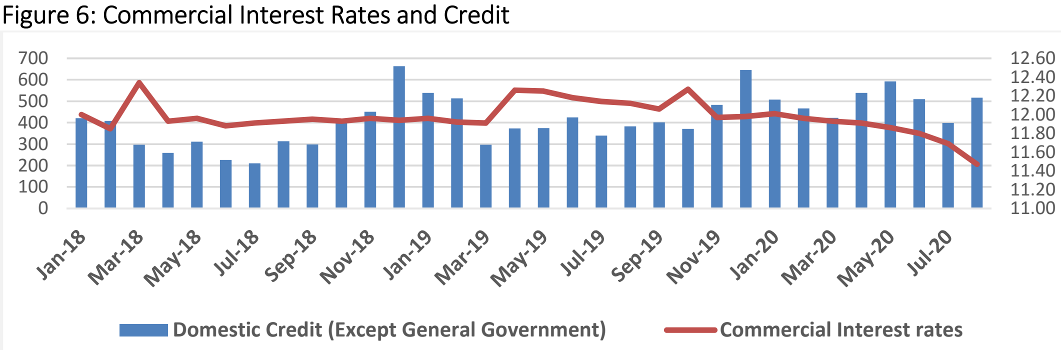
Source: Ministry of Finance, 2020.

2.2.3 Financial Sector Trends

Commercial Interest Rates and Credit

The amount and cost of credit to the private sector is an important indicator for private sector development. Loans to the private sector were at an average interest rate of 11.47% in August 2020, these have declined from 12.12% the same time last year. Total domestic credit, excluding general government, was $517 million in August 2020, with an average of $429 million over the prior 12 months. Please note: The commercial interest rate between January 2017- July 2020 has retrospectively been revised down as the Central Bank of Timor did not previously include BRI (Bank Rakyat Indonesia) in their calculation of the weighted average of commercial interest rates.

Figure 6: Commercial Interest Rates and Credit



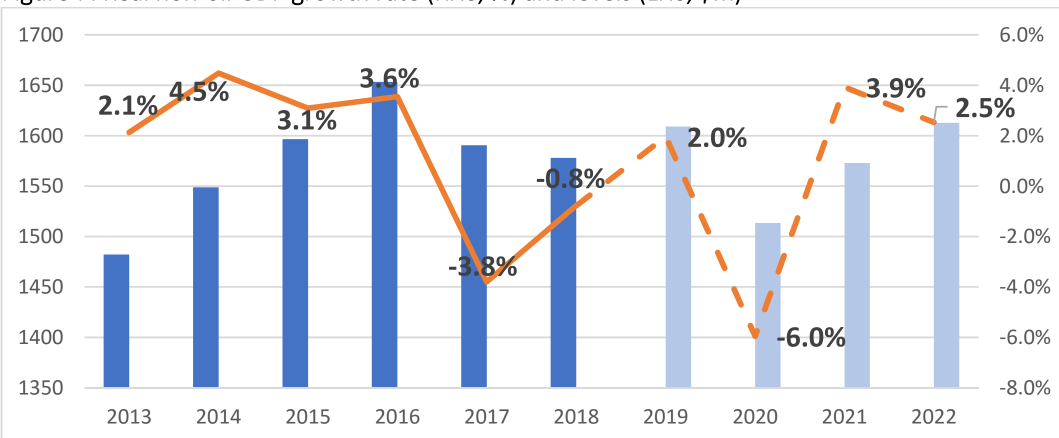
Source: Banco Central Timor-Leste, August 2020. Interest Rate (RHS, %), Credit (LHS, $m).

2.2.4 Economic Outlook

The Ministry of Finance is forecasting non-oil GDP growth to be -6.0% for 2020. This is due to the delayed Budget approval which restrains public spending and political uncertainty which has a negative impact on the private sector along with the impact of the COVID-19 crisis and associated state of emergency. 2021 is due to see GDP return to positive growth of 3.9% as a result of a rebound in private investment and household consumption. This forecast reflects historic data from National Accounts 2000-2018 and will be updated accordingly when the National Accounts 2019 are published.

Over the medium term, Ministry of Finance expects return to positive sustainable growth based on political stability and private sector investment.

Figure 7: Real non-oil GDP growth rate (RHS, %) and levels (LHS, $m)



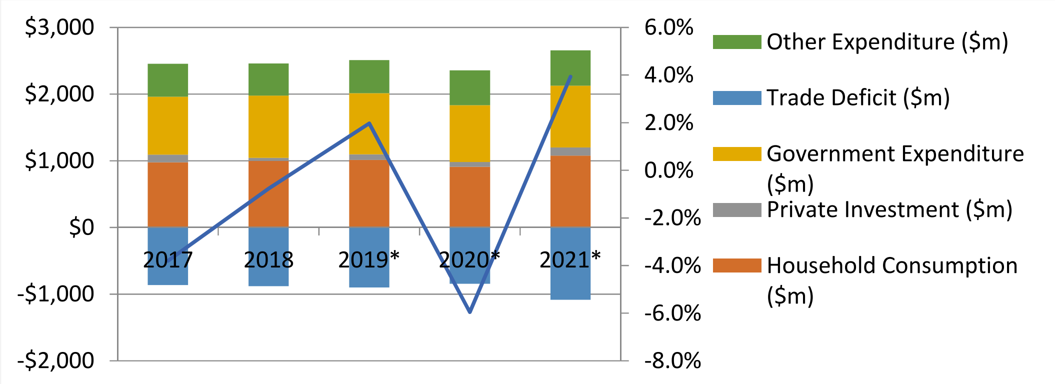
Source: Timor-Leste National Accounts 2000-2018; 2019-2022 Economic Forecasts, Ministry of Finance, 2020.

The negative impact of COVID-19 and the state of emergency on living standards will be lessened due to the various government policies aimed at assisting the most vulnerable during the crisis including the payment of 60% for the employment salary and stabilising credit line to maintain the purchase power and capacity of the private sector. Consumption is likely to fall during 2020 particularly during the months of the State of Emergency. A low inflationary environment due to the fall in world oil prices will help consumption to some extent, but the increase in the cost of rice will hit the poorest the most.

Public sector investment in 2020 was somewhat constrained by the duo-decimal system. However, the new coalition should provide the political stability for the Budget to be approved for 2021 providing greater momentum for public infrastructure projects, especially in education, health, and water and sanitation. These projects will also provide jobs for Timorese people. The infrastructure assets resulting from this public investment as well as legal reform will create an environment conducive to strong growth in the private sector, boosting growth into the future. In addition, 3 year Economic Recovery Package aims to stimulate the recuperation of the economy post-COVID-19 crisis.

In the short and medium term one will see continued construction on the Tibar Bay Port, and the expansion of existing and new commercial projects throughout the country. Such investments are consistent with the Government's economic strategy, alongside continued investments in human capital and education, to attract investors and consequently creating jobs domestically.

Figure 8: Components of non-oil GDP, 2017- 2021



*Source: Timor-Leste National Accounts 2000-2018; 2019-2021 Economic Forecasts, Ministry of Finance, 2020.*indicates forecast*

Table 7: Non Oil Real GDP, 2016-2022, $million

2015 $m prices	2016	2017	2018	2019*	2020*	2021*	2022*
Private Consumption	976	1,011	1,037	1,044	945	1,110	1,151
Public Consumption	927	873	864	959	1,047	969	997
Total Consumption	1,902	1,883	1,901	2,003	1,992	2,079	2,149
Private Investment	126	143	70	109	100	155	197
Public Investment	527	401	465	386	260	421	382
Total Investment	653	544	535	495	360	576	579
Other	26	26	23	12	6	3	1
Total National Expenditure	2,582	2,454	2,459	2,510	2,357	2,657	2,729
Exports	53	32	35	32	31	45	50
Imports	(981)	(896)	(916)	(933)	(875)	(1,129)	(1,166)
Non-oil GDP	1,653	1,590	1,578	1,609	1,513	1,573	1,613

Source: Timor-Leste National Accounts 2000-2018; 2019-2020 Economic forecast, Ministry of Finance, 2020. P (preliminaria), P** (projection).*

Risks, Uncertainty and Assumptions

Economic forecasts or projections aim to predict annual GDP growth rates and high level macroeconomic figures. Making forecasts about what macroeconomic variables may be in the future is important to help governments and businesses make decisions with regard to policies, planning and investment. However, it is important to understand that in order to make these predictions, we have to make some assumptions about future conditions. Therefore all projections always include an element of uncertainty. The main uncertainties in the forecast come from imports and government budget execution. If government spending is particularly import-dependent, meaning that much of the new spending goes to goods and services from outside Timor-Leste, the GDP forecasts for future years may be reduced downwards as imports have a negative effect on final GDP.

In addition, if there is a large change in execution rates this may have a noticeable impact on the economy, especially given that the state budget makes up a large portion of Timor's GDP. Execution rates differ each year for different reasons and also depend on the absorptive capacity of the Timor-Leste economy.

2.3 National Development and Priorities

Six areas are defined as priorities for the 2021 Budget and of the remainder of the Government's mandate, 2021-2023:

2.3.1 Government Priorities for 2021

Table 8: Priorities of the VIII Government, 2021

No.	Priority
1	Social Capital Development
2	Economic Development
3	Development of Basic Infrastructure
4	Development and Protection of the Environment
5	Institutional Development
6	Reform to Key Pillars

The proposed budget allocations aim to reflect, therefore, such priorities which are described below.

Social Sector Development

- Create education and training opportunities which are of quality, inclusive and which respond to the needs of the economy.
- Continue to prepare the health sector in terms of quality and service delivery especially in response to the COVID-19 pandemic.
- Improve drinking water and sanitation infrastructure to ensure quality of life, health and prevention of disease.

Economic Development

- Focus on recovery of the economy following the economic downturn due to the impacts of COVID-19 in 2020.
- Facilitate investment in the private sector, prioritising small and medium size enterprises.
- Create employment options to increase national productivity and opportunity for all.
- Increase agricultural productivity and food security by improving and creating new infrastructure, distribution channels and storage of agricultural products.
- Diversify the economy and increase the growth rate in an inclusive and sustainable manner, following government priorities.

Development of Basic Infrastructure

- Develop ports, airports, roads both urban and rural
- Development of logistical capacity both land, waterway and air

Development and Protection of the Environment

- Promote sustainable behaviour and environment
- Emphasise the principle of reduce, reuse and recycle

Institutional Development

- Consolidate defence and foreign affairs institutions
- Consolidation of external relations

Reform to Key Pillars

Make improvements in the following sectors:
- Pubic Administration
- Judicial Reform
- Fiscal and Public Finance Management Reform.

2.3.2 Economic Recovery Package (ERP)

In addition to the priorities above, on 12th August, the Government approved an Economic Recovery Package with the objective of aiding the recuperation of the economy post COVID-19 between 2021 and 2023. The plan had 3 clear objectives:
- Increasing employment: ensuring all jobs are both productive and dignified
- Realisation and consolidation of public social investment programmes (Education, Health, Housing and Social Protection)
- Review productive sectors and promote areas that contribute to economic growth

The final Economic Recovery Package is $123.9 million. This includes both ongoing activities as well as additional economic recovery measures for LM/SFA/Ms if they provide essential services/contribute to essential activities. The Ministry of Finance has also mapped existing/new donor support received which will be detailed in Budget Book 5 2021.

Table 9: Budget and Implementing Institutuion of PRE in 2021

Implementing institutions of FRE	Total
Municipal Administration of Aileu	396,836
Municipal Administration of Ainaro	441,029
Municipal Administration of Covalima	442,008
Municipal Administration of Lautém	430,907
Municipal Administration of Liquiçá	450,288
Municipal Administration of Manatuto	382,691
Municipal Administration of Manufahi	404,586
Municipal Administration of Viqueque	501,466
Municipal Authority of Baucau	654,847

Implementing institutions of FRE	Total
Municipal Authority of Bobonaro	548,625
Municipal Authority of Dili	652,458
Municipal Authority of Ermera	694,259
National Center For Employment And Vocational Training	41,000
Public Service Commission	17,200
National Hospital Guido Valadares	1,739,000
National Health Institute	235,290
Ministry of State Administration	31,416,640
Ministry of Agriculture And Fisheries	5,177,675
Ministry of Education, Youth And Sport	31,711,000
The Ministry of Justice	2,067,000
Ministry of Health	12,651,000
Ministry of Public Works	21,503,286
Ministry of Tourism, Commerce And Industry	2,185,000
Ministry of Transport And Communication	3,042,000
Ministry of Coordinating Economic Affairs	340,000
Secretariat of The Professional Training Employment	1,354,000
Secretariat of Cooperative	3,500,000
Secretariat of State for Environment	540,000
Business Regisration and Verification Service	438,000
Total	**123,958,091**

Economic Development: , promote sustainable livestock production, improve access to microcredit, create mobile training, organize career fairs, research on potential employment, organize technical vocational and professional training, promote of small and micro businesses, develop new web services for tourism promotion, create a new tourism authority and tourism zone, increase production and diversification of agricultural products, improve business registration services, improve access to seeds and machinery, etc.

Social Capital: Reforestation and rehabilitation of degraded areas (including community rural resource management programme), develop water supply systems for agriculture, build additional CAFÉ schools and ESG buildings, improve teacher training programs for the various teaching degrees (INFORDEPE), construct health posts, capacity build health professionals, integrate traditional and allopathic medicine through legal means, construct specialized clinics, provide a line of credit to universities, etc.

Institutional Framework: Approve associated regulations of land law, prepare regulatory frameworks for the business environment, increase functionality of the legal system, further decentralization of administration, public administration reform, etc.

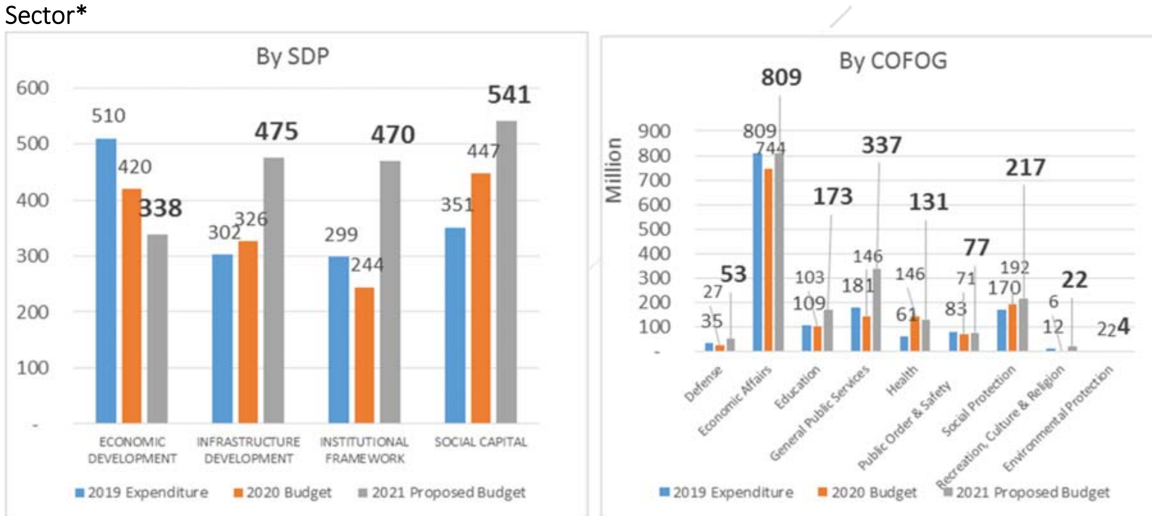
Infrastructure Development: Create tourist and cultural infrastructure areas, improve basic sanitation, bio-fuel and new storage methods, construct and rehabilitate infrastructure at the municipality level, establish industrial centers, etc.

2.3.3 Analysis of the 2021 Proposed General State Budget

Timor-Leste's Strategic Development Plan is organized around four pillars: Institutional Framework, Social Capital, Economic Development and Infrastructure Development, where the last three have been designed as priority in the VIII Constitutional Government's mandate. The proposed 2021 Budget allocates the largest share to the Social Capital Sector, followed by Infrastructure Development, Economic Development, and Institutional Framework. However this is excluding loan disbursements. Note that Infrastructure Development and Economic Development both contribute to Economics Affairs under COFOG classification.

Following instead the international sectorial and more detailed classification COFOG (see Figure 9), it can be observed that the Economic Affairs sector remains the largest, in line with previous year, followed by General Public Services, Social Protection, Education, Health, Public Order and Safety. However it should be noted that the COFOG classification breaks down the SDP Social Capital sector into Social Protection, Health, Education and Recreation, Culture and Religion.

Figure 9: Comparison of 2019 Expenditure, Budget 2020 & Proposal Budget 2021 budgets by Sector*



*Source: Ministry of Finance, 2020. *This does not include loans.*

2.4 Revenues

2.4.1 Overview of Revenue Projections

Non-oil domestic revenues are expected to rise in 2021, in comparison to the sharp decline in 2020. 2020 is expected to see a 10.1% fall from collections in comparison to 2019.This is due to the impact of COVID-19, both directly through the State of Emergency as well as other knock-on effects of the pandemic. While it is still unclear how long the impact of COVID-19 will affect both the global economic system as well as the internal Timorese economy, current forecasts predict that 2021 will see a 10.6% rise in domestic revenue collections as the economy bounces back from the COVID-19 induced recession. This is a significant increase from forecast 2021 revenues in the previous budget which has predicted a 6.5% rise in comparison to 2020 revenue estimates. The key driver for this rise is the higher than originally estimated government expenditure for 2021 and the related growth in forecast GDP.

Future projections of non-oil domestic revenues are expected to grow positively year-on-year. Greater private sector activity, political stability and the continuation of government capital projects will also help to promote revenue growth. The positive trend is expected to continue until 2025, given current macro-economic growth expectations.

Timor-Leste is highly dependent on oil revenue which represented nearly 80% of total revenue in 2019. However, petroleum revenues are expected to decline as production from existing field draws to a close. 2021 is the first year in recent years where domestic revenues will make up the majority of total revenues. This makes Fiscal and Public Financial Management Reforms a priority for the country going forward. Overcoming the tax base issue, improving revenue collection capacity, introducing new fiscal instruments as well as reviewing the existing ones, revisiting tax policies and legislation that promotes investments could help lead to increased revenue collection, considerably improving both fiscal and non-fiscal revenues.

It is important to note that future year forecasts do not include additional revenue from such reforms, as these are still to receive Parliamentary approval.

Table 10: Total Revenue, 2019 – 2025, $million

	2019 Actual	Proj 2020	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Total Revenues	**947.9**	**478.5**	**258.7**	**234.8**	**320.8**	**218.7**	**229.0**
Domestic Revenues	191.7	172.3	**190.6**	202.1	212.1	218.7	229.0
Petroleum Revenues (excl investment return)	756.3	306.1	**68.1**	32.7	108.7	-	-

Source: Ministry of Finance, 2020.

Domestic Revenues

Domestic revenues are composed of tax revenues, fees and charges, interest on cash balances and revenues from autonomous agencies and special administrative regions. The effect of the change in structure of EDTL from part of the Ministry of Public Works to a public enterprise has included in the given forecasts. The potential impact to domestic revenues will be explored in its own section, 2.4.1.6.

Table 11 breaks down domestic revenues into these categories showing actual and forecasted amounts between 2019 and 2025**.**

Table 11: Domestic Revenue 2019 – 2025, $million

	2019 Actual	Proj 2020	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Total Domestic Revenue	**191.7**	**172.3**	**190.6**	**202.1**	**212.1**	**218.7**	**229.0**
Taxes (excluding RAEOA-ZEESM)	122.3	110.5	**123.6**	133.2	138.0	141.3	148.1
RAEOA-ZEESM Taxes	3.9	3.2	**3.3**	0.4	4.4	4.6	4.7
Fees and Charges	56.4	51.3	**54.3**	55.2	59.5	62.3	65.1
Interest	0.63	0.53	**0.58**	0.59	0.57	0.58	0.57
Autonomous Agencies and Special Administrative Regions	8.4	6.8	**8.8**	9.0	9.7	10.1	10.6

Source: Ministry of Finance, 2020.

2.4.1.1 Tax Revenues

Tax revenues consistently comprise the largest source of domestic revenues in Timor-Leste, totalling 64% of total domestic revenues in 2019. This is estimated to continue in 2021, with total tax revenues (including RAEOA-ZEESM taxes) making up 66.6% of total domestic revenues based on the current forecasts. Tax projections are summarized in Table 12 and are divided into Direct Taxes and Indirect Taxes. The table does not include RAEOA-ZEESM taxes as those have not been forecast at the line item level. Total RAEOA-ZEESM taxes can be found in Table 11.

2020 tax collection is expected to fall significantly in comparison to 2019, an estimated 10.1% fall. This is largely due to the State of Emergency and other spill over effects of the global pandemic. Indirect taxes, those levied on goods and services, are effected the most. Excise tax, the largest single contributor to domestic revenues, is estimated to fall by around a fifth compared to collections in 2019. Sales tax and import duties are expected to fall by 12.8% and 10% respectively. Withholding tax, the second largest tax contribution, is forecast to rise slightly in comparison to 2019. This is due to an extremely high collection in January 2020, 2.5 times collections in January 2019, due to delayed payments at the end of 2019. Corporate taxes are also forecast to increase due to high collections during the first half of the year, particularly in Q1. At the end of Q3 2020, tax revenues equalled 77.2% of the forecast revenue for the year. The highest two taxes are excise and corporate taxes which equal 82.9% of their total, implying that their total for the year may be higher than estimated, while the lowest is Public Sector income tax at 58.3% which may suggest the final collection for the year will be lower than its forecast. In 2019, the total cumulative tax revenue at the same point in the year was 73.9% of total tax collections for the year.

Forecasts for 2021 see a significant rise in tax revenues, rising an estimated 11.8% compared to 2020 estimates, though they are still expected to just exceed their pre-COVID-19 levels. Comparing 2019 collections and 2021 forecasts, tax revenues are just 1% higher.

Direct taxes are expected to see a smaller rise in 2021, due to their smaller decline in 2020. Indirect taxes are usually the main drivers of growth and forecast to rise 15.4% in comparison to 2020 estimates. The largest rise is expected by Excise and Sales taxes, the ones that are also predicted to fall the most in 2020, thought there are still not expected to exceed their pre-COVID-19 levels until 2023.

Future years are expected to see a rise in tax revenues, driven by a stable macroeconomic and political environment. The positive trend is expected to continue through 2025. The large increase in capital expenditure in 2022 and 2023 sees Withholding tax, the tax commonly linked to capital projects, rise significantly during the same period. Additional reforms in the tax collection systems, with the shift to SIGTAS (Standard Integrated Government Tax Administration System) 3.0, should enhance the Tax Authority's capacity to enforce greater tax compliance. However it is important that other tax instruments are explored during this time period, to increase the tax base of the country and help ensure fiscal sustainability in the medium and long term.

Table 12: Total Tax Revenue, Actuals and Projections 2019 – 2025, $million

	2019 Actual	Proj 2020	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Total Tax (excluding RAEOA-ZEESM)	**122.3**	**110.5**	**123.6**	**133.2**	**138.0**	**141.3**	**148.1**
Direct Taxes	51.2	50.7	**54.6**	63.1	62.4	62.2	65.3
Income Tax	20.5	18.6	**19.8**	20.1	21.7	22.7	23.7
Individual Income (Public Sector)	7.2	7.4	**6.9**	7.0	7.6	7.9	8.3
Individual Income Other	13.2	11.2	**12.9**	13.1	14.1	14.7	15.4
Corporate Tax	8.7	9.7	**10.4**	10.6	11.4	11.9	12.5
Withholding Tax	22.0	22.4	**24.4**	32.4	29.3	27.6	29.1
Indirect Taxes	71.1	59.8	**69.0**	70.1	75.6	79.1	82.7
Service Tax	3.7	3.6	**3.8**	3.8	4.1	4.3	4.5
Sales Tax	15.3	13.4	**15.1**	15.3	16.5	17.3	18.1
Excise Tax	38.3	30.3	**36.3**	36.9	39.8	41.6	43.5
Import Duties	13.9	12.5	**13.8**	14.1	15.2	15.9	16.6

Source: Ministry of Finance,2020.

2.4.1.2 Fees and Charges

Fees and charges include a wide selection of categories from non-tax sources that contribute to domestic revenue. These comprise administrative fees, utility payments and royalty payments to the Government from natural resources other than petroleum. Fees and charges historically make up around 30% of total non-oil domestic revenues. In 2021, they are forecast to make up 28.5%.

Fees and Charges in 2020 are estimated to fall 9.1% compared to those collected in 2019. This is because of the impact on electricity payments, the largest contributor to revenues and often making up over 60.6% of total collections. Electricity payments were heavily hit during Q2 2020, the introduction of the subsidy during the state of emergency, deceasing 30% compared to the previous year. Due to this overall collections for electricity are expected to fall around a quarter in 2020 compared to the total for 2019. Other significant drivers, such as property rentals, visa fees and social games receipts, are also expected to fall. A large dividend from BCTL is one of the few line items expected to rise, with a 50.8% increase from the amount collected in 2019.

Forecasts for 2021 see a significant growth in collections, with a growth rate of 5.9% compared to 2020 projections. This is a lower rate of growth than other contributors to domestic revenues. However the overall amount is not predicted to exceed 2019 levels until 2023. Electricity fees and charges are forecast to continue to be the largest contributor, making up 60.6% of the total. Other line items expected to be significant are BCTL payments, property rentals and mining and quarry royalties.

Projections for outer years are expected to see a positive trend given the current forecasts of GDP growth in 2022 and beyond. Growing decentralization of collections has also seen the introduction of non-fiscal instruments in the municipalities through advertising and parking services. Further decentralization, improvements and reinforcement of collection mechanisms in line ministries and the introduction of new non-tax instruments are expected to boost collections. Contributions from transport, property rentals, dividends and social games fees and charges are forecast to return to a stable growth path from 2021.

Please note, future projections continue to include payments from EDTL through electricity fees and charges and new installations. When EDTL becomes a public enterprise, their revenues will be held internally and therefore will no longer be a part of the central government account. This will cause a significant reduction in fees and charges collections, as well as domestic revenues overall. The potential effects will be explored in more detail in 2.4.1.6.

Table 13: Fees and Charges, Actuals and Projections 2019 – 2025, $thousands

		2019 Actual	**Proj 2020**	**Proj 2021**	**Proj 2022**	**Proj 2023**	**Proj 2024**	**Proj 2025**
Collecting Ministry	**Total Fees and Charges**	**56,443.0**	**51,307.9**	**54,312.5**	**55,191.2**	**59,515.4**	**62,253.1**	**65,116.8**
Ministry of Finance	Other Non-Tax Revenues of Customs	479.3	717.0	**739.7**	751.6	810.5	847.8	886.8
Ministry of Finance	Customs Service Fees	4.4	3.3	**4.0**	4.0	4.4	4.6	4.8
Ministry of Finance	Customs Penalties	5.3	3.9	**3.7**	3.8	4.1	4.3	4.5
Ministry of Finance	Late Payment Interest Sales	5.2	3.9	**4.0**	4.1	4.4	4.6	4.8
Ministry of Tourism, Commerce and Industry	Commercial License Fees	22.8	5.0	**18.3**	18.6	20.0	21.0	21.9
Ministry of Transport and Communication	Postage Fees	25.8	21.6	**26.4**	26.8	28.9	30.3	31.7
Ministry of Justice	Property rentals	4,249.3	2,691.2	**3,956.7**	4,020.7	4,335.8	4,535.2	4,743.8
Ministry of Public Works	Water Fees	145.8	135.1	**207.8**	211.2	227.7	238.2	249.2
Ministry of Transport and Communication	Vehicle Registration Fees	1,408.3	1,178.8	**1,345.2**	1,367.0	1,474.1	1,541.9	1,612.8
Ministry of Transport and Communication	Vehicle Inspection fees	781.7	648.7	**801.6**	814.6	878.4	918.8	961.1
Ministry of Transport and Communication	Driver License Fees	523.4	288.0	**536.7**	545.4	588.1	615.2	643.5
Ministry of Transport and Communication	Franchising Public Transp Fees	227.4	190.3	**233.2**	237.0	255.6	267.3	279.6
Ministry of Transport and Communication	Transport Penalties/Trajectory	133.5	97.7	**136.9**	139.2	150.1	157.0	164.2
Ministry of Transport and Communication	Other Transport Fees	51.8	158.0	**175.7**	178.6	192.6	201.4	210.7
Ministry of Justice	Passport & ID	1,658.1	898.1	**1,304.3**	1,325.4	1,429.3	1,495.0	1,563.8
Ministry of Interior	Visa Fees	3,041.2	1,439.1	**1,985.3**	2,017.4	2,175.5	2,275.5	2,380.2

		2019 Actual	Proj 2020	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Courts	Tribunals - Fines & Penalties	435.7	496.6	**446.8**	454.0	489.6	512.1	535.6
Ministry of Transport and Communication	Vehicle Inspection Imported	62.7	51.3	**64.3**	65.4	70.5	73.7	77.1
Ministry of Public works	Electricity Fees & Charges	32,674.0	23,998.7	**32,936.9**	33,469.8	36,092.1	37,752.4	39,489.0
Ministry of Transport and Communication	TL Internet Domain Revenue	281.8	180.9	**259.5**	263.6	284.3	297.4	311.1
Secretary State Vocational Training and Employment	Fines & Forfeits	451.2	229.3	**260.2**	264.4	285.1	298.2	311.9
Ministry Petroleum Resource and Minerals	Mining & Quarry Ops. Royalty	2,401.7	1,802.2	**2,332.9**	2,370.6	2,556.4	2,674.0	2,797.0
Ministry of Finance	Bid Document Receipts - Ministries	147.4	26.7	**74.1**	75.3	81.2	84.9	88.8
Ministry of Finance	Auctions	468.0	16.8	**435.5**	442.6	477.3	499.2	522.2
Ministry of Tourism, Commerce and Industry	Social Games Receipts	1,626.8	880.5	**1,000.2**	1,016.4	1,096.0	1,146.5	1,199.2
Ministry of Tourism, Commerce and Industry	Rent of Government Property	51.1	68.6	**52.4**	53.2	57.4	60.0	62.8
Ministry of Agriculture and Fisheries	Forestry Products	93.4	80.9	**95.7**	97.3	104.9	109.7	114.8
Ministry of State Administration	Sanitation Services Fee	9.9	9.8	**10.2**	10.3	11.1	11.7	12.2
Ministry of Health	Registration of Health Professionals	22.3	15.3	**22.9**	23.2	25.0	26.2	27.4
Ministry of Education	Polytechnic Institute of Betano	65.6	74.7	**67.3**	68.4	73.7	77.1	80.7
Presidency of the Council Ministers	Printing Fee - PCM	147.0	162.1	**150.8**	153.2	165.2	172.8	180.8
Ministry of Health	Pharmaceutical Fee	45.9	39.7	**46.5**	47.3	51.0	53.3	55.8
Ministry of Finance	BCTL Dividends	4,342.1	6,549.8	**4,034.0**	4,099.3	4,420.5	4,623.8	4,836.5

		2019 Actual	Proj 2020	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Ministry of Finance	Other Non-Tax Revenue	157.2	134.1	**124.0**	126.0	135.8	142.1	148.6
Ministry of State Administration	Dili Municipality - Advertising Revenue	123.8	148.0	**172.5**	175.3	189.0	197.7	206.8
Ministry of State Administration	Ainaro Municipality - Advertising Revenue	2.5	3.0	**3.0**	3.1	3.3	3.5	3.6
Ministry of State Administration	Covalima Municipality - Advertising Revenue	6.5	1.4	**6.7**	6.8	7.3	7.7	8.0
Ministry of State Administration	Baucau Municipality - Advertising Revenue	4.1	1.2	**4.2**	4.3	4.6	4.8	5.1
Ministry of State Administration	AM Ermera- Advertising Revenue	4.5	8.9	**5.7**	5.8	6.2	6.5	6.8
Ministry of State Administration	Aileu Municipality - Advertising Revenue	1.1	1.4	**1.1**	1.2	1.3	1.3	1.4
Ministry of State Administration	Dili Municipality - Parking Fee	22.2	21.9	**30.7**	31.2	33.6	35.2	36.8
Ministry of State Administration	Administrative Sanctions and Fines	2.5	1.7	**2.6**	2.6	2.8	2.9	3.1
Ministry of Public Works	EDTL Receipts - New Installation	28.6	173.1	**192.2**	195.4	210.7	220.3	230.5

Source: Ministry of Finance, 2020.

2.4.1.3 Interest

Interest reflects interest payments received from cash held in Government funds. 2019 saw a growth in interest rates and cash balances held by the government, meaning interest reached a high of $0.62m. This expected to fall in 2020 as interest rates across the world decline. Collections are expected to remain relatively stable over the next 5 years, ranging between $0.56m and $0.61m.

Table 14: Interest Receipts, Actuals and Projections 2019 – 2025, $thousands

	Proj 2019	Proj 2020	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Interest Receipts (all funds)	626.7	528.9	**584.8**	592.4	569.4	582.3	571.5

Source: Ministry of Finance, 2020.

2.4.1.4 Autonomous Agencies and Special Administrative Region

The number of autonomous agencies has been increasing steadily in recent years, reflecting government's desire to grant greater financial independence to institutions to improve their efficiency. In 2021, they are forecast to make up 4.6% of total collections

Autonomous Agency collections are expected to fall 10% in 2020, in comparison to collections in 2019. This is largely due to a fall in Port charges due to restrictions on goods movement during the state of emergency. Revenues from of National University Fees by UNTL expected to fall slightly, as well as receipts from IGE. These reductions are forecast to be off-set by increased collections by CLN from sale of local product and rice and Licensing Fees from ANC.

In 2021, collections from autonomous agencies and RAEOA-ZEEMS fees and charges are expected to rise 16.8% compared to those forecast in 2020. This is driven by a rise in collections from APORTIL.

Bamboo Centre is expected to rise significantly due to increased demand in line with the strategic plan and a return to historic rates. CLN – Sale of Local Product, IGE receipts, AIFAESA fees and SENAI Centre revenues are also all predicted to see large proportional increases to return to their pre-COVID-19 levels. Future years expect to see a growth in revenues even further as the economy recovers from lockdown and the global effects of COVID-19.

Table 15: Autonomous Agencies and Special Administrative Region, Actuals and Projections 2019-2025, $Thousands

	2019 Actual	**Proj 2020**	**Proj 2021**	**Proj 2022**	**Proj 2023**	**Proj 2024**	**Proj 2025**
Total Autonomous Agencies	**8,405.1**	**6,809.8**	**8,828.5**	**8,982.4**	**9,660.9**	**10,105.3**	**10,570.2**
CLN - Sale of Local Product	360.2	107.9	**216.1**	219.6	236.8	247.7	259.1
ANC - Licensing Fee	1,462.4	1,389.7	**1,520.9**	1,545.5	1,666.6	1,743.3	1,823.5
APORTIL - Port Charges & Fees	3,517.0	2,657.9	**3,583.8**	3,641.7	3,927.1	4,107.7	4,296.7
IGE - Receipts	407.4	222.1	**416.8**	423.5	456.7	477.7	499.7
SAMES - Receipts	-	27.7	**34.4**	34.9	37.7	39.4	41.2
UNTL - National University Fees	1,213.0	1,153.1	**1,524.7**	1,549.3	1,670.7	1,747.6	1,828.0
HNGV - Hospital & Medical fees	249.7	278.0	**325.2**	330.5	356.4	372.7	389.9
Bamboo Centre Tibar - Revenue	-	0.5	**51.6**	52.5	56.6	59.2	61.9
AMRT - Fees	3.6	3.9	**3.7**	3.7	4.0	4.2	4.4
IADE Service Fees	3.0	2.4	**3.1**	3.1	3.4	3.5	3.7
AIFAESA Fees	87.0	52.0	**89.2**	90.6	97.7	102.2	106.9
SENAI Centre - Revenue	-	1.5	**2.0**	2.1	2.2	2.3	2.4
SERVE IP - Revenue	-	61.6	**68.4**	69.5	74.9	78.4	82.0
CLN - Sale of Rice	365.1	180.4	**232.0**	235.7	254.2	265.9	278.1
ZEESM - Fees and Charges	736.9	671.2	**756.7**	780.0	815.8	853.4	892.6

Source: Ministry of Finance, 2020. ZEESM revenue includes fees and charges only, tax revenue is presented separately in table 11.

2.4.1.5 EDTL

As mentioned previously, EDTL revenues consistently make up over 60.6% of fees and charges, often contributing over 60.6%. Fees and charges are around 28.5% of total domestic revenues.

The move to make EDTL a public enterprise will allow it greater autonomy and the ability to take its own decisions regarding policy decisions including future planning. However it also mean that they get greater control of their revenues which will become independent of Central Government, kept in their own private account and no longer part of the General Government Account. This will cause a significant fall in domestic revenues. For instance in 2021 projections, revenues excluding EDTL contributions are 17.3% lower. This trend continues across the 5 year time horizon given.

Table 16: Impact of EDTL Structure change to Domestic Revenues 2021 – 2025, $million

	Proj 2021	Proj 2022	Proj 2023	Proj 2024	Proj 2025
Total Domestic Revenue	**190.6**	**202.1**	**212.1**	**218.7**	**229.0**
Total Domestic Revenue excluding EDTL Revenues	**157.5**	**168.5**	**175.8**	**180.8**	**189.3**
Electricity Fees and Charges	*32.9*	*33.5*	*36.1*	*37.8*	*39.5*
EDTL Receipts - New Installation	*0.19*	*0.20*	*0.21*	*0.22*	*0.23*

Source: Ministry of Finance, 2020.

2.4.2 Petroleum Fund Revenue

The Petroleum Fund remains the principal source of financing for the state budget each year. The total withdrawn from the Fund can be broken down into the Estimated Sustainable Income (ESI) and any excess withdrawal that is justified by the Government to be in the long-term interests of Timor-Leste. This section presents the ESI calculation for 2021 along with the underlying assumptions. It also describes the Fund’s investment strategy, its performance and projections for the Fund over the budget period.

2.4.2.1 Calculating Petroleum Wealth and the ESI for 2021

Withdrawals from the Fund are guided by the ESI. The ESI represents the maximum amount that can be withdrawn from the Petroleum Fund in a fiscal year so as to leave a sufficient Fund balance for an amount of the equal real value to be appropriated in all later years. The ESI is set to be 3% of the Petroleum Wealth, which comprises the balance of the Fund and the Net Present Value of future petroleum revenue.

The Petroleum Wealth (PW) and the ESI are usually only updated once a year as part of the main budget process. The ESI 2020 was recalculated in August 2020 as part of the new Budget Book 2020. Some of the key assumptions had changed significantly since the first estimate in September 2019, including the opening balance of the Fund, production, costs and oil price. The 2021 Budget Book was prepared shortly after the 2020 Budget Book and generally shares the same assumptions, as explained below.

Total Petroleum Wealth on a Net Present Value basis is estimated to be $18,262.4 million on 1 January 2021. This is $410 million higher than the figure previously calculated in the 2020 Budget, which is caused by an upward revision to expected petroleum revenues and investment returns in 2020. Table 17 shows the estimated Petroleum Wealth and the ESI from 2019 and onwards, assuming that withdrawals from the Fund are equal to the projected withdrawals in this budget book. The ESI for 2021 is $547.9 million. The ESI estimates for the following financial years decline as a result of the projections for continued excess withdrawals.

Table 17: Petroleum Wealth and the Estimated Sustainable Income (ESI) $milion

	2019*	2020*	2021	2022	2023	2024	2025
Estimated Sustainable Income (PWx3%)	529.0	544.4	547.9	526.6	478.9	431.3	391.8
Total Petroleum Wealth (PW)	17,633.6	18,145.1	18,262.4	17,552.6	15,964.9	14,376.7	13,059.9
Opening PF Balance	16,489.6	17,691.8	18,065.6	17,417.7	15,858.2	14,376.7	13,059.9
Net Present Value of Future Revenues	1,144.0	453.2	196.8	134.9	106.7	0.0	0.0

*Source: Ministry of Finance, 2020. *ESI for 2019 and 2020 figure as estimated in Budget 2019 and 2020.*

The key assumptions behind the calculations are set out in Table 18 and discussed below.

Table 18: Key Assumptions behind the ESI Calculation in 2021

Asset recognition	Forecast petroleum revenues are included only for projects with approved development plans. Bayu-Undan (BU) is the only operating field.
Petroleum Reserves and Production Forecasts	The project operator provides production estimates. The Operator provided 3 scenarios in August 2020 for Low, Base, and High forecasts. The average of the Low-Base case production is used for both ESI 2020 and ESI 2021.
Oil price forecast	Brent crude oil has been shown to be the best indicator of the price of BU liquid products, namely condensate and LPG. ESI for Budget 2020 and 2021 is prepared using the average of the Energy Information Agency's (EIA) Low case and Reference case for Brent in its Annual Energy Outlook (AEO) for 2020, released in January 2020.
Prices for specific petroleum products	BU produces condensate, Liquefied Petroleum Gas (LPG) and Liquefied Natural Gas (LNG). Forecast assumptions for condensate and LPG are derived from historical differentials observed with Brent. The historical relationship has been relatively stable, with condensate averaging about 95 percent and the LPG averaging about 71 percent of the benchmark. Liquefied Natural Gas (LNG) prices are forecast using the provisional price formula negotiated between the Darwin LNG (DLNG) facility and Japanese LNG buyers. The price formula is renegotiated every three years.
Production costs	This is the central estimate of future capital and operating costs as provided by the project operator Santos. The estimate includes proposed drilling and higher decommissioning cost provisions.
Discount rate	Under Schedule 1 of the Petroleum Fund Law, the interest rate used to discount future petroleum revenue is the expected rate of return on the portfolio of financial assets held in the Fund. The Fund's investment strategy is for 5% cash, 55% bonds, 35% equities and 5% in alternatives. The expected long-term nominal return on the portfolio was revised down to 3.8 percent in the last quarter of 2019.

Source: Ministry of Finance, 2020.

Changes in the ESI 2021

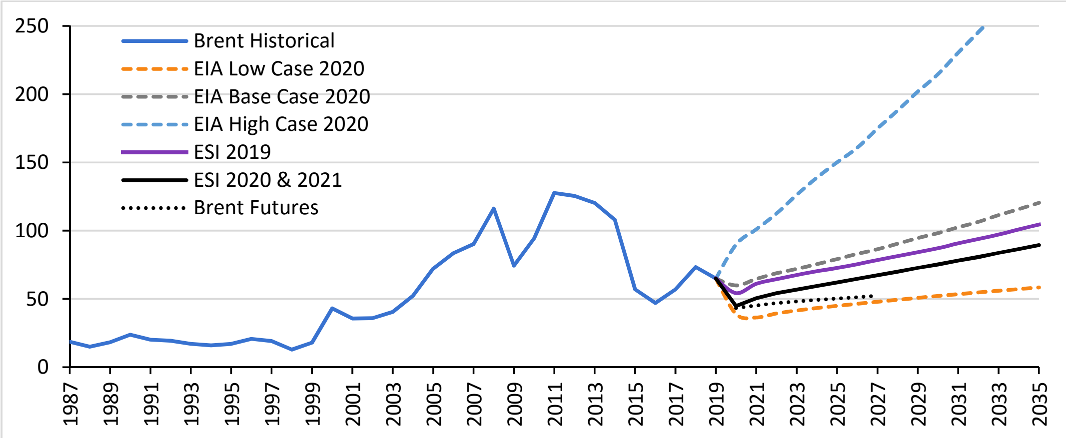
The current estimate of the 2021 ESI is $12.3 million higher than the estimate in the Budget Book 2020 of $535.6 million. The difference is limited given that the two budgets were prepared in close succession this year. Both estimates adopt the actual value of the Fund at the beginning of 2020; the same production forecasts; the same oil price forecasts; the same price differentials; the same costs; and the same discount rate.

The assumed investment return for 2020 incorporates the Fund's performance to date. The Fund's return as at September 2020 is estimated as 5.2%. Incorporating the actual return and adjusting the estimates of quarter 4 returns for the very low bond yields, leads to the annual return estimate of 5.9%. This is higher than the expected long-term nominal return of 3.8%.

The other difference is the assumed petroleum revenue for 2020, which was previously forecast to be $268.7 million. The actual net petroleum receipts until September are already $290.4 million. The annual estimate is revised up to $306.1 million to account for the amounts received and estimated revenue in quarter 4 2020. The projection for 2021 is maintained at $68.1 million.

The oil price forecasts represent the average of the Low and Base cases of the Brent oil prices forecast by the US Government's Energy Information Administration (EIA). The estimated prices for 2020 is $41.2 per barrel, increasing to $50 in 2021 and $54 in 2022. The actual average Brent benchmark price from January to August 2020 was $40.9 per barrel. The EIA now expects that monthly Brent spot prices will average $42.3/b during the fourth quarter and rise to an average of $50/b in 2021.[3]

Figure 10: Oil Price Forecast in the 2021 ESI (from Budget 2020 to Budget 2021)



Source: Ministry of Finance, 2020

As noted in previous Budgets, the Bayu-Undan field is a mature field and its productivity has gradually declined since its peak in 2012. The production from its existing wells has decreased with increasing water and declining pressure. The decline is shown in Figure 11A and 11B. The Bayu-Undan Infill Well (BUIW) project in mid-2018 has helped to boost recent production relative to projections a few years ago. A new drilling program plan has been put forward for the authority's approval.

Figure 11: Bayu-Undan Production Forecast in the 2021 ESI

3 EIA's Short-Term Energy Outlook, released on September 9, 2020. www.eai.gov.

Figure A. BU Liquids Forecasts for B2020

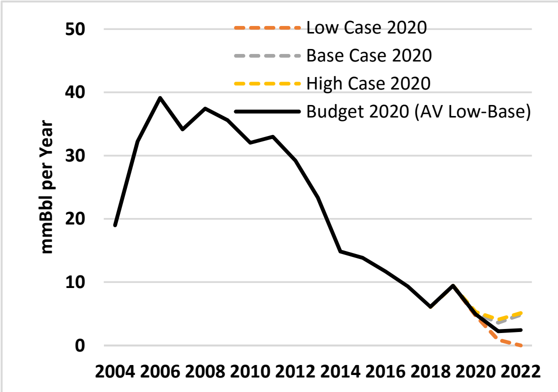
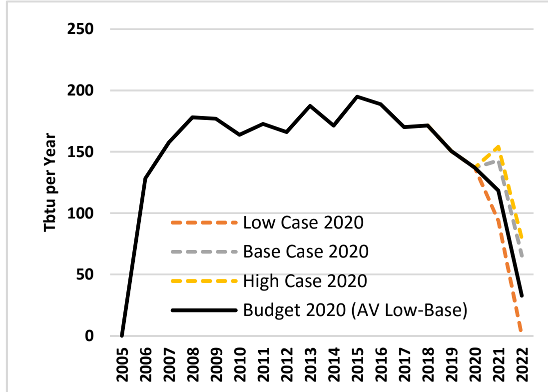


Figure B. BU Gas Forecasts for B2020

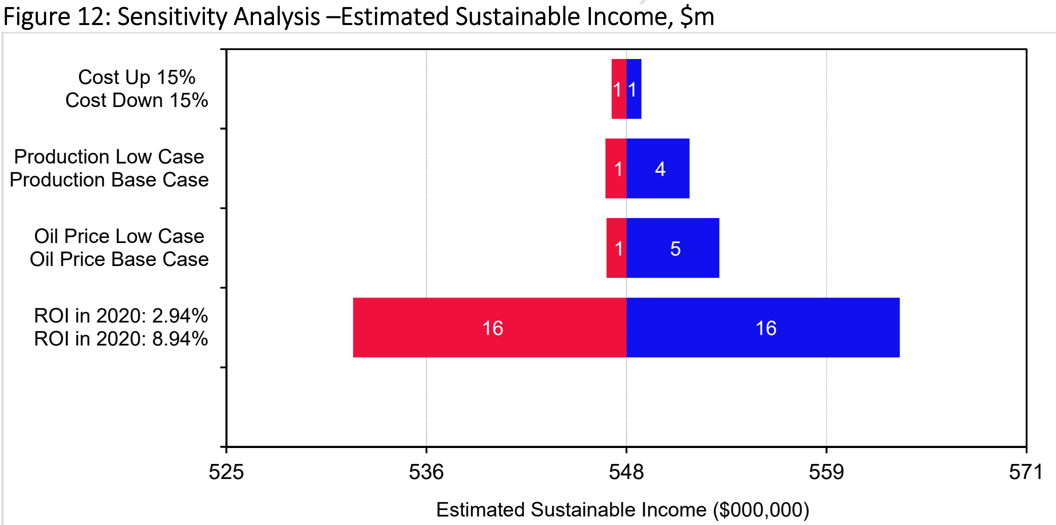


Source: Ministry of Finance, 2020.

Sensitivity Analysis

The Government's objective is to prepare an ESI that is prudent overall, as required by the Petroleum Fund Law. While the calculations are based on the best information available, each input is subject to significant uncertainty. Figure 12 shows how the 2021 ESI of $547.9 million would change if the assumptions for key variables were changed individually. Each sensitivity calculation is briefly described below.

Figure 12: Sensitivity Analysis –Estimated Sustainable Income, $m



Source: Ministry of Finance, 2020

1. The value of the Fund at the beginning of 2021 depends on the assumed investment return for 2020. The annual return for 2020 is estimated to be 5.9% after accounting for actual returns to date. The realised return for 2020 depends on market movements in the last quarter. Variations of +/-3.0% are applied to illustrate how volatility can impact on the Fund's closing value. Changing the annual investment return to 2.9% or 8.9% sees the ESI change by $16 million (up/down).

2. The calculated ESI 2021 is not that sensitive to the forecast of oil price. As noted above, the forecast of future Brent prices is based on the average of the EIA's long-term Low and Base

Cases. If EIA's Low or Base forecast of Brent prices is applied, the ESI would be approximately $1 million lower or $5 million higher.

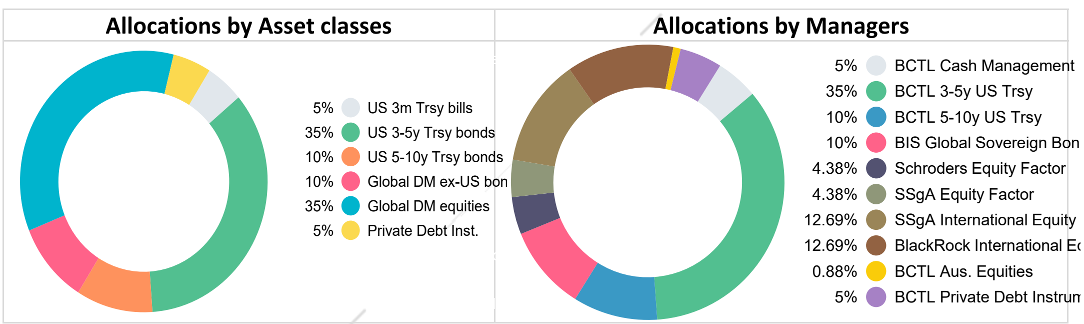
3. The calculated ESI 2021 is not that sensitive to changes in production forecasts and costs. If the Low or Base case production forecast is used, the ESI will fall by $1 million or rise by $4 million, respectively. If the costs change by 15% up or down, the ESI would change by $1 million up or down.

2.4.2.2 Petroleum Fund Management and Projections

The Petroleum Fund Law sets out the Fund's eligible investments, the guidelines for its asset allocation and the risk limits. Since January 2019, the Petroleum Fund Law is to be read in conjunction with the First Amendment of the Law No 13/2005, the Petroleum Activities Law, which was modified to allow investments in petroleum operations.

The Petroleum Fund is currently invested 5% in cash, 55% in Government bonds, 35% in equities and up to 5% in petroleum related operations through a private debt placement in Timor GAP E.P. The breakdown by asset classes and by managers are shown in Figure 13 below.

Figure 13: Petroleum Fund Strategic Asset Allocation and Managers Breakdown, as of August 2020

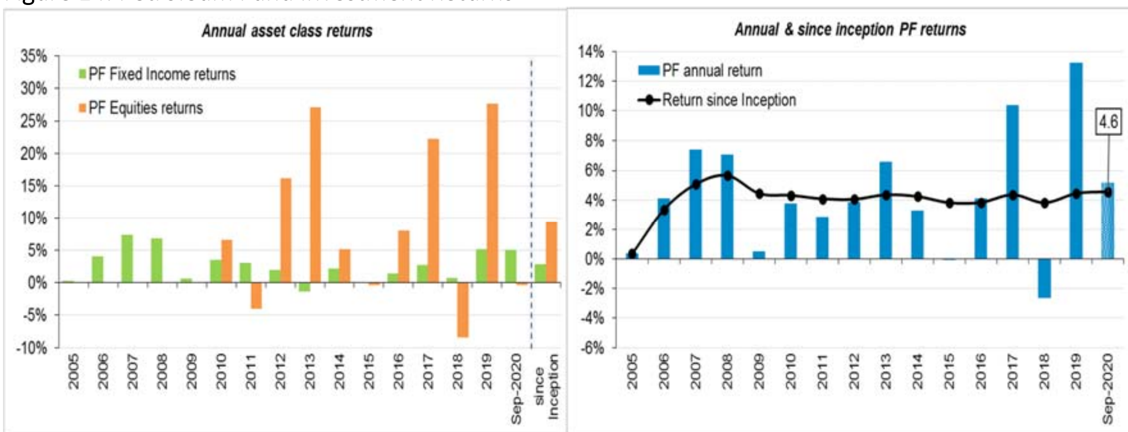


Source: Ministry of Finance, 2020

Equities are the growth assets in the Petroleum Fund's portfolio. The long-term horizon that follows from the fiscal framework means that the Fund can benefit from equities higher expected returns, while weathering the associated year-to-year volatility. Figure 13 shows that the equity portfolio has boosted the Fund's performance by returning 9.9% per annum since the first investment in stocks in 2010. This compares to the bond portfolio's average annual return of 2.0% over the corresponding period.[4] The Fund's return since inception to September 2020 is 4.6% per annum, which is 2.8% in real terms after accounting for US inflation.

[4] Please see the Petroleum Fund Annual Report for 2019 for a more detailed discussion on the performance of the Fund.

Figure 14: Petroleum Fund Investment Returns

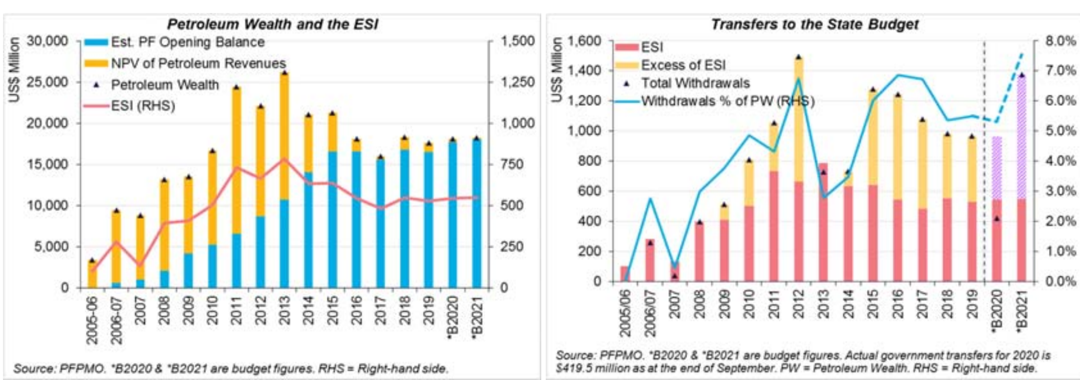


Source: Ministry of Finance, 2020.

The Fund's fiscal framework is interrelated with the investment strategy and faces two substantial challenges. The first is that expected investment returns are now considerably lower than when the 40% equity allocation was originally devised to meet a 3% real return target. Interest rates are currently very low, which will result in low bond returns over the long-term. As a result, the Petroleum Fund is highly unlikely to earn a 3% real return over the next 10 years based on its current asset allocation. The equity allocation would need to increase significantly in order to meet that return, which is not appropriate currently, taking into account the country's ability and willingness to bear risk. This means that the true level of sustainable withdrawals is lower than 3%.

The second challenge is that withdrawals have not followed the fiscal framework. Under the permanent fund framework, sustainable withdrawals are offset by the expected real investment return, thereby protecting the Fund's purchasing power. However, as Figure 14 shows, withdrawals have exceeded the ESI since 2009, averaging about 5% of Petroleum Wealth rather than the 3% in the PF Law. The budgeted withdrawals for 2020 and 2021 are also shown. Governments have justified excess withdrawals on the basis of prioritizing economic development. While the real value of Petroleum Wealth has depleted, the Petroleum Fund's balance was able to grow when petroleum receipts were high.

Figure 15: History of the ESI, Petroleum Wealth and Withdrawal



Source: Ministry of Finance, 2020.

The real value of Petroleum Wealth has depleted as a result of the excess withdrawals, although the Petroleum Fund's balance was able to grow when petroleum receipts were high. However, going forward, there will be a number of years where the Fund's balance is expected to fall: withdrawals are projected to exceed the expected investment returns and the low petroleum revenues. The long-term sustainability of the Fund needs to be carefully managed during this period. Persistently high withdrawals for an extended period risks exhausting the Fund, even if inflows from Sunrise or other fields commence.

The risk in the investment portfolio needs to be managed during a decumulation phase. Reducing the Fund's equity allocation is being considered to account for projected withdrawals. By way of example, the Investment Advisory Board have noted that a horizon of only 10-years would warrant a gradual but significant reduction in the equity allocation over the coming years. Given very low bond yields, the result will be a much lower expected return for the total Fund.

Updated projections for the Petroleum Fund

The Petroleum Fund's balance is a function of petroleum receipts, investment income and government withdrawals. Table 19 shows an update of Petroleum Fund revenues. As noted, petroleum receipts for 2020 is revised up to $306.1 million from $268.7 million in the Budget 2020, although remains significantly lower than receipts in 2019. Petroleum revenue are forecast to continue to decline in 2021 and 2022, before rising to $108.7 million in 2023 as a result of the VAT on decommissioning. The projections do not include Greater Sunrise as the development is not yet approved.

Table 19: Petroleum Fund Revenues 2019-2024, $million

	2019 Actual	2020	2021	2022	2023	2024	2025
Total Petroleum Fund Revenue	2,857.2	1,337.7	729.7	653.2	672.4	511.6	460.2
Petroleum Fund Investment Return	2,100.9	1,031.6	661.6	620.5	563.8	511.6	460.2
Total Petroleum Revenue	756.3	306.1	68.1	32.7	108.7	0.0	0.0
FTP/Royalties	331.8	138.5	27.9	6.1	0.0	0.0	0.0
Profit oil	97.1	30.8	5.0	0.0	0.0	0.0	0.0
Income Tax	120.3	23.4	7.3	0.0	22.1	0.0	0.0
Additional Profit Tax	181.6	54.7	0.5	0.0	0.0	0.0	0.0
Value Added Tax	6.7	25.2	8.6	8.1	86.6	0.0	0.0
Other Tax Payments	18.7	33.5	18.8	18.5	0.0	0.0	0.0

Source: Ministry of Finance, 2020.

The Fund's investment return for the year to September is +5.2%, which translates to net income of $906.5 million. This followed last year's strong return, when equities returned 27.7%. The equity portfolio has posted a return of -0.04% for the year to September, while the fixed income allocation posted a return of +5.1%. Equities have recovered from the sharp fall in the March quarter that was associated with the coronavirus outbreak and strict lockdowns. Risk assets have been boosted by monetary and fiscal policy stimulus, although the economic outlook remains uncertain. The expected investment income for 2020 is assumed to be 5.9%, while for 2021 and beyond is assumed to be the long-term nominal return assumption of 3.8%.

The Parliament has twice approved extraordinary withdrawals from the Fund. The total is $536.3 million, of which $220.0 million is allocated to respond to Covid-19 and $316.3 is to fund the

Treasury account during the duo decimal period until the Budget 2020 is approved by Parliament. There has only been $419.5 million of withdrawals for the year until August.

The Fund's balance is $18,469.5 million as of September 2020. This is an increase of $777.7 million from the start of the year. Table 20 shows that the Fund's balance is expected to end 2020 at $18,065.7 million after accounting for the revenue estimates and deducting the estimated withdrawal of $963.9 million in 2020 approved by Parliament.

Table 20: Estimated Petroleum Fund Savings, $million

	2019 Actual	2020 Prov.	2021	2022	2023	2024	2025
Opening PF Balance	15,803.6	17,691.8	18,065.7	17,417.8	15,858.2	14,376.7	13,059.9
Petroleum Revenue (excluding PF Interest)	756.3	306.1	68.1	32.7	108.7	0.0	0.0
Petroleum Fund Interest, Net*	2,100.9	1,031.6	661.6	620.5	563.8	511.6	460.2
Total Withdrawals	969.0	963.9	1,377.6	2,212.8	2,153.9	1,828.4	1,899.2
Closing PF Balance	17,691.8	18,065.7	17,417.8	15,858.2	14,376.7	13,059.9	11,620.9

Source: Ministry of Finance, 2020.

Total withdrawals to finance the 2021 state budget are $1,377.6 million. This represents 7.5% of Petroleum Wealth and exceeds the 2021 ESI by $829.7 million. Table 20 shows that the Fund is forecast to decline to $17,417.8 million by the end of 2021 as the withdrawals exceed petroleum receipts and investment returns. This is projected to continue each year, with the Fund's balance falling to $11,620.9million by the end of 2025. These are central forecasts and considerable variation needs to be expected given that investment returns are volatile. As the Fiscal Sustainability section explained, the Fund is expected to continue to decline in value beyond the projection period, unless there is a significant change in fiscal policy or until significant new petroleum revenues come online.

2.5 Expenditure and Development Partner Commitments

Total expenditure in the 2021 budget is $2,050.1 million (including donor funded activities of $155.1 million and loans of $70.7 million). The total 2021 State Budget 22.0% higher than that allocated for 2020. This is mainly because i) economic recovery measures, ii) new measures introduced that were not possible in 2020 due to consecutive state of emergencies and the COVID-19 pandemic, and iii) non-continuation of duo-decimal system in 2021.

2.5.1 Expenditure by Fund

Public expenditures are spread across the Consolidated Fund of Timor-Leste (CFTL), the Human Capital Development Fund (HCDF), loans and European Union Budget Support. Since 2016, the Infrastructure Fund is an autonomous agency under the CFTL. Compared to the allocations for the 2020 State Budget, allocations for 2021 have increased for CFTL by 27.0%. However, HCDF has increased by 21.1% and loan disbursements have increased by 17.8%, to introduce new measures and increase allocations of existing programmes which was not possible in 2020.

Table 21: Expenditure by Fund, $million

	2019 Actual	2020 Budget	2021 proj	2022 proj	2023 proj	2024 proj	2025 proj
Combined Source Budget	**1,405.6**	**1,681.0**	**2,050.1**	**2,499.9**	**2,382.7**	**2,044.5**	**2,167.7**
Government Expenditures by Fund	**1,243.8**	**1,497.0**	**1,895.0**	**2,433.4**	**2,370.7**	**2,035.7**	**2,159.0**
CFTL (excl. loans, inc. DBS-EU and social security)	**1,169.6**	**1,426.3**	**1,811.3**	**2,366.0**	**2,310.8**	**1,987.3**	**2,066.8**
Social Security	*35.1*	*41.5*	***42.7***	*44.4*	*46.2*	*48.0*	*50.0*
European Union (Budget Support)	*6.7*	*10.6*	***9.1***	*9.0*	*5.0*	*2.8*	*3.8*
HCDF	17.8	10.7	**13.0**	13.5	14.1	14.6	15.2
Borrowing/Loans (disbursements)	49.8	60.0	70.7	53.9	45.9	33.8	77.0
Development Partner Commitments	**161.8**	**184.0**	**155.1**	**66.5**	**12.0**	**8.7**	**8.7**

Source: Ministry of Finance, 2020.

2.5.1.1 Consolidated Fund of Timor-Leste

The CFTL is the Government's central account and includes all expenditures for line ministries and autonomous agencies with the exception of the HCDF. Within it, recurrent and capital expenditures are spread across five appropriation categories as laid out in Table 22.

Total allocations in the CFTL will increase by 27.0% in 2020 compared to the 2020 State Budget.

The Public Transfers allocations for many ministries and agencies have also increased, with the allocation for the category a whole 22.9% higher than in the 2020 State Budget. The CFTL Goods and Service have decreased by 16.4%. This is because Goods and Services budget had increased in 2020, despite the duo-decimal system, to finance the COVID-19 Fund. The reduction in 2021 is as this magnitude of increase will not be continued from 2020.

On the other hand, allocations to Minor Capital and Capital and Development have increased by 587.6% and 162.9% respectively, compared to the 2020 State Budget. This to allow for new projects in the 2021 State Budget since allocation to these categories was very limited in 2020.

Table 22: Breakdown of CFTL expenditure, $million

	2019 Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Total CFTL Expenditure	**1,169.6**	**1,426.3**	**1,811.3**	**2,366.0**	**2,310.8**	**1,987.3**	**2,066.8**
Recurrent	**904.8**	**1,264.0**	**1,346.9**	**1,400.8**	**1,456.8**	**1,515.1**	**1,575.7**
Salary and Wages	203.0	206.7	**239.3**	248.8	258.8	269.1	279.9
Goods and Services	362.6	488.6	**408.5**	**424.8**	**441.8**	**459.5**	**477.9**
Public Transfers	339.3	568.7	**699.1**	727.1	756.2	786.4	817.9
Capital	**264.8**	**162.3**	**464.4**	**965.2**	**854.0**	**472.2**	**491.1**
Minor Capital	27.8	8.9	**61.2**	63.6	66.1	68.8	71.5
Capital and Development	237.0	153.4	**403.3**	901.6	787.8	403.4	419.6
Infrastructure Fund (excl. loans)	226.2	124.1	**267.8**	760.7	641.4	251.1	261.2

Source: Ministry of Finance, 2020.

Salaries and Wages

The allocation for Salaries and Wages ($239.3 million), a 15.8% increase in the 2021 State Budget compared to the allocation for 2020. The Government has budgeted for increases to finance key measures as follows:

Key Measures

- $11.1 million to RAEOA-ZEESM for payment of civil servants.
- $1.3 million to Timor-Leste Defense Force (F-FDTL) for the new member recruitment .
- $0.6 million to all applicable institutions through the Whole of Government for the internal promotion for civil servants.

Goods and Services

The CFTL Goods and Services budget (not including HCDF) for 2021 ($408.5 million) is set to decrease by 16.4% compared to the allocation in the 2020 State Budget. This includes financing for RAEOA-ZEESM, special roads, sanitation and flood control projects, and special prevention and mitigation measures related to the COVID-19 pandemic.

Key Measures

- $23.9 million to the COVID-19 Fund for the continuation of the prevention and mitigation program.
- $23.8 million to RAEOA-ZEESM to finance new investment as well as for regular expenditure, such as fuel and maintenance for Oécusse.
- $13.8 million to Ministry of Public Works for the maintainance of roads and for a flood control programme to protect against possible damage caused by floods on the coast and inland.
- $13.0 million to the Human Capital Development Fund for its programme on scholarship, technical training, vocational training and other training, for students abroad as well as in Timor-Leste.
- $8.5 million to the Whole of Government for the Counterpart Fund. This will contribute to the continued implementation of key counterpart funding projects. This includes purchase of Nakroma II ferry.
- $8.1 million to the Whole of Government for legal services. This fund enables the state to defend itself in various legal cases.
- $7.9 million to SAMES for acquisition of medications and pharmaceutical goods to help improve the quality of health services provided throughout the country.
- $6.9 million to Ministry of Public Works for maintenance of equipment and edifices.
- $3.4 million to the Whole of Government for the payment of quotas to international institutions. This will ensure the continued participation of Timor-Leste in regional and international activities.
- $3.1 million to the Whole of Government for the population and housing census.
- $2.5 million to Administration of Ports of Timor-Leste (APORTIL) for fuel and maintenance of ferry Nakroman.

- $1.2 million to the Ministry of Council of Ministers for supporting the health and housing of members of government.
- $1.0 million the Ministry of Interior for food and non-food items for natural disasters.
- $0.5 million to the Whole of Government for activities and general support of the Community of Portuguese Speaking Countries (CPLP).
- $0.5 million to the Whole of Government for membership of ASEAN.

Public Transfers

Public Transfers comprise all of the money the Government spends on public grants and consigned payments. The allocation for this category is $669.1 million, a 22.9% increase to the 2020 State Budget. It includes the mitigation and prevention package for the COVID-19 pandemic, maintenance of Hera and Betano generators through the newly formed public enterprise EDTL, a soft loan programme for the Ministry of Tourism, Commerce and Industry, housing for vulnerable population, and a community health diagnostic programme, amongst others. $29.2 million included in Whole of Government will be transferred to RAEOA-ZEESM as a part of its Capital Development budget.

Key Measures

- $194.5 million to the Ministry of Public Works (EDTL, public enterprise and BÉ Timor, public enterprise) towards fuel and maintenance of electricity generators in Hera and Betano. This includes to pay for the debt of fuel supply, maintenance of electricity transmission (150KW) and sub-stations of 20KW - towers at critical junctions at seven locations N117, N31, N71, N72, N15, N24, N34 and N76. Providing electricity throughout the whole country is key to generating growth and development across the country. BÉ Timor projects will focus on water and sanitation throughout the country.
- $93.6 million to Ministry for National Liberation Combatants Affairs for veteran pensions, scholarships for family members and health treatment.
- $83.6 million given to the Ministry of Petroleum and Mineral to support the National Petroleum Authority and Minerals (ANPM), TIMOR GAP and the Institute of Petroleum and Geology (IPG). This money is required to ensure Timor-Leste maximizes the benefits from its natural resources. This includes investment planning, ISO certification and mapping of geological data.
- $42.7 million to the Whole of Government for the Contributory and Non-Contributory Regime. This will be transferred to Institute of National Social Security for implementation.
- $40.0 million to the Whole of Government for capitalisation of the National Bank of Commerce of Timor-Leste (BNCTL).
- $33.0 million to the Ministry of State Administration. This includes $8.0 million for the National Program for Village Development (PNDS) as well as $25.0 million for housing for vulnerable populations.
- $22.8 million to the Ministry of Education, Youth and Sport for concessions for public and private schools, payment of contractual teachers and operational costs for CAFÉ schools.
- $15.5 million to the Whole of Government for the provision of pensions for permanent civil servants under the contributory regime.

- $15.0 million to the Whole of Government to support church activities through the Episcopal Church Conference.
- $12.5 million to the Whole of Government for payment of loans.
- $11.6 million to the Ministry of Health for treatments abroad, primary healthcare and the subsidy for Cuban Doctors in Timor-Leste. These investments are important to further improving the quality of health services for the population.
- $10.0 million to the Whole of Government for capitalisation of the Central Bank of Timor-Leste (BCTL).
- $8.9 million to the Ministry of Social Solidarity and Inclusion for a social assistance programme at the community level.
- $6.4 million to Secretariat for Youth and Sport, to provide support for various sporting events and youth activities throughout the year, including a subsidy for the Football Federation and Liga Amadora.
- $6.0 million to Whole of Government for pension payments for former leaders and former members of sovereign bodies.
- $5.9 million to the Office of the Prime Minister for civic welfare. This includes support for NGOs, the construction of Ai-Mutin and Becora Churches and activities of various civil societies.
- $4.4 million to Secretary State for Cooperatives for subsidy to cooperative groups.
- $4.3 million to RAEOA-ZEESM to finance recurrent costs and commitment in 2021.
- $3.5 million to the COVID-19 Fund to continue the prevention and mitigation program.
- $2.5 million to the Whole of Government for creating a line of credit for private universities.
- $2.5 million to the Whole of Government as contributions for international financial support. This will support the international community and allow Timor-Leste to further influence the global community.
- $2.0 million to the Whole of Government for a public private partnership diagnostic of health issues at the community level.
- $1.8 million to the Secretariat of State for Vocational Training Policy and Employment (SEPFOPE) for the self-employment programme. This will contribute towards promoting job creation and economic growth.
- $1.8 million to the Secretary of State for Social Communication to provide subsidy for Radio Television Timor-Leste (RTTL) and community radio.
- $1.5 million to the National Parliament for subsidies to Parliament banches.
- $1.0 million the Ministry of Interior for contingency measures for natural disasters.
- $1.0 million the Ministry of Tourism, Commerce and Industry for a soft loan programme.
- 0.6 million to the Ministry of Higher Education, Arts and Culture for supporting arts activities.
- $0.6 million to the Ministry of Social Solidarity and Inclusion for a programme on HIV/SIDA.
- $0.5 million to the Ministry of Coordination of Economic Affairs for subsides to industries and small businesses.
- $0.3 million to Presidency of the Republic for a community solidarity programme.

Minor Capital

Minor Capital includes expenditures on vehicles, furniture and other movable assets. The 2021 budget ($61.2 million) for this category reflects a 587.6% increase compared to the 2020 State Budget ($8.9 million). This category did not receive any proper allocation therefore this will consider in 2021.

Key Measures

- $9.8 million to Ministry of Agriculture and Fisheries for mechanical workshop, vehicles, industrial boats, cold chain units, fibre glass boats, spare parts for agricultural equipment and tractor, and other minor equipment.
- $9.1 million to Ministry of Finance for a Disaster Recovery Data Centre and associated equipment, server and licenses for Customs, security equipment, x-ray equipment and weight bridge for border security and customs.
- $4.8 million to Ministry of State Administration for motor vehicles for municipalities, IT hardware including data servers for Alieu as well as desktops for municipal administrative posts, equipment for the Technical Secretariat for Election Administration for the 2022 presidential election, and other minor equipment.
- $2.9 million to Ministry of Education for motor vehicles, informatics equipment, furntiture for schools and libraries, as well as projectors.
- $2.4 million to RAEOA-ZEESM for the purchase ambulance vehicles, potable water trucks, operational vehicles, electronic equipment, furniture and others.
- $2.0 million to IGE-Equipment for the purchase of Heavy equipment and other associated equipment to contruct and maintenance for rural roads including intervention to emergency needs.
- $1.9 million to the National Police of Timor-Leste (PNTL) for the purchase of motor vehicles and security equipment amongst others.
- $1.9 million to the Ministry of Defense for security equipment, informatics hardware and communication equipment.
- $1.9 million to the Ministry of Health for the purchase of multi-functional ambulances, medical equipment for referral hospitals and health centres.
- $1.7 million to the TIC for the purchase of motor vehicles and EDP equipment,etc.
- $1.7 million to the Ministry of Interior for the purchase of motor vehicles, security equipment, EDP equipment etc.
- $1.6 million to the Ministry of Foreign Affairs and Cooperation for the purchase of motor vehicles, furnitures for the central office and Diplomatic office overseas.
- $1.6 million to the Ministry of Planning and Teritorial for the purchase of motor vehicles, furniture, EDP equipment and office supplies.
- $1.6 million to municipalities for the purchase of motor vehicles, EDP equipment, office supplies, furniture etc.
- $1.1 million to the Ministry of Transport and Communication for the purchase of motor vehicles, EDP and communication equipment.

- $1.1 million to the Defense Forces of Timor-Leste (FALINTIL) for the purchase of motor vehicles, informatics hardware, photocopy equipment etc.
- $1.1 million to Courts for the purchase of motor vehicles, furniture, EDP equipment, communication equipment etc.
- $0.9 million to the Ministry of Public Works for the purchase of motor vehicles, EDP equipment etc.
- $0.8 million for the National University of Timor-Leste (UNTL) for payment of debt to Timor Telcom and purchase of office equipment (student's desks).
- $0.7 million to the Ministry of Justice for the purchase of motor vehicles, communication equipment etc.
- $0.7 million to the Ministry of Social Solidarity and Inclusion for the purchase of funeral vehicle, communication equipment, EDP equipment etc.
- $0.5 million to Prosecutor General of the Republic for the purchase of motor vehicles, security equipment, EDP equipment etc.

Capital and Development

The 2021 allocation ($403.3 million) for Capital and Development (CD) will increase 162.9% compared to the allocation for 2020. A number of new projects will be started in 2021 which was not possible in 2020 due to the COVID-19 pandemic and duo-decimal system. As shown in Table 23, Capital and Development allocations under the CFTL are broken down into $267.8 million for the Infrastructure Fund (excluding loans), $10.7 million for the District Development Programs, and $124.7 million for other Capital and Development projects across line ministries including RAEOA-ZEESM.

Note, when $29.2 million for RAEOA-ZEESM is included in Capital Development, the total Capital Development budget (including loans) will be $503.2 million.

Key Measures

- $267.8 million to the Infrastructure Fund for the construction of continued multiyear projects and new projects.
- $56.3 million to RAEOA-ZEESM which includes the financing of new and continued projects for its regional development. This excludes a transfer it will receive from the central government of $29.2 million which will be used to finance its capital projects.
- $64.8 million for the completion of new, retained and re-appropriated line ministry projects.
- $10.7 million for the Integrated Municipality Development Programme (PDIM).
- $3.6 million to the COVID-19 Fund to continue the prevention and mitigation program.

Table 23: Capital and Development Expenditures, $million

	2019 Act.	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Total Capital and Development	**237.0**	**153.4**	**403.3**	**901.6**	**787.8**	**403.4**	**419.6**
Infrastructure Fund (excl. loans)	226.2	124.1	**267.8**	760.7	641.4	251.1	261.2
District Development Programs	4.0	6.0	**10.7**	11.1	11.6	12.0	12.5
Ministries / Agencies	6.8	23.4	**124.7**	129.7	134.9	140.3	145.9

Source: Ministry of Finance, 2020. The PNDS budget has now been moved to Public Transfers from Capital Development.

2.5.1.2 Infrastructure Fund

According to the Strategic Development Plan, a central pillar for the long-term development of Timor-Leste is the building and maintenance of core, productive infrastructure in order to support sustainable economic growth, social inclusion, and promote the national connectivity. The Infrastructure Fund was established in 2011, with the role of financing the strategic infrastructure projects on the multi-year basis. Since 2011 up to 2020 a total of $4.8 billion has been approved and $3.1 billion or 64% executed through the IF to finance IF programs, including the Public Private Partnerships projects (PPPs) and external loans. Since 2016, the Infrastructure Fund has been operated as an autonomous agency.

The VIII Constitutional Government set the infrastructure development priorities in the area of basic infrastructure for both social and economic sectors. That includes programs for roads, bridges, water and sanitation, and the provision of sustainable energy. Many projects have already been completed in previous years. Other important infrastructure will be required to support modernization and growth of the Timor-Leste's economy, including digital infrastructure, transport and logistics infrastructure for trade, as well as supporting of industrial development.

In 2021 the total IF budget for 21 programs (including loans and operational cost $1.1 milion) is $339.6 million with the biggest share in the Portfolio allocated for roads and bridges (33%), Information System (13%), Loan funded projects (21%), and the remaining budget allocated to the rest IF programs (power sector, defence and security, public building, water and sanitation, agriculture and others). The budget for 2021 has been allocated to the projects that already has contracts that need to be paid by the government toward the end of 2021 and some priority projects for education, health, defence and security sector, related to the land border protection and prevention of COVID-19.

Table 24: Infrastructure Fund budget and projection, $million

Infrastructure Programs, $ millions	2019* Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Total Budget (excluding MPS including loans)	276.0	184.1	338.5	829.5	708.1	327.9	206.9
Total Budget (excluding MPS & Loans)	226.2	124.1	267.8	760.7	641.4	251.1	129.9
Agriculture	1.0	1.2	3.8	36.0	33.7	11.6	0.7
Water and Sanitation	0.3	2.6	3.4	45.5	33.2	6.1	0.5
Urban and Rural Development	4.3	2.3	6.2	13.1	5.9	3.1	2.5
Public Buildings	1.0	3.3	7.7	47.2	61.8	30.8	6.1
Education	0.2	0.1	4.8	39.0	49.9	28.8	3.4
Electricity	9.9	4.3	18.3	1.9	0.7	0.0	0.0

Infrastructure Programs, $ millions	2019* Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Informatics	4.1	2.6	41.6	14.7	8.4	2.3	0.0
Health	0.1	0.2	4.8	7.1	5.1	1.8	0.0
Security and Defence	2.5	3.8	13.9	36.6	26.5	9.5	1.5
Social Solidarity	0.0	0.6	1.0	2.7	1.1	0.4	0.0
Tasi Mane	45.3	2.0	8.5	286.4	289.5	113.0	108.8
Airports	5.3	4.0	19.8	35.4	27.5	13.7	0.0
Preparation of Designs and Supervision	0.2	3.6	9.4	17.5	7.5	2.5	0.0
Roads	134.7	80.0	105.2	118.3	51.7	19.1	2.7
Bridges	9.1	3.5	4.9	2.8	5.3	0.8	0.0
Ports	0.2	2.0	1.8	5.4	5.4	1.2	0.8
Tourism	0.1	0.0	0.7	0.3	0.0	0.0	0.0
Financial System for Supporting Infrastructure	3.2	3.1	2.9	4.2	3.0	3.0	3.0
Youth and Sport	0.4	0.6	2.0	9.6	10.4	3.5	0.0
Maintenance and Rehabilitation	4.4	4.3	6.9	37.0	14.7	0.0	0.0
Loans Program	49.8	60.0	70.7	68.8	66.7	76.8	77.0

*Source: Major Projects Secretariat, the Ministry of Planning and Teritorial, 2020. *2019 Actual Budget execution according to the Free Balance Records.*

2.5.1.3 Expenditure by Loan Financed Projects

Expenditure on loan-financed projects in 2021 is expected to reach $70.7 million, as presented in Table 25. This is a 17.8% increase compared to the allocation in the 2020 State Budget is as new projects will be initiated after the hiatus in 2020 due to the COVID-19 pandemic and state of emergency periods. A detailed description of these projects is presented in Section 2.6.3.

Table 25: Expenditure on Loan Financed Projects, $million

	2019 Actual	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.	2024 Proj.
Loan Expenditure	49.8	60.0	**70.7**	68.8	66.7	76.8	77.0

Source: Ministry of Finance and Ministry of Planning and Teritorial, 2020.

2.5.1.4 Human Capital Development Fund

The Human Capital Development Fund (HCDF) created in 2011, has as its main objective to develop the human resources of the strategic priority areas in line with the National Strategic Development Plan. The programs financed through the HCDF are classified into four main groups, whichh are: Vocational Training, Technical Training, Scholarships and Other Types of Training.

The vocational training program is primarily focused on training young people in a foreign language to seek opportunities for service abroad and training in the industry. The technical training program covers training activities for public administration as part of the professional development program to raise the capacity of civil servants in all government departments. The scholarship program aims to increase the knowledge and skills necessary for the country's economic and social development. It covers grants and scholarships for the children of veterans, civil servants, teachers at private universities and young people without means. The other types of training program covers programs related to research, studies, inspection, professional internship to promote the newly graduated beneficiaries of HCDF scholarships and others.

The total budget for the Human Capital Development Fund (HCDF) is $12,995 million for the 2021 State Budget. The amount allocated is to finance the 4 types of training programs and 59 activities of 16 government institutions. The 2021 allocated amount is low when compared to previous years (except the year 2020 when the budget was only $10,7).

The following table summarizes the budget allocations for the HCDF by program. As shown in Table 26, the majority is allocated to the scholarship program, which represents more than half of the total approved budget, i.e. 60% of the total budget. The remaining programs have the following budget allocation: technical training program (24%), other types of training program (8%) and vocational training program (8%).

As a result of the worldwide COVID-19 pandemic situation there have been certain restrictions on HCDF programme implementation in 2021, such as the suspension of all training, both short and long term (new scholarships) abroad.

Table 26: Human Capital Development Fund by Program, $million

	2019 Actual	2020 Budget	2021 Budget	2022 Proj.	2023 Proj.	2024 Proj.	2025 Proj.
Total HCDF (by Program)	**17.7**	**10.7**	**12.995**	**25.8**	**26.8**	**27.8**	**28.9**
Vocational Training	3.3	0.8	1.078	3.7	3.8	3.9	4.1
Technical Training	5.3	1.3	3.146	7.2	7.5	7.8	8.1
Scholarships	7.0	6.8	7.764	12.5	13.0	13.5	14.0
Other Training	2.1	1.9	1.007	2.4	2.5	2.6	2.7

Source: Secretariat for Human Capital Development Fund, 2020.

2.5.2 Ministry Allocations

The summary of line Ministries' final allocation are presented in the Table 27.

Table 27: Proposed Allocation to Line Ministries, $000

SDP Sector	Ministry	2020 Proposed Budget('000)
Economic Development	Ministry of Agriculture and Fisheries	31,964
	Ministry of Petroleum and Mineral Resources	85,573
	Ministry of State, Coordinator of Economic Affairs	2,117
	Ministry of Tourism, Commerce and Industry	11,802
	Secretariat of State for Vocational Training Policy and Employment	6,244
	Secretariat of State for Cooperative Sector	7,623
Infrastructure Development	Ministry of Planning	15,211
	Ministry of Public Works	240,674
	Ministry of Transport and Communications	13,348
Institutional Framework	Appropriations for all of Government	228,533
	Minister of State for the Presidency of the Council of Ministers	5,023
	Ministry of Defence including FDTL	39,222
	Ministry of Finance	34,133
	Ministry of Foreign Affairs and Cooperation	26,738
	Ministry of Interior including PNTL	54,459

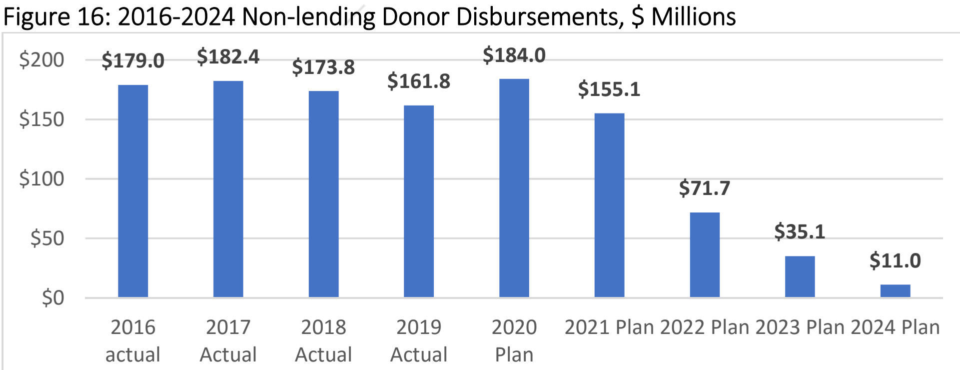
SDP Sector	Ministry	2020 Proposed Budget('000)
	Ministry of Justice	15,523
	Ministry of Legislative Reform and Parliamentary Affairs Including SECS	9,930
	Ministry of State Adminstration	52,809
	Prime-Minister	10,267
Social Capital	Ministry of Education, Youth and Sports Including SEJD	111,478
	Ministry of Health	58,848
	Ministry of Higher Education, Science and Culture Including SEAC	6,320
	Ministry of National Liberation Combatants Affairs	104,521
	Ministry of Social Solidarity and Inclusion	19,943
	Secretariat of State for Equality and Inclusion	2,554
	Secretariat of State for Environment	2,955
	Secretariat of State for Youth and Sport	9,476

Source: Ministry of Finance, 2020.

2.5.3 Development Partners' Commitments

Development Partners' support is forecasted to experience a nearly 16% reduction as compared to 2020 figures. This is due to two reasons. First, the coronavirus pandemic created a significant need for increased spending in Timor-Leste to fortify the nation against the potential spread of COVID-19. Secondly, donor reporting for 2020 was conducted in mid-year 2020, thus development partners had a clearer sense of how much they would be disbursing by the year's end. Please note that the European Union's Direct Budget Support programs are not included in these figures.

Figure 16: 2016-2024 Non-lending Donor Disbursements, $ Millions



Source: Aid Transparency Portal, report generated on September 28, 2020.

In 2021 the five donor groups that are scheduled to disburse the highest amounts of funding are as follows: Government of Australia ($54.2 million; 35.0% of total), Portugal including funding from Camoes ($18.2 million; 11.8% of total), the European Union ($13.7 million; 8.9%)[1], the

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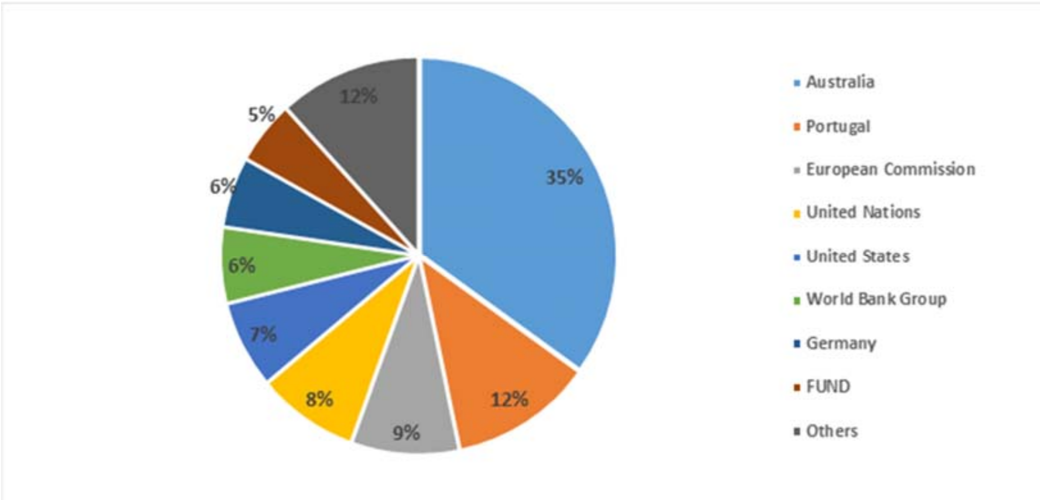
[1] This figure does not include the approximately €8.0 million that will be provided to the GoTL's Treasury via Direct Budget Support. This funding is intended to support Government's efforts towards PFM Reform, Decentralization, and Nutrition.

United Nations ($12.9 million; 8.3%), and the United States of America ($11.1 million; 7.2 %;). Please refer to Part 5 of Budget Book #5 for a detailed summary of donor and executing agency disbursements.

Figure 17: Planned Non-lending Disbursements by Donor Group



Source: Ministry of Finance, 2020.

2.6 Financing

2.6.1 Definition of Financing

The total budgeted expenditure for 2021 is higher than the domestic revenue that will be collected over the same period. This results in a non-oil deficit (domestic revenue minus expenditure). This deficit is financed through a number of sources; withdrawals from the Petroleum Fund (PF), loans, the use of the cash balances (from both the Treasury and RAEOA/ZEESM accounts) and European Union Budget Direct Support. Withdrawals from the PF can be either within a sustainable amount, using the revenue of the fund, or excess withdrawals above this sustainable level (see next section). Table 28 below shows the amount drawn from each of the financing items.

Table 28: Source of Financing, 2021-2025, $million

	2021	2022	2023	2024	2025
Total Financing	**1,156.5**	1,704.7	1,678.3	1,382.9	1,456.8
Excess Withdrawals from PF	829.7	1,641.8	1,627.4	1,346.3	1,453.0
Use of Cash Balance	247.0	0.0	0.0	0.0	0.0
Use of Treasury Cash Balance	150.0	0.0	0.0	0.0	0.0
Use of RAEOA/ZEESM Cash Balance	97.0	0.0	0.0	0.0	0.0
Borrowing /Loans (disbursements)	70.7	53.9	45.9	33.8	77.0
European Union (DBS)	9.1	9.0	5.0	2.8	2.8

Source: Ministry of Finance, 2020

2.6.2 ESI and Excess Withdrawals

There are important economic reasons for distinguishing between revenue and financing items. Domestic revenue results from taxes borne by companies and individuals in Timor-Leste from production and income made. The ESI is the sustainable level of use of petroleum revenue, to ensure the continued use of the petroleum fund for ever. Spending only up to total revenue (domestic reviews and ESI) is a position that maintains fiscal sustainability. It is a benchmark level of spending for understanding the long run trend of government finances. The ESI can therefore be considered revenue. The government has changed the definition of revenue to include the ESI to make clearer what is fiscally sustainable.

The ESI is equal to 3% of the net petroleum wealth equals $547.9m in 2021. This is a slight increase from the ESI in 2020 due to the increase in the Petroleum Fund balance. Further details on the ESI and petroleum wealth can be found in Section 2.4.2.1 of this Budget Book.

The Government plans to withdraw $829.7m in excess of the ESI in 2021. This is a near doubling of the excess withdrawals in 2020 which totalled $419.6m. Excess withdrawals are in line with the Government's frontloading policy. These excess withdrawals are being used to finance core infrastructure and human capital, which is necessary for long-term growth.

2.6.3 External Loans

Government has been implementing infrastructure development programme as one of the main strategies at contributing to turning Timor-Leste into an upper middle-income country by 2030 in accordance with the Strategic Development Plan 2011-2030. Achieving this goal, however, requires substantial financing resources that is often not available domestically in sufficient amount and in favourable terms, making foreign borrowing indispensable. It allows the country to invest and consume beyond the limits of its internal production capacity; thus, more rapid growth and poverty alleviation.

As any of other young small states, Government is currently relying on agencies of governments or Multilateral Development Banks for its external concessional borrowing. By definition, concessional loan is a loan that has a lower interest rates than those on the market or by grace periods, or a combination of these. Concessional loans typically have long grace periods.

The following table estimates loan concessionality of different funds relatively compared to withdrawing money from petroleum fund reflecting the concessional nature of much of the debt agreed with the international financial institutions.

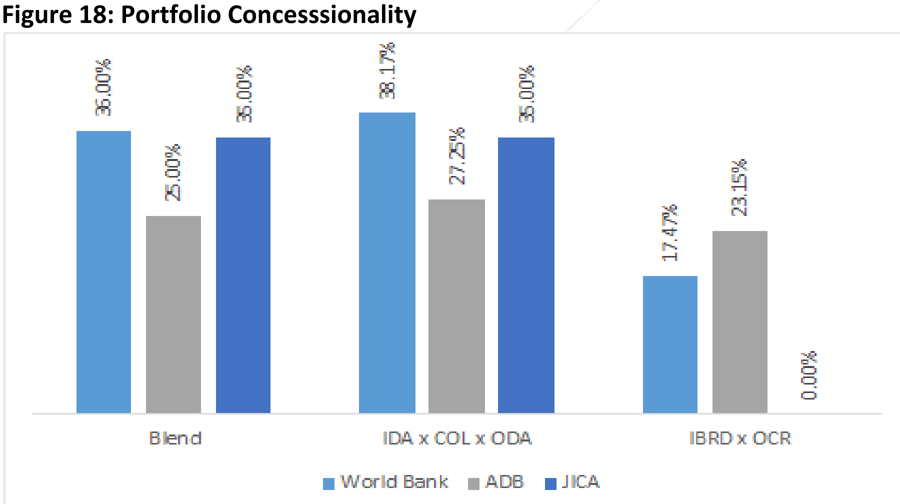
Table 29: Concessionality Estimates

IFIs/Program	Amount of initial loan ($ million)	Currency	Exchange rate adjust-ent as of 30/6/2020	Maturity (Years)	Grace Period (Years)	Interest rate Average Estimation (%)	Up-front fee (%)	Concessi-onality (%)
Asian Development Bank								
COL	117.02	USD,SDR	114.73	25.50	5.20	2.00	-	27.25
OCR	154.63	USD,SDR	154.63	25.00	5.00	2.20	-	23.15
Total	271.65		269.36					
World Bank								
IDA	119.20	USD,SDR	119.24	32.00	7.50	1.5	0.25	38.17
IBRD	15.00	SDR	15.00	28.00	8.00	3.00	-	17.47
Total	134.20		134.24					
JICA								
ODA	68.70	JPY	49.00	30	10	0.61	-	49.53

Source: Ministry of Finance, 2020

There seems to be an inverse concessionality relationship between ADB and WB loan funds. While it is cheaper to get a fixed rate loan from IDA-World Bank, ADB's floating rate loan, OCR, offers a greater concessionality than IBRD. On the other hand, despite it has the highest percentage of 49.53% at the point of loan origination, the concessionality level of JICA's loan fluctuates significantly over the years due to currency devaluation.

Figure 18: Portfolio Concesssionality



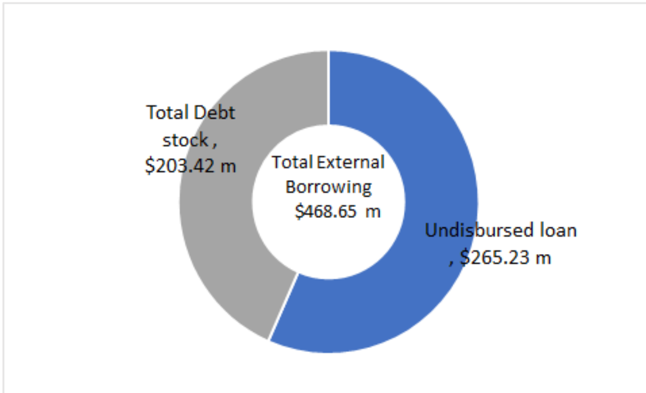
Source: Ministry of Finance, 2020

At the portfolio level, so far the World Bank's IBRD and IDA offers the most competitive loan package. While ADB currently ranks below the others, its level of concessionality can be further enhanced through extending more concessional loans with fixed rates.

Total Borrowing

As of end of June 2020, the total signed loan agreements was US$ 474.57 million of which US$ 5.92 million has been repaid since 2017 leaving a balance of US$ 468.65 million. The balance is a total borrowing is composed of total disbursed outstanding debt and undisbursed loans. The share of undisbursed loans accounted for US$ 265.23 million and outstanding disbursed amounted to US$ 203.42 million.

Figure 19: Total External Borrowing



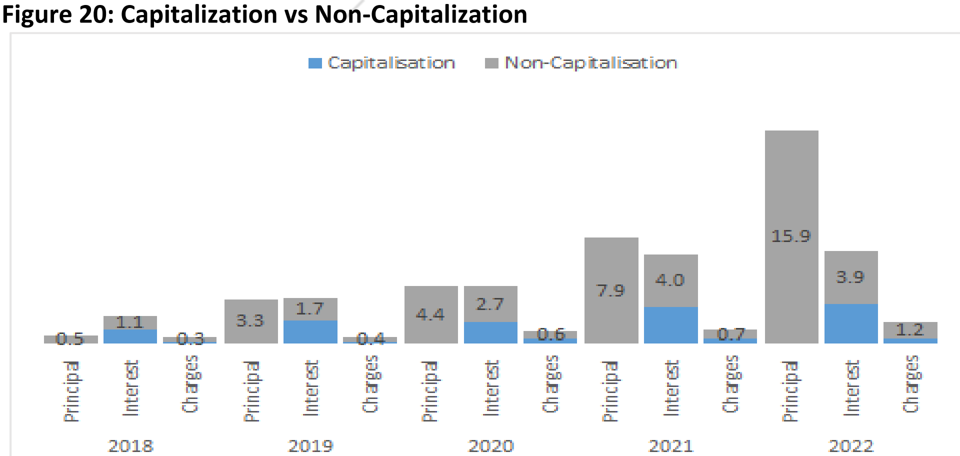
Source: Ministry of Finance, 2020

Debt Service

Debt service includes payment of interest, principal and other miscellaneous charges. During grace periods, other than principal repayment, some of the cost components are normally paid from loan accounts also known as capitalization. These include interest, commitment charges, and other fees and charges.

As most of the ongoing loan grace periods is coming to an end, the amount of debt service that have to be settled in cash as part of loan service payments increases significantly. While in 2018 the ratio of non-capitalisation to capitalization is only 2 to 1 the comparative numbers rise to 7 to 1 by 2022.

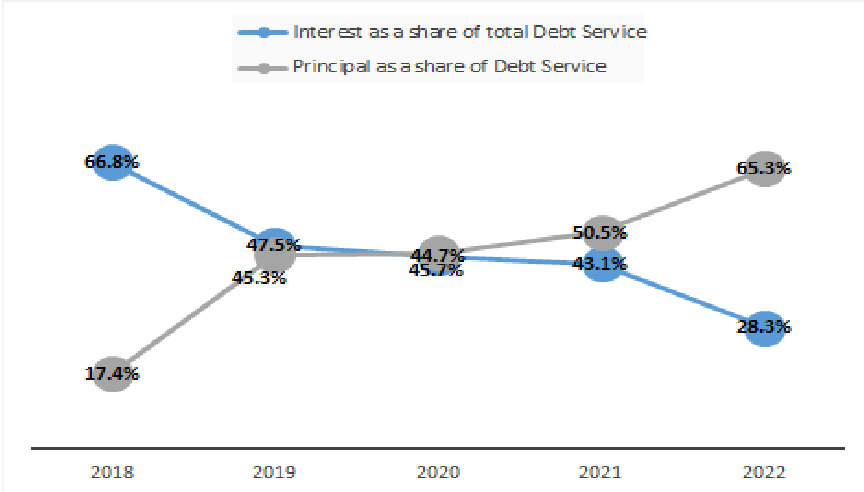
Figure 20: Capitalization vs Non-Capitalization



Source: Ministry of Finance, 2020

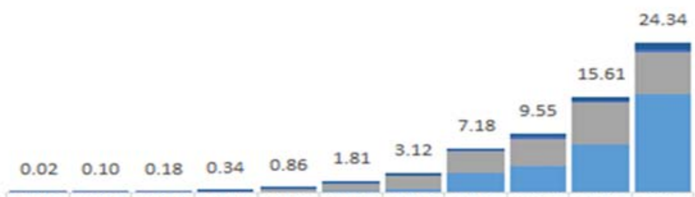
As illustrated below, the trend occurs as a consequence of the amount of payments on the principals of the loans overtakes the amount of interest payments. The cross point in 2020 is about $4.3 million.

Figure 21: Interest vs Principal



Source: Ministry of Finance, 2020

Figure 22: Debt Service, 2012-202, $millions



	2012	2013	2014	2015	2016	2017	2018	2019	2020f	2021f	2022f
Service Charge ($ millions)	0.00	0.00	0.00	0.04	0.14	0.23	0.33	0.36	0.40	0.62	0.98
Commitment Charge ($ millions)	0.02	0.10	0.13	0.13	0.17	0.18	0.16	0.15	0.52	0.37	0.57
Interest payment ($ millions)	0.00	0.00	0.05	0.17	0.55	1.15	2.09	3.41	4.27	6.73	6.89
Principal repayment ($ millions)	0.00	0.00	0.00	0.00	0.00	0.25	0.54	3.25	4.36	7.88	15.90
Total	0.02	0.10	0.18	0.34	0.86	1.81	3.12	7.18	9.55	15.61	24.34

Debt Management Operation

Debt management objective is to manage the government debt in such a way to minimise the cost of debt in the long term while taking risk in its management into account within fiscal sustainability framework. It includes setting the appropriate balance between the public debt and the fiscal variables as well as risk management.

Changes in External Debt Stock

The stock of total external debt remains manageable, increasing by 27%, from $248.27 million, at end-2020 to $311.09 million, at end-2021. This increase results primarily from an expected rise in disbursements, relative to 2020 and the contracting of new construction project for the national road from Aitutu-Letefoho.

Table 30: External Debt Indicators, 2017-2021, % GDP & Revenue

	2017	2018	2019	2020f	2021f
Total External Debt to GDP	6.7%	9.2%	11.9%	16.3%	20.0%
Total Debt Service to Revenue	0.3%	0.4%	1.0%	1.3%	2.2%
In million of US dollars, unless otherwise indicated					
Memorandum items:					
Total external debt	107.10	145.71	192.20	248.27	314.60
Debt Service	1.81	3.12	7.18	9.55	15.61
GDP	1590.50	1578.10	1620.00	1523.00	1572.00
Revenue	671.15	741.17	720.67	716.75	719.76

Source: Ministry of Finance, 2020. Note: GDP figure for Y2019 is an estimate. F= forecast.

Despite the continued increase in the amount of the stock of external debt, the debt to GDP forecast in 2021 remains below debt burden and threshold benchmarks established under IMF/WB Debt Sustainability Framework for Low Income Countries. Being assessed as a country with debt carrying capacity at a moderate level, Timor Leste's debt threshold is currently set at 40%.

The total debt service to revenue ratio remains stable, increasing by about 0.8% points to 2.2% in 2021 mainly due the commencement of principal repayments of several loans. Larger principal repayment in turn increases the rate of decline in the amount of outstanding external debt. The debt threshold benchmark of this ratio is 18%. These marginal increases in the indicators have not diminished Timor-Leste's strong debt sustainability position.

Table 31: Foreign Exchange & Interest Risks

Risk Indicators for the Period 2017-2021					
	2017	**2018**	**2019**	**2020f**	**2021f**
Total share of US dollar debt to total external debt	75%	76%	73%	69%	67%
Total share of non-US dollar debt to total external debt	25%	24%	27%	31%	33%
Total share of floating rate debt to total external debt	47%	49%	47%	45%	41%
Total share of fixed rate debt to total external debt	53%	51%	53%	55%	59%
In million of US dollars, unless otherwise indicated					
Memorandum items:					
US Dollar Debt	80.04	110.17	139.83	171.81	209.76
Floating Rate Debt	50.70	70.68	90.41	110.48	129.86

Source Ministry of Finance, 2020. F= forecast.

Risk Factors

Additionally, government also continues to exercise prudent management of the risks associated with external debt management. These include management of interest and exchange rate risks. Over the period, the external debt portfolio is mostly denominated in fixed interest rates and US dollar currency. The high share of fixed rate debt contracted from external creditors has helped to minimise government's interest rate risk and keep the cost of debt servicing to a sustainable level. The total share of fixed rate debt to total external debt is expected to increase from 55%, in 2020, to 59% in 2021. Fixed rate debt has been acquired from external creditors such as ADB, JICA and WB.

On the exchange rate, government has also greatly benefited from the US dollar as the foremost funding currency in its external debt portfolio as Timor Leste's economy is highly dollarized. It helps mitigate external debt against volatility of currency rate changes. While the ratio between US dollar debts to non-US dollar debt shows a slight downward trend after year 2018 the magnitude is relatively large and sustained over the years with expected ratio of about 2 to 1. It means that for each additional debt over 60% is likely to be denominated in US dollar debt.

External Debt Sustainability

Debt sustainability refers to the ability of government to meet its current and future debt service obligations. In evaluating debt sustainability, the most commonly used method is to utilize a tool jointly developed by the World Bank-International Monetary Fund, known as the new debt sustainability framework (DSF) for Low-Income Countries (LICs), implemented since July 2018 where Timor Leste's debt –carrying capacity is currently assessed as "moderate" with a low risk of debt distress using the country-specific macroeconomic indicators and the World Bank's Country Policy and Institutional Assessment (CPIA).

As shown, government's external debt remains sustainable as necessary conditions of debt sustainability holds over the projection period. While debt ratios remain well below their respective thresholds, risk indicators are consistent with the risk profile of the government's loan policy note.

Internally, while specific laws or regulations being developed regarding how debt sustainability are to be interpreted and implemented the practice so far for external debt sustainability has been that any loan to be taken out by government must have a considerable degree of concessionality or the overall financial costs of borrowing should be lower than the opportunity cost of withdrawing funds from the Petroleum Fund.

Table 32: Cost of Borrowing VS PF Investment Return

Year	PF Annual Investment return %	PF Investment return since inception %	All-in Costs Borrowing %
2017	10.36	4.36	1.7
2018	-2.63	3.82	2
2019	13.25	4.45	2.3
Aug-20	6.47	4.68	1.4
2021f	3.8	3.8	1.84
2022f	3.8	3.8	2.3
2023f	3.8	3.8	2.2

Source: Ministry of Finance, 2020. F= forecast.

The cost of government borrowing has been kept lower than Petroleum Investment return ensuring the future debt servicing costs remain well within its capacity to repay. The trend is expected to continue in the medium term until changes in the country's classification by new income level. Timor Leste is currently classified by International Financial Institutions as a low income country which helps it benefit most from concessional lending.

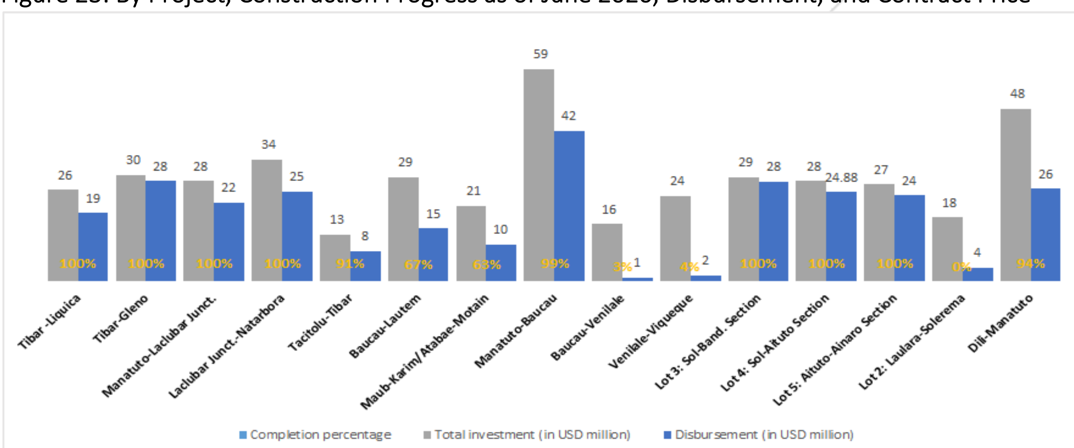
Project Progress

Over the period between 2012 and 2020, government has been heavily investing in major road infrastructure projects through concessional loans. The funding are currently used to fund 15 ongoing construction projects of which 7 are already completed and 3 are expected to be finalized by end of 2020. In total, it represents an achievement rate approximately 67%.

The three projects nearly complete include Tibar (Port)-Tacitolu four-lane sections, Dili-Manatuto, and Manatuto-Baucau roads. On the other hand, the 5 ongoing construction projects involves roads connecting Baucau-Lautem, Atabae-Motain/Maubara-Karimbala, Laulara-Solerema, Baucau-Venilale, and Venilale-Viqueque. The last three road sections are relatively new projects as the construction works were just starting in mid-2019. For that reason, the projects progress are still low nearly 4%.

Additionally, a new concessional loan has also been signed with the World Bank to implement road sections from Aituto-Hatuibilico-Gleno. The project is currently under the preparation for procurement phase.

Figure 23: By Project, Construction Progress as of June 2020, Disbursement, and Contract Price



Source: Ministry of Finance, 2020

In dollar amount, the total capital contribution made by this investment is $429.85 million which is by a ratio of total investment, concessional loans contributed approximately 62%. Of this rate, $157.07 million has been disbursed leaving a balance of $109.33 million to be spent for next 2-3 years in accordance with project duration estimates. On the other hand, state contribution to the overall budget of Civil Works contract was $163.45 million with an estimated remaining $43.77 million for further disbursement.

Table 33: Total Investment in Civil Works, $million

Source of Fund	Total Investment in Civil Works	Disbursement As of June 2020	Contract Balance
Loan Fund	266.4	157.07	109.33
State Contribution	163.45	119.68	43.77
Total	429.85	276.75	153.09

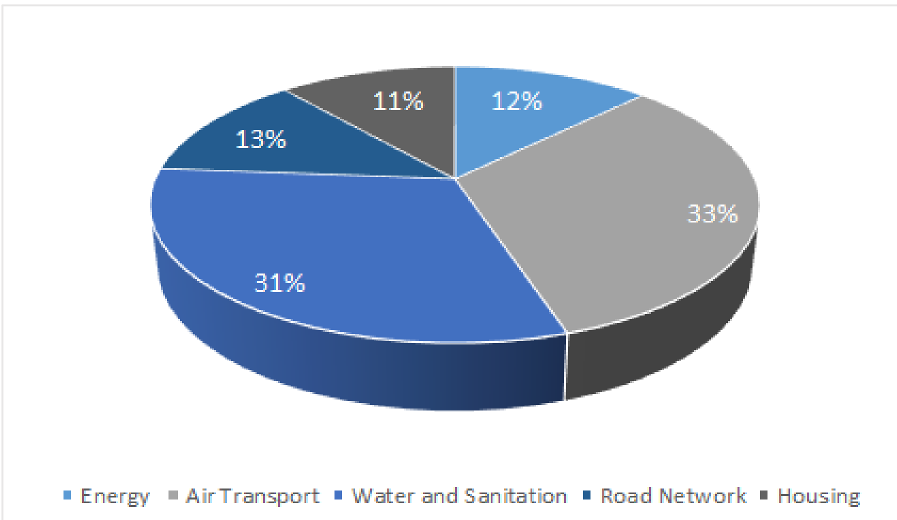
Source: Ministry of Finance, 2020

It is important to note that as projects grow in sizes and complexities there needs to make adjustment to the ongoing project management hierarchical organization. On this, Government is currently planning to establish a two- level of hierarchy of Project Management Units with the objective of improving project execution and completion. The roles and responsibilities may vary depending on what activities to be assigned to the units in accordance with project management life cycles.

Future loans

A well-established infrastructure is critical for the delivery of economic diversification, long-term development sustainability, and poverty reduction. It supports the development of the private investments and employment creations. While infrastructure investments have so far been focused on road networks development, energy, water and sanitation, housing, and airport are also a priority investment programme to be developed and financially supported through new concessional loan package. For 2021, Government is proposing $400 million as a loan ceiling for negotiation with potential lenders.

Figure 24: Sectoral Allocation of Proposed ceiling for 2021



Source: Ministry of Finance, 2020

Complying with the priority for social sector development, over 50% of the ceiling is allocated to key relevant infrastructure in addressing the needs of the poor by enabling better access to safe water, electricity as well as affordable housing. Another key social sector is education which is fundamental for human development. The loan ceiling 2020 already includes BEST project funded by the WB with the objective of strengthening basic educational system in Timor Leste. The project implementation starts in 2021. Dili Airport development and road networks, on the other hand, would help ease constraints to access both local and global markets by reducing transport costs.

Table 34: Total Loan Disbursement, 2020-2024, $million

	Total	2020	2021	2022	2023	2024
Loans	342.99	60.00	70.70	68.76	66.73	76.8

Source: Ministry of Finance, 2020

2.6.4 Government Bonds

The 2021 Budget draft law includes a proposal for a US $20 million celling for the possible issuance of public debt bonds, in addition to the US $400 million celling of concessional loans, for a combined public debt ceiling of US $420 million, depending on the approval of the Government bonds legal framework during 2021.

The issuance of public debt bonds is the preferred source of Government borrowing among developed economies, but has over the past decades become increasingly popular among low-income developing countries.

According to data from the IMF, since 1995, 49 emerging market and developing economies have issued international sovereign bonds at least once since, spread among capital market bonds, syndicated loans and private placements, tempted by the increased interest of investors.

Starting in 2010, as risk appetite improved and global interest rates further declined, international investors, inclined to diversify their asset portfolio, resumed their search for yield in a low-interest rate environment and sovereigns took advantage of low global interest rates to finance themselves in international markets. As a result, bond issuances among emerging market and developing economies picked up considerably.

This presents an opportunity to Timor-Leste to provide a diversification of funding sources, beyond concessional loans and withdrawals from the Petroleum Fund, and may eventually attain a lower rate of interest than those, therefore proving more attractive.

The recent creation of the Social Security Reserve Fund, which by law should invest part of its funds in national Government bonds, should provide the necessary demand to initiate small syndicated and or private placement issuances with a short maturity. If successful, more substantial emissions might follow in the subsequent years.

The regulation of bonds, and its subsequent issuance, should result from a wide discussion on the medium term Government financing policy, its relation to the existing instruments (namely concessional loans) and should benefit from the expertise of international partners like the World Bank and the IMF. The regulation should define the specific instruments to be used, the issuer, the type of issuance, the type of investor allowed, the interest rate and the maturity of the bond, among other elements.

Following recommendations to advance with the regulation and issuance of bonds, namely from the National Parliament, the Government proposes a specific celling allocation for bonds in the 2021 Budget draft law, as not to use the concessional loans celling allocation of US $400 million, to allow the process to move forward in 2021, if possible.

2.6.5 Use of Cash Balance

The total cash balance to be used to finance 2021 State Budget is $247.0 million. $150.0 million is to come from the Consolidated Fund of Timor-Leste (CFTL) held in the Treasury Account. The other $97.0 million is to come from the cash balances held by RAEOA/ZEESM. There is no forecasted rollover of cash balances for the HCDF from 2020.

Table 35: Use of Cash Balance in 2021, $million

	2021
Cash Balance HCDF	**0.0**
Treasury Cash Balance	**150.0**
RAEOA_ZEESM Cash Balance	**97.0**
Total Cash Balance	**247.0**

Source: Ministry of Finance and Secretariat for the Human Capital Development Fund, 2020.

2.6.6 Budget Support

Timor-Leste has been receiving Budget Support (BS) from the European Union since 2014. The latest agreement was signed in 2016 under the 11th European Development Fund.

In 2019, EU BS was recorded off budget in a separate account and not including in the CFTL total. In 2020, and for all subsequent years, it became on-budget as the funds went directly to the Government system with the money held in a Treasury sub-account. This means EU BS is considered as a financing for 2021 State Budget.

The money from EU BS is used directly by the beneficiary ministries for the public financial management program (Ministry of Finance), malnutrition (Ministry of Health) and decentralization (Ministry of State Administration).

The funds are directly given to the country's government without prior earmarking. However, a variable tranche depends on specific Key Performance Indicators (KPIs) agreed upon by the Ministry of Finance and the EU. While the funds are not separate or additional to the Ministry's core business, they must support clearly stated priorities and the Ministry's own planning framework.

Total amount of BS for 2021 State Budget is $9.1 million. Of that amount, $4.03 million is distributed to the Ministry of Finance, $2.24 million to the Ministry of Health and $2.80 million to the Ministry of State Administration.

2.6.7 Public Private Partnerships

2.6.7.1 Overview of Public Private Partnerships in Timor-Leste

In general terms, the Public Private Partnership (PPP) refers to arrangements in which the private sector build infrastructure assets and provides services that traditionally have been provided by the State. The underlying rationale for PPPs in Timor-Leste stems from the fact that this arrangement may potentially allow the Government to benefit from the private sector expertise and financing, which then results in higher quality and efficiency, as well as lower risk borne by the Government. The government will also benefited from shifting the risks onto the private partner – for example, the risk of delays or cost run-ups in construction.

Another advantage is the fact that the bundling together of the various stages of providing an infrastructure service creates the right incentives for the contractor to perform to a high standard. Should the same contractor is responsible for building, operating and maintaining a piece of infrastructure for a number of years, it will have an inherent incentive to build it in a way that optimizes the operation. Another advantage of proceeding with PPP arrangement is the fact that PPP contracts are typically output-based and extracting value-for-money through risk transfer to the private sector over the life of the project, rather than input-based as is generally the case with traditional procurement. This means that the Government is certain of paying for actually-functioning services that meet actual social needs.

Timor-Leste began exploring PPPs as a modality for project implementation over the last 9 years and started out by establishing a PPP Policy, PPP legislation and a dedicated PPP Unit under the Directorate General for External Resource Mobilization and Management, Ministry of Finance. The PPP policy establishes key principles of PPP, while the legislations (Decree-Laws no. 42/2012 as amended by Decree-Law no. 02/2014 and Decree-Law no. 08/2014) confirms the policy as formal process, sets a framework for enabling the public and private sectors to be parties in a PPP arrangement; define the powers of relevant agencies and regulates the procedures associated with the PPP Projects Cycle. All of these seek to ensure that only high-quality projects, which have high social and economic returns and which are aligned with the government's strategic priorities, are considered for implementation through a PPP modality. For instance, the legislations on PPPs include a requirement that all PPP projects undergo both a pre-feasibility study and a full-fledged feasibility prior to proceeding to the procurement phase.

Decree Law no. 8/2014 stipulates the formation of PPPU, a unit under the Ministry of Finance to take on the task of facilitating, managing and implementing the PPP Project Cycle in coordination with line ministries and under oversight of the Council for Administration of Infrastructure Fund (CAFI). Another important role of the PPP Unit is to promote and create environment for attracting foreign direct investment (FDI) through PPP modality, while at the same time looking for ways of encouraging local private sector involvement in PPP projects by pursuing policies and regulations that will allow for development of small to medium scale PPPs. One Sector that have high potential for this is the Tourism Sector.

2.6.7.2 Existing PPPs Projects

Currently, one PPP project is in Implementation and Operation Stage (Tibar Bay Port PPP), one in Procurement and Negotiation Stage (Medical Diagnostics) while others in Feasibility Stage (Affordable Housing, Cristo Rei and Presidente Nicolau Lobato International Airport).

Tibar Bay Port Project

The PPP modality chosen for Tibar Bay Port was a 30-year concession, including the design, partial financing, construction, operation and maintenance of the port infrastructure. The project was awarded to a consortium comprised by Bolloré Africa Logistics and SDV East Timor through an international competitive bidding which formed Timor Port SA (Concessionaire) to implement it.

The concession agreement was signed on 3rd June 2016 between the GoTL and the TPSA and the concession was awarded for 30 (thirty) years including a construction period which started on 30 August 2018 and expected to be completed by May 2022. The construction progress until end of September 2020 was 33.5%.

The Environmental License was awarded on 15 March 2018 and currently extended until 15 March 2022. So far there is no record of environmental impacts resulting from the construction of Tibar Port.

The capital expenditure of the Phase-I is around USD 300 million. The Concessionaire will fund the majority of the amount by means of equity and debt and the GoTL has allocated an amount of USD 129.45 million as Viability Gap Funding (VGF) to the Concessionaire. Until end of September 2020, the total amount disbursed from VGF was USD 45.31 million.

The Escrow Account is earning interests. As of 30 September, 2020, interest earned amounted to $8.422m, deposited in the Escrow Interest Account. The Escrow Agreement stipulated that the interest earned can only be transferred to the Government account after the closing of the Escrow Account and/or termination of the Escrow Agreement.

Medical Diagnostics

Medical diagnostics PPP is currently in preparation of tender documents and other necessary structures (e.g. accessible data room) which are the early steps in the procurement and negotiation Stage. The Feasibility Study and Transaction Structuring Report (TSR) have been approved by CAFI on 11 July 2019 with clearance issued by the Ministry of Health in June 2019.

The TSR recommended that the project upgrade imaging and laboratory diagnostic centers in the National Hospital, all referral hospitals and 8 Community Health Centers (CHCs) to achieve a demand coverage of 98.2% of the total population. Concession period is recommended at 11 years to consist of 1 year of upgrading and construction of National Hospital, all referral hospitals and CHCs and 10 years operation period. The estimated of Government contribution will be about $12 million per year for operation and maintenance of health diagnostic services.

It is estimated that the contribution of private sector will be around $11 million for the upgrading or construction of facilities, operate and maintain Laboratory and Imaging centers and provide quality diagnostic services to patients in Timor-Leste. In addition, private sector also will employ and train diagnostic services staff, comply with local regulation and international best practices in health care service delivery. Potential bid parameter and bid evaluation criteria have also been recommended. However, the project is on hold since the beginning of 2020 due to various reasons, particularly with the coronavirus disease (COVID-19) outbreak. Given that Financial Advisory Service Agreement (FASA) has expired on June 2020, both Government of Timor-Leste and International Finance Corporation (IFC) conducted negotiation and agreed to sign the extension of FASA, in which the discussion continued and concurred that IFC need to reassess and adjust Transaction Structure Report based on the impact of COVID-19 due to large amount of assistance on medical equipment and infrastructure provided by international development partners. Apart from that, both parties agreed that the project should be implemented gradually in order to achieve the targeted 98.2% of demand coverage of the total population.

Affordable Housing

The right to access to housing is enshrined in the Constitution of Timor-Leste and a major priority for the Government. Acknowledging the need and importance of better housing facilities, the Government has initiated multiple measures to address the issues associated with it. The Government is exploring formal interventions in developing housing and enabling housing finance markets in partnership with the private sector, and is actively looking to identify suitable land parcels to realize this program. The Government's immediate target is to create 4,000 new dwellings for people across various income groups. This Project aims to contribute to this target by delivering approximately 2,000 affordable dwellings on 20 ha of land made available by the Government using a Public Private Partnership (PPP) approach.

Through PPP modality, the pre-feasibility study for Affordable Housing PPP project has been completed, submitted and approved by Council for Administration of Infrastructure Fund (CAFI) to proceed with next step. Currently in the proses of finalizing the Financial Advisory Service Agreement (FASA) document between GoTL and IFC *(International Finance Cooperation)*. The study made an assessment of the housing ecosystem in Timor Leste including existing housing market, the housing value chain which considers the demand and supply sides of the housing provision in Dili and make recommendations for the creation of a vibrant housing market in the capital. Among the recommendations are – facilitating access to construction finance products and incentivize developers to provide market-based solutions for affordable housing (supply side) and facilitate access to home loans/mortgages for households with effective purchase power (demand side) and make available subsidy program to increase access to housing for qualified low income groups. Subsequent step for the project is to proceed with Feasibility Study phase where deeper analysis of the technical, legal, commercial as well as social and environmental terms are conducted.

Development of President international Nicolau Lobato Airport

Pursuant to the decision of the Council of Ministers to develop the International Airport of Presidente Nicolau Lobato ("Airport") through PPP Hybrid modality, this modality entails the combination of investment from private and public. The implementation involves public investment through Engineering, Procurement and Construction (EPC) contract with possibility of involvement of private sector for construction, operation and maintenance of the entire airport.

The Feasibility study for Airport development is underway with good progress, and construction of these components will commence in 2022 and expected to complete by 2024/25. Financing of these components, such as extension of the runway to 2.1 Km, aprons, taxiway, partial parallel taxiway and control tower will be financed through ADB loan in the amount of $130 million inclusive of 23% counterpart funding from government.

Meanwhile, preparatory studies for other key components (e. g. Terminal) and other sub-components will be initiated in 2021 and financed through state financing with potential involvement of private investment. The Japan International Cooperation Agency (JICA) expressed their commitment to undertake preparatory studies and construction of airport terminal through grant financing of $44 million. One important element of preparatory study includes resettlement of affected communities who reside in the surrounded area of the runway expansion. This includes the preparation of Resettlement Action Plan (RAP) which will be established by the Government with the support of airport stakeholders.

The implementation of RAP is expected to take place as soon as it is completed. Meanwhile, the implementation of phase 1 of Financial Advisory Service Agreement (FASA) with IFC is progressing well, and it is expected to conclude before end of 2020. The FASA phase 1 consists of technical, financial, environmental and social (E&S) and legal due diligence and structuring. Phase 2 comprises of tender and award of contract to selected bidder. The Airport project also receives plethora of interest from some international agencies whose commitment still subject to final confirmation.

Cristo Rei PPP

The Cristo Rei PPP has finalized its pre-feasibility study through Grant financing from the USAID Tourism for All (USAID TFA) program. The preparation of the pre-feasibility study was coordinated between USAID TFA, the Directorate General of Tourism under the Ministry of Tourism, Commerce and Industry (MTCI) and the PPPU under the Directorate General for Management and Mobilization of External Resources (DGMMER) of Ministry of Finance. The scope of the PPP project covers operation and maintenance of the facility with some repair and upgrade of existing facilities to ensure safety, expansion of restaurant and green space and creation of a ticketing space, all for the purpose of ensuring better recreational and spiritual experience. The Pre-Feasibility Study has found that the project is highly viable given the level of visitation by domestic and international patrons. It was preliminarily recommended that the project be structured according to the Design, Finance, Built, Operate and Transfer (DFBOT) modality with Concession contract model for certain duration with all CAPEX (100% of CAPEX) borne by the private sector. Upon approval of the CAFI, the project can proceed to Feasibility Study phase where deeper analysis of the technical, legal, commercial, social and environmental aspects are conducted.

2.6.7.3 New Initiatives

Tourism PPP

Tourism has been defined as a co-pilar of long term economic strategy in the VIII Constitutional Government Program and the National Tourism Policy. This sector has been estimated to account for 10.4% of global GDP and 9.9% of global employment.

While the sector is still at its infancy, the Government recognized tourism as an important engine for the development of economic activities in the country and considered this sector as a nascent economic sector meaning it is showing potential to grow rapidly in the near future with sufficient investment in tourism site improvement, operation and maintenance of the facilities, better access to the sites as well as upgrade to the hospitality standards. Another important sub-sector of Tourism is marketing of what Timor-Leste has to offer. Tourism marketing will increase awareness about the country globally and drive demand (increase tourist visits), providing reasons for sustained investment in the Sector. On the other hand, Dili International Airport will be upgraded soon and a rapid increase in the capacity of the airport will materialize.

Other New PPP Initiatives

In 2021, UPPP will explore new initiatives in several sectors identified with potential to be implemented through PPP modality. These projects were identified through:

- Alignment with VIII Government Program and Priority
- Potential to realize better value for money
- Preparation of business case for the projects
- Projects meeting preliminary requirements to technical, legal, economic, commercial, social and environmental aspects

As a result from the above process, UPPP produced a preliminary list of projects for scoping and evaluation prepared with the support of development partner agencies including the International Finance Corporation (IFC), USAID and Asian Development Bank (ADB). Projects for consideration including projects in the energy sector, technical and vocational education and training and other projects in transport and agricultural sectors. Next step is that the preliminary list of PPP projects will be coordinated with relevant line ministries before being presented to CAFI for approval.

3 2021 General State Budget Law

Please, note that this document will be submitted separately.

3.1 Annexes

Please, note that this document will be submitted separately.

4 Supporting Documents

4.1 Justification for Transfer from the Petroleum Fund

4.2 ESI Report: Requirement for Transfer from the Petroleum Fund for the 2021 ESI

4.3 ESI Report: Transfers from the Petroleum Fund in Excess of ESI 2021

Supporting documents will be presented separately

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