

25 June 2010

Excellency,

**Subject: Summary of the Timor-Leste's Strategic Development Plan
(2011 – 2030)**

On behalf of the United Nations System, I would like to congratulate you for initiating the process of the long-term Strategic Development Plan (SDP) for Timor-Leste for the period 2011-2030, the summary of which was released by the Government of Timor-Leste on 7 April 2010 at the Timor-Leste and Development Partners' Meeting. .

I welcome the ultimate goal to move this country from a low-income to an upper-middle income country by 2030. I further welcome the determination to build a diversified economy and the strong commitment to build human capital. The identification of three strategic sectors (agriculture, petroleum and tourism) as triggers for further economic growth through sector investment plan is also well-founded. I compliment you for undertaking nation-wide public consultations on the SDP to obtain feedback from the Timorese on their aspirations and also note your intention to present the draft to the National Parliament for discussion.

With a democratically elected leadership and in the presence of oil revenues being accumulated in the Petroleum Fund (recently surpassing US\$5 billion), I believe Timor-Leste has a real opportunity to make a "big push" for development, improve the lives of the people and enhance prospects for peace and stability. In the spirit of contributing positively to the draft SDP, I would like to make a few comments for your consideration.

**H.E. Mr. Kay Rala Xanana Gusmão
Prime Minister
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Dili**

As the country prepares to participate in the 2010 Millennium Development Goal (MDG) Review Summit in September in New York this year, it is important to highlight the importance of the MDG framework as the guiding force for action and investment in sectors that would promote human development and achieve the MDG targets in a sustainable manner. Experience from many countries across the world indicates that higher income levels do not automatically translate into higher levels of human development. Pursuing higher growth rates alone has further proven to be inadequate in promoting equitable and inclusive growth. The SDP provides an excellent opportunity for the government to rededicate itself to achieving the MDGs by making macro-economic policies MDG-sensitive and allocating enhanced human and financial resources to the social sectors to achieve the MDGs.

You may agree that a disquieting feature of recent development pattern has been the growing disparities between rural and urban areas. This is an undesirable trend considering that the vast majority of the Timorese population live in villages and are dependent upon subsistence agriculture. Persistent deprivation of the rural areas is already manifesting itself in migration, particularly of youth, to the urban areas. A renewed focus on the rural areas should therefore be an urgent priority. Therefore, policies for enhanced investment in agriculture and rural areas need to be put in place to increase incomes, create employment and boost demand for local products. This will, in turn, create conditions for rapid growth of the economy, as visualized in the summary SDP document. Budgetary allocation to the agriculture sector, in the past, has perhaps not been commensurate with the needs of the rural population. Correction of this anomaly, as indeed is reflected in the summary SDP, will go a long way in addressing the rural-urban imbalances in levels of development and contributing to long-term peace and stability. Furthermore, special attention must be given to the challenge of youth unemployment in both rural and urban settings.

The 2007 Timor-Leste Survey of Living Standards has shown that the proportion of people living below the poverty line of \$0.88 per capita per day has gone up from 36% in 2001 to nearly 50% in 2007. While we hope that this has changed in light of the cash transfers and investments undertaken by the government under your leadership, there are concerns that the inequalities might have worsened over the past few years. While we await more scientific results on poverty and inequality, there are signs of growing inequality as one travels through the rural and urban areas in the country. It is therefore imperative that the incomes of the bottom 40% of the population be raised. The fact that other countries in the south-east Asian region have been able to grow rapidly while simultaneously reducing poverty and inequality also gives me hope that this country can do the same. It may be pertinent to mention that these countries did not rely solely on the growth to “trickle down” but put policies and programmes in place to make growth inclusive. Growth and equality are not mutually incompatible.

In the above context, I would also like to flag an important macro-economic issue. The realization of double-digit growth rates visualized under SDP is inextricably linked to the incremental capital-output ratio which in turn is an indicator of how well we use our capital resources. In the context of Timor-Leste where cost of doing business is very high due to inadequate infrastructure and lack of enabling environment, the assumed ratio of 5 may not materialize. However, much depends on the composition of future investment – both sectorally and as its break up into public and private investment.

As the country is situated within a dynamic region, private sector investment of the order of 15 percent of GNP is feasible though the country needs to take several steps to make this happen. The country needs to strengthen, in a relatively short timeframe, its communications, transportation and financial infrastructure to attract private sector, both foreign and domestic. In the short-run, offering fiscal incentives and concessions is not a bad idea. The regulatory framework is currently not very conducive and Timor-Leste does not rank

very high in terms of ease of doing business. This requires urgent steps. The foreign investment law should be enacted soonest to attract investments which will help to generate employment, improve labour skills, promote newer technologies and also contribute to enhance foreign exchange of the country. When enabling conditions are in place for the private business, this will also pave the way for small rural entrepreneurs to expand their businesses and thus unleash domestic entrepreneurship.

It would be a challenge to mobilize adequate resources to finance the SDP and meet the goals stipulated therein. With the global aid environment becoming increasingly unpredictable and many donor countries still reeling from the economic crisis, availability of international resources to operationalize the SDP would become increasingly difficult. Further, the domestic resource mobilization scenario through tax and non-tax revenue is unlikely to be buoyant in the near future. Against this backdrop, I consider the country's oil wealth a blessing. It has been the consistent position of the United Nations that somewhat enhanced, but prudent, use of oil revenues will go a long way in providing a better life for the Timorese people. A key determinant of whether oil wealth becomes a boon or a bane is the institutional capacity, that is, the extent to which the state apparatus is accountable and staffed by skilled personnel with integrity. Whether or not oil rich countries fall victim to the "Dutch disease" will depend in large part on the extent to which they invest oil windfalls in public assets (e.g. infrastructure, education, health) that raise productivity rather than consumption. This, in turn, requires good governance and, in particular, transparency and reliable public information on the sources and uses of oil earnings, and the expected flow of oil earnings in the future.

An expenditure framework for the medium-term strategic plan should be developed to link with the assumptions. In this context, the total financial and sectoral outlays required to achieve the vision should be spelt out. How much of financial resources would come from domestic sources and how much will be expected from bilateral and multilateral assistance and also loans from development partners could be more clearly articulated.

A major challenge in making the SDP work would be the lack of national capacities. In this regard, I welcome the emphasis in the summary SDP on human capital investment. In the long run, all the investment in education, including vocational training, would ensure that the country has enough human capacities, technical and managerial, to implement different sectoral programmes. However, in the short run, the country should not shy away from 'buying' such capacities abroad whenever they are not readily available in-country. The experience of countries in the middle-east is a case in point.

The country's natural resource base is fragile and fast degrading. Land, water and forests, on which bulk of the population depend, are under stress. Upland areas are particularly vulnerable to environmental degradation. In this context, I would like to propose that the SDP give further consideration to the constraints imposed on economic development activities by the country's natural environment and renewable resources. Throughout the plan there is a need to recognize the poverty-environment nexus and incorporate measures to conserve and protect the natural resource base — land, water, biodiversity — so that development activities in each of the major sectors (agriculture, infrastructure, energy, urban development, tourism, forestry, fisheries) are environmentally sustainable. The plan should also give greater recognition to the need for each sector's development to be adapted to the disruptive impacts of climate conditions and climate change.

Timor-Leste is passing through a demographic transition of unprecedented proportions. It has one of the highest population growth rates in the world and one of the highest fertility rates. The decline of fertility from 7.8 in 2003 to 5.7 in 2009 indicates that investment in women's health and education is the best policy to regulate the family size and ensure family

welfare. It is my firm belief that addressing the overriding challenge of population growth needs to begin with further investment in people. It is in this spirit that we would like to advocate for investment of significant resources in health and education, of which we see a welcome reflection in the summary SDP.

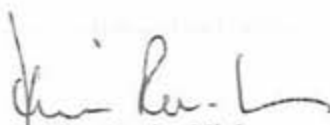
The SDP would also benefit from further emphasis on the promotion of gender equality and the empowerment of women in all sectors so that women play an equal role in the development processes and benefit equally from the fruits of development.

An improvement in governance is a *sine qua non* to achieving sustainable growth. I welcome the initiatives taken by the Minister of Finance to improve budget execution in order to strengthen the effectiveness of revenue collection, the efficiency and effectiveness of public expenditure, as well as financial management and accountability within the budgetary process. These changes must be buttressed by concomitant changes in audit function and anti-corruption mechanisms. A well-functioning independent audit agency in Timor-Leste, will contribute significantly to future foreign capital-raising plans by increasing the range of willing lenders and decreasing the cost of borrowing required to assist in the providing the capital needed to implement the SDP. As a corollary, an enhanced anti-corruption "architecture" needs to be in place as well. Such institutions play a critical oversight role in a democracy and must be staffed by people of the highest integrity and professionalism.

While the SDP is a strategic policy document focusing on economic development of the nation, it is essential to also give adequate consideration to building government's monitoring and evaluation (M & E) functions/systems to support evidence-based policy making, support ministries and agencies in managing activities and programmes and enhance transparency and accountability.

The UN System rededicates itself to working towards the realization of the vision of "good-bye conflict, welcome development" by forging solid partnerships to promote a bright future for the citizens of this country. As you embark on the process of finalizing the SDP, views from a cross-section of stakeholders and cross-fertilization of ideas will make this process even more participatory. The UN System stands ready to engage in further consultations with you and your Government on the further development and operationalization of the SDP.

Please accept, Excellency, the assurances of my highest consideration.



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