



## EXECUTIVE SUMMARY: KEY MESSAGES OF THE REPORT

Timor-Leste has made substantial progress in the years following its independence in 2002 and particularly since the 2006 crisis. The 2011 Timor-Leste National Human Development Report (TLNHDR) charts this progress and provides a detailed assessment of:

- **The current state of human development in Timor-Leste;**
- **The key challenges to be met;**
- **How these challenges can best be addressed in the coming years.**

Human development enables the realization of human potential. It focuses on what people can do and become—their capabilities—and about the freedom they have to exercise real choices in their lives. Human development is intrinsically linked to the Millennium Development Goals.

### **The Petroleum Fund and Human Development**

**A fundamental issue for the country is the way in which the revenue from its Petroleum Fund—the single largest source of revenue for Timor-Leste—can best be utilised to promote human development through the development of the non-oil economy, and in particular the rural sector—home to 80 percent of the country’s population, approximately 41 percent of whom it has been estimated recently are living in poverty.**

Consequently, the TLNHDR focuses on the ways in which the non-oil economy can best be developed. In doing this, it aims to:

- **Present the achievements of the country thus far in meeting its development goals.** This presentation and the TLNHDR’s subsequent assessment are made on the basis of the most detailed and contemporary data currently available, and as accurately as possible. In areas where such data is unavailable, assessments are based on information obtained through available reports and documents, and from discussions with relevant stakeholders. The assessment details the reality of the country’s development—a reality that contrasts with stereotyped views often encountered internationally of a country mired in poverty, with ongoing conflicts and a potential to succumb to the ‘resource curse’.

- **Generate discussion on the appropriateness and relevance of the various strategies available for the development of the non-oil economy, and particularly the rural sector.**

This will be the most crucial issue facing Timor-Leste in the coming years. Consequently, the TLNHDR focuses on how the country's petroleum wealth can most effectively be used for implementing pro-poor economic growth, developing the rural sector, enabling poverty reduction, facilitating employment generation and promoting private sector development. In its discussion of strategies for developing the rural economy, and in its presentation of a Macro-Economic Framework for achieving the Millennium Development Goals (MDGs), the TLNHDR directly addresses these issues and makes specific suggestions for strategic development in particular sectors.

### **Achievements since Independence**

In the initial years of the country's post-independence development, major steps were taken to rebuild the nation. Free and fair elections were held, and a Constitution drafted, with almost all the constitutionally mandated institutions created in a relatively short period of time, by 2005. The post-2002 Fretilin Government addressed a range of development challenges in a pro-poor growth *National Development Plan* (NDP) applauded by donors as an exemplar of a Poverty Reduction Strategy. The Plan put forward a 'Development Vision', which has continued to act as a guide to the implementation of sector development strategies. Within the crucially important petroleum sector, the Government devised a legal framework for production, taxation and revenue management, viewed favourably as an exemplar of international best practice, consistent with the principles adopted by the Extractive Transparency Initiative.

### **Underlying Problems and the 2006 Crisis**

**Accompanying these achievements, however, there remained pervasive, ongoing problems—high youth unemployment, falling per capita incomes and increasing poverty rates in rural areas.** These problems undoubtedly had an influence on the outbreak of the country's 2006 crisis, which also resulted from continuing divisions within the police, military and the political elite.

Economically, the 2006 crisis had a profound impact. Progress during 2002-5 was set back dramatically. The non-oil economy contracted by 5.8 percent, delivery of social and welfare services was severely restricted, and unemployment worsened. 2007 data indicate that per capita income in the non-oil economy was approximately 20 percent lower in 2006 than in independence year 2002. As a result of the crisis, at the beginning of 2007, approximately 150,000 internally-displaced people were living in temporary camps, in poor conditions, fearful of returning to their villages.

## **Post 2006: Addressing National Priorities and Promoting Growth**

Faced with this situation, subsequent governments and particularly the present coalition Government—*Aliança Maioria Parlamentar* (AMP), led by Prime Minister Xanana Gusmão, have focused on addressing the underlying issues contributing to the crisis—improving public safety and security, enhancing social protection, addressing the problems faced by youth, tackling unemployment, improving social service delivery, and promoting clean and effective government. The TLNHDR assesses the extent to which the Government's strategy of focusing on these national priorities has succeeded in addressing the main post-2006 problem areas, and examines its emerging strategy for promoting growth, human development and poverty reduction, as the Government finalises its *Strategic Development Plan* (SDP) for the years 2011-30.

## **Human Development in Timor-Leste**

The 2011 TLNHDR provides a thorough description and assessment of the current state of human development in Timor-Leste. According to the most detailed assessment of living standards currently available—as presented in the 2007 Household Living Standards Survey—poverty is widespread in Timor-Leste. This survey concluded that approximately 50 percent of the population was living in poverty in 2007. The next surveys enabling us to track poverty are the 2010 Census and a further household survey, in 2011. The results of the census should be available later in 2011, and of the household survey by 2012. Based on data made available from the Ministries covering the years to the end of 2009, the TLNHDR has reached the conclusion that these surveys are likely to show that **poverty conditions have improved substantially since the 2007 Household Survey**. Given the Government's policies of cash transfers to vulnerable groups, the subsidising of food prices, and the creation of jobs through initiatives funding labour-intensive employment in areas such as infrastructure development, it is highly likely that poverty levels have improved since 2007. From 2007-9, for example, Government funded labour schemes employed 40,000 Timorese annually, and the 2009 *Pakote Referendum* infrastructure development programme created 64,000 short-term jobs in the rural sector. Government data estimate economic growth at 12.2 percent in 2009, with average per capita incomes in the non-oil economy increasing from \$398 per year in 2007 to \$499 in 2008 and \$599 in 2009. Other estimates, from the World Bank and the Asian Development Bank, give somewhat different rates of growth for 2009, respectively of 5.0 and 7.4 per cent. Whichever estimate is taken, the relatively high rate of economic growth is likely to have had a positive impact on poverty. Beyond these projections and assumptions, however, as yet there is insufficient data to confirm these trends definitively. Significantly, however, further evidence for 2008-9—based largely on district reports from the Ministries of Agriculture, Economy and Development, and Health, together with reports from NGOs working in the districts and from

observations by those working in the President's Office on supporting small-scale poverty reduction village projects—suggests that in most districts, poverty levels may have improved. Recent World Bank predictive estimates suggest a poverty incidence rate of 41 percent in 2009. Accepting this approximate figure, and on the basis of current trends, poverty levels are likely to decline further in the coming years. Despite this improvement, however, there remain significant human development problems, notably in the areas of energy provision, food security and nutrition, access to education and health services and high levels of employment—of concern particularly for the country's youth. The TLNHDR argues that these pressing problems can only be addressed sustainably through the development of appropriate strategies for the development of the non-oil economy and particularly of the rural sector.

### **Promoting Sustainable Development of the Rural Sector and the Non-Oil Economy**

**Timor-Leste currently is in a challenging situation. Despite recent progress, many of its population remain poor, and there is considerable scope for improvements in levels of human development. To meet present and future needs the wealth from its oil must be utilised effectively to promote sustainable development of the non-oil economy.** This raises a key question of how large accumulations can best be managed economically and politically to promote development. Discussions on this issue are ongoing, with Government plans to increase the level of withdrawals from the Petroleum Fund to finance key areas of development, such as infrastructure. The TLNHDR engages in this debate, by examining how withdrawals have been used thus far and suggesting ways in which use of withdrawals can be improved—based on international best practice, and assessing in detail the possible risks to ongoing good management. In contrast to commentators who argue that the portents for good management are not wholly favourable, the TLNHDR concludes that successive **Governments in Timor-Leste have shown themselves to be fully capable of managing the Fund. Additionally, in recent years, the Government has succeeded in reducing the potential for seriously divisive conflict. However, the potential for conflict remains, and can be fuelled by continuing sources of resentment. As the TLNHDR argues in its last two chapters, potential bases for resentment can best be addressed by an inclusive and equitable development of the non-oil economy—reducing poverty in the agricultural sector by improving rural livelihoods and generating employment in the non-agricultural sectors.**

### **Achieving the Millennium Development Goals**

As outlined in the Report, Timor-Leste has made substantial progress in many MDG areas. It has achieved its 2015 goals for infant and under-5 mortality rates, for antenatal care coverage, and for the proportion of TB detected cases (under Directly Observed Therapy Short Course - DOTS). It is on track to achieve its MDGs in areas such as net enrolments in primary education, proportion of births attended by

skilled health personnel, contraceptive prevalence rate, incidence rates associated with TB, and proportion of population with access to an improved drinking water source. However, Timor-Leste remains off-track for achieving remaining MDGs, such as proportion of population below the national poverty line, prevalence of underweight children under five years of age, proportion of children reaching fifth grade, proportion of children immunized against measles, maternal mortality ratio, proportion of population with comprehensive correct knowledge of HIV/AIDS, incidence associated with malaria, and proportion of population using an improved sanitation facility.

The Macro-Economic Framework presented in the TLNHDR outlines strategies for Timor-Leste to achieve all its MDGs by 2025. The framework is developed on the basis of a growth strategy, based on an average growth rate of eight percent in the non-oil economy over the next 15 years. The TLNHDR argues that such a strategy is feasible, financially sustainable, and will enable efficient and productive use of the Petroleum Fund, provided efforts are made to develop appropriate strategies for the development of the non-oil economy and primarily for the rural sector, mobilizing domestic resources to promote private sector development.

### **Strategic Development Plan**

The TLNHDR presents detailed strategies for developing the non-oil economy, reducing poverty and improving current levels of human development and MDG indicators.

The analyses, assessments and strategies for developing the non-oil economy and the rural sector, as presented in the TLNHDR, will be of use to the Government as it engages in its ongoing stakeholder consultations and moves towards the final formulation of its *Strategic Development Plan* (SDP), striving to realise the Development Vision set out by and for its people at independence.

The TLNHDR will also enable the international community to have a clear and detailed picture of the substantial achievements of the country thus far and the challenges that remain in the areas of human development.

### **Challenges and Risks**

**The key issue for the country is the management and use of its petroleum resources.** Whilst in recent years there has been an obvious need to address short term needs via cash transfers and subsidies, for the longer-term, revenues must be focused on investing in public assets that raise productivity. There is an obvious danger to the sustainability of the Petroleum Fund, the single largest revenue source for the country, if the government makes excessively large withdrawals beyond its

delivery capacity to finance a high and rising level of public investment. As outlined in the TLNHDR's Macro-Economic Framework for the attainment of the MDGs, **a moderate-to-high growth strategy, emphasising rural development, from within a human development framework, can contain inequality and spread more widely the benefits of growth.** Such a strategy is also likely to focus more on pro-poor sectoral allocations of public expenditure, thereby enabling the use of the Petroleum Fund to benefit the population more equitably and at the same time reduce the rate of depletion of the fund. This will be a major aim of the forthcoming *Strategic Development Plan (SDP)*.

**Increasing disparities between rural and urban areas are a further major challenge for the promotion of pro-poor, human development in the coming years. A renewed focus on the rural economy is an urgent priority.** Policies for enhanced investment in agriculture and the rural economy need to be put in place to increase incomes, create employment, and boost demand for local products. Budgetary allocation to the agricultural sector in the past has not been commensurate with the needs of the rural population, and this requires rectification.

**Whilst poverty levels have improved in recent years, poverty remains pervasive.** Policies to address levels of poverty cannot rely solely on the “trickle down” effect of petroleum wealth, but as shown by the experiences of countries in the Southeast Asian region, policies and programmes must be put in place to ensure that growth is inclusive.

**Since substantial increases in investment are required for the development of the non-oil economy and the rural sector, Timor-Leste needs to strengthen its communications, transport and financial infrastructures within a relatively short time-frame.** The present regulatory framework is not particularly conducive to investment, and improving this is vital. The foreign investment law needs to be enacted as soon as possible to attract investments capable of generating employment, improving labour skills, and promoting technological upgrading.

Timor-Leste's natural resource base is fragile and fast degrading. Land, water and forested area are under considerable stress. Greater attention is needed to deal with the impact of the environment on poverty, through the promotion of measures to conserve and protect the natural resource base so that development activities are environmentally sustainable.

**Timor-Leste is experiencing demographic changes with profound implications for its future development.** It has one of the highest birth rates in the world, the majority of its population are below the age of 21, and migration from the countryside to the capital Dili is at very high levels. The challenges of employing this rapidly expanding urbanising population are immense, as are the challenges for

reducing its current high birth rates, not least by a significant increase in investment in health and education.

**Improvements in governance are a crucial precondition for achieving sustainable growth. In recent years, budget execution has improved substantially.** However, these changes need to be buttressed by concomitant changes in audit function and anti-corruption mechanisms, via the development of a fully-functioning independent audit agency. An enhanced anti-corruption system also needs to be fully implemented.

**As outlined in the draft of its *Strategic Development Plan* the Government is aware of the importance of these development challenges, and is further developing and refining its specific strategies to address them.** Ongoing progress in addressing these challenges is crucial, since not addressing them adequately could exacerbate or revive factors that have been shown to impact on stability in the past. These include groups exploiting grievances based on continuing levels of unemployment and poverty, discontent within the large youth population sometimes manifest as gang violence, tensions within the security sector, a sense that formal judicial processes are inadequate to guarantee criminal accountability, disputes over unresolved land ownership issues accumulated over decades, and dissatisfaction arising from perceived lack of good governance practices. The Government has addressed these issues and continues to address them, particularly in relation to the security forces, where substantial progress has been made in recent years.

**Successfully promoting pro-poor policies also fundamentally requires a greater involvement in decision-making by those for whom many of the policies are devised, namely Timor-Leste's rural population.** Successfully promoting human development and alleviating poverty will depend on rural communities being convinced that the implementation of strategies devised will be beneficial for them. Hence the importance of villagers being involved actively in development decisions affecting their livelihoods, of their meaningful participation, promoted via an effective decentralisation to the districts and below. Parliament currently is still working on laws introducing municipal governments in each of the country's 13 districts, and on the process of elections of these governments. Establishing district-level governments and devolving genuine power and authority to them will go some way to decentralising decision-making. Recently, the Government decided to postpone the municipal elections until 2014. It would be of considerable benefit if these could be introduced earlier, to make the political system more inclusive, enabling local participation through municipal governments. There is little doubt that capacity-building at local level is required for the successful introduction of local government. Yet, capacity does already exist in many areas, and the lack of it should not be used as a justification for not extending political participation to the districts and villages.