República Democrática de Timor-Leste

State Budget 2020

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 2020 State Budget, following the approval of the Council of Ministers.

The documentation for the 2020 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 2020 State Budget.

Sara Lobo Brites
Vice-Minister and Acting of Minister of Finance

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2.1 Executive Summary

Government Policy

The Government of Timor-Leste's policies as guided by Strategic Development Plan are laid out in the Annual State Budget, with the long-term objective to become an upper middle income country by 2030. Achieving this goal, the Government is investing in infrastructure and key economic and social sectors including health, education and agriculture. Budget Book 1 for 2020 summarizes the plans on pursuing these policies for the current fiscal year.

Table 1: Combined Source Budget 2018-2024, $million

	2018 Actual	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Combined Source Budget	**1,343.9**	**1,681.3**	**1,841.5**	**2,276.6**	**2,127.2**	**1,892.2**	**1,770.7**
Government Expenditures by Fund	**1,172.7**	**1,482.0**	**1,668.0**	**2,193.7**	**2,091.9**	**1,878.5**	**1,757.0**
CFTL (excl. loans)	**1,119.0**	1,375.0	**1,574.5**	**2,100.0**	**2,023.9**	**1,818.0**	**1,708.0**
HCDF	14.5	20.0	**13.0**	13.5	14.1	14.6	15.2
Borrowing/Loans (disbursements)	39.2	87.0	**73.0**	80.2	53.9	45.9	33.8
Europe Union (Direct Budget Support)	-	-	**7.5**	8.6	5.0	2.8	-
Development Partner Commitments	**171.2**	**199.2**	**173.5**	**82.9**	**35.3**	**13.7**	**13.7**

Source: National Directorate of Budget and Development Partners Management Unit, Ministry of Finance, 2019.

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. The real non-oil GDP growth was -0.8% in 2018, recovering from -3.8% in 2017. Despite Timor-Leste experiencing negative growth, household consumption continued to increase, which suggesting that living standards are improving. There were some challenges during 2018 that have continued into 2019, and these have affected the growth forecasts. The 2020 Budget will deliver strong growth of 6.0%.

Expenditure

Total expenditure in the 2020 budget is $1,668.0 million (excluding donor funded activities of $173.5 million). The total 2020 State Budget 12.6% higher than that allocated for 2019. This is because the Government plans to commence large social capital and economic development programmes in 2020.

Social capital, national connectivity and economic development are priorities in the 2020 State Budget. 28.4% of the proposed 2020 proposed General State Budget will be allocated to the Social Capital Sector's Ministries and Agencies, with 9.5% going to Education and 13.0% to Social

Protection and 7.3% to Health. The Government will introduce programmes to increase employment and self-reliance for Timorese citizens. The Government has allocated budget for the construction of houses for veterans, in line with its objectives to combat poverty.

Line ministries and autonomous agencies have been allocated a 23.1% overall increase in Goods and Services allocations from 2020. This increase will support them to execute their priorities in 2020. Increases in Goods & Services allocation will impact national connectivity positively. This includes purchases of boats for public water transportation and provision of new aviation services. The Government will also purchase a fleet to patrol the maritime borders of Timor-Leste to keep them secure.

Table 2: Fiscal Table, $m

	2016 Actual	2017 Actual	2018 Actual	2019 Budget	2020 Budget	2021	2022	2023	2024
Total Expenditure (incl. loans)	**1,658.6**	**1,208.4**	**1,172.7**	**1,482.0**	**1,668.0**	**2,193.7**	**2,091.9**	**1,878.5**	**1,757.0**
Total (excl. loans)	**1,628.0**	**1,178.1**	**1,133.5**	**1,395.0**	**1,595.0**	**2,113.5**	**2,038.0**	**1,832.6**	**1,723.2**
Recurrent	1,056.4	947.5	828.8	1,049.8	**1,147.6**	**1,185.7**	**1,233.2**	**1,282.5**	**1,333.8**
Salary and Wages	178.6	197.0	197.2	214.2	**235.6**	245.0	254.8	265.0	275.6
Goods and Services (inc. HCDF)	406.8	345.4	319.1	472.9	**582.3**	597.8	621.7	646.6	672.4
Public Transfers	471.1	405.0	312.5	362.7	**329.7**	342.9	356.6	370.9	385.7
Capital	602.2	261.0	343.9	432.3	**520.4**	**1,008.0**	**858.7**	**596.0**	**423.2**
Minor Capital	20.8	12.4	7.8	31.5	**31.5**	32.8	34.1	35.5	36.9
Capital and Development (including loans)	581.4	248.6	336.1	400.7	**488.8**	975.2	824.6	560.5	386.3
Revenue	**744.5**	**671.2**	**741.1**	**730.2**	**747.3**	**748.1**	**726.8**	**701.2**	**685.4**
Domestic Revenue	199.7	189.6	190.7	201.2	**210.5**	221.4	233.2	242.3	256.1
Estimated Sustainable Income (ESI)	544.8	481.6	550.4	529.0	**536.8**	526.7	493.6	458. 9	429.3
Fiscal Balance	**(914.1)**	**(537.2)**	**(431.5)**	**(751.8)**	**(920.8)**	**(1,445.6)**	**(1,365.1)**	**(1,177.**3)	**(1,072.**6)
Financing	**885.8**	**871.8**	**771.4**	**754.4**	**920.8**	**1,445.6**	**1,365. 1**	**1,177.**3	**1,072.** 6
Excess Withdrawals from the PF	700.0	597.1	432.1	667.4	**459.7**	1,209.9	1,256.0	1,079.1	988.1
Use of Cash Balance	155.1	244.4	300.2	-	**380.6**	**146.9**	**50.1**	**49.6**	**49.7**
Cash Balance of Treasury	155.1	244.4	300.2	-	254.3	50.6	50.1	49.6	49.7
Cash Balance of RAEOA/ZEESM	-	-	-	-	126.3	96.3	-	-	-
Borrowing/Loans (disbursements)	**30.6**	**30.3**	**39.2**	**87.0**	**73.0**	**80.2**	**53.9**	**45.9**	**33.8**
European Union – DBS	**-**	**-**	**-**	**-**	**7.5**	**8.6**	**5.0**	**2.8**	**-**

Sources: Ministry of Finance, 2019.

Domestic revenues

In 2020, domestic revenues growth is expected to continue on a growth path following the 2017 and 2018 slowdown, reaching $210.5m. This positive trend is driven by the positive macro-economic performance of the country, stronger private sector performance, continuation of government construction contracts and introduction of new fiscal instruments. Non-oil revenue is expected to keep growing in the medium term thanks to a combination of improvements in administration, fiscal reform and the introduction of new fiscal instruments, at current economic growth expectations.

The Estimated Sustainable Income (ESI) is the sustainable amount of petroleum revenue which can be withdrawn from the Petroleum Fund each year. Since spending only up to non-oil revenue and the ESI allows the maintenance of fiscal sustainability, ESI is considered a component of total revenue. The ESI for 2020 is calculated at $536.8 million.

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 Direct Budget Support for Europe Union to finance the deficit in 2020.

The total amount budgeted to be withdrawn from the PF in 2020 is $996.5 million, with excess withdrawals of $459.7 million. The Government considers that excess withdrawals are necessary in the medium term to finance priority capital expenditures.

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 2020 is $73.0 million.

The total use of the cash balance for 2020 State Budget is $380.6 millions, of which from the Consolidated Fund of Timor-Leste (CFTL) is $254.3 million and from RAEOA/ZEESM is $126.3 million

Total Budget Direct Support from Europe Union for 2020 State Budget is $7.5 millions. This is a new source of financing that is introduced and included in this budget, as the support will be used directly by Government's institutions.

2.2 Economic Overview

2.2.1 Summary

Table 3: Economic Indicators, 2019-2021, %

Summary	Forecast		
	2019	2020	2021
Real GDP (non-oil)	4.0%	6.0%	4.7%
Inflation CPI	1.0%	2.7%	2.4%

Source: National Directorate of Economic Policy, Ministry of Finance, 2019.

- Real non-oil GDP growth is expected to accelerate, with growth of 4.0% in 2019 and 6.0% in 2020. This return to growth is driven by an end to political uncertainty and return to strong government expenditure.
- Inflation is expected to remain low and stable at 1.1% in 2019 and 2.7% in 2020. This will positively contribute to increasing Timor-Leste competiveness, with inflation expected to be lower than the regional average.
- The exchange rate forecast suggests there will be some small depreciation in the near future, providing an overall stable foundation for traders, alongside improved competitiveness.

2.2.2 Macroeconomic Trends

2.2.2.1Growth

Table 4: Economic Growth, 2017-2020, %

Country	Actual		Forecast	
	2017	2018	2019	2020
World	3.8%	3.6%	3.3%	3.6%
Advanced Economies	2.4%	2.2%	1.8%	1.7%
Emerging and Developing Economies	4.8%	4.5%	4.4%	4.8%
Emerging and Developing Asia	6.6%	6.4%	6.3%	6.3%
China	6.8%	6.6%	6.3%	6.1%

Source: IMF World Economic Outlook April 2019.

Timor-Leste

Timor-Leste experienced GDP growth, averaging 4.7% per year over 2008-2018. These strong 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[1] 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.

For the first time since 2006, the non-oil GDP growth in 2017 rate was negative (-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. Government spending was lower as a result of a lower budget ceiling compared to 2016 and relatively low execution rates. Political uncertainty also led to lower business activity. The coffee harvest, the main source of exports, was affected by a poor season.

However, aided by the low inflationary environment, household consumption increased by 7.0% and 2.2% in 2017 and 2018, respectively. Which suggests that living standards continued to increase in Timor-Leste.

[1]Withdrawals from the Petroleum Fund in excess of the ESI.

Table 5: 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: General Directorate of Statistics, Ministry of Finance, 2019.

International

Globally, after strong growth in 2017 and early 2018, growth is now projected to slow from 3.6 percent in 2018 to 3.3 percent in 2019. This reduction is driven by the decline in growth rate of advanced economies and the emerging market and developing Asia, from US-China trade tension, tighter policy in response to macroeconomic imbalances in Argentina and Turkey, credit tightening in China, weakness in Germany's auto sector, and higher interest rates. However, the global growth is projected to stabilize in 2020 at around 3.6 percent, mainly due to a rebound in emerging markets and developing economies especially in Argentina, Turkey and a few other stressed economies. 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 (%)

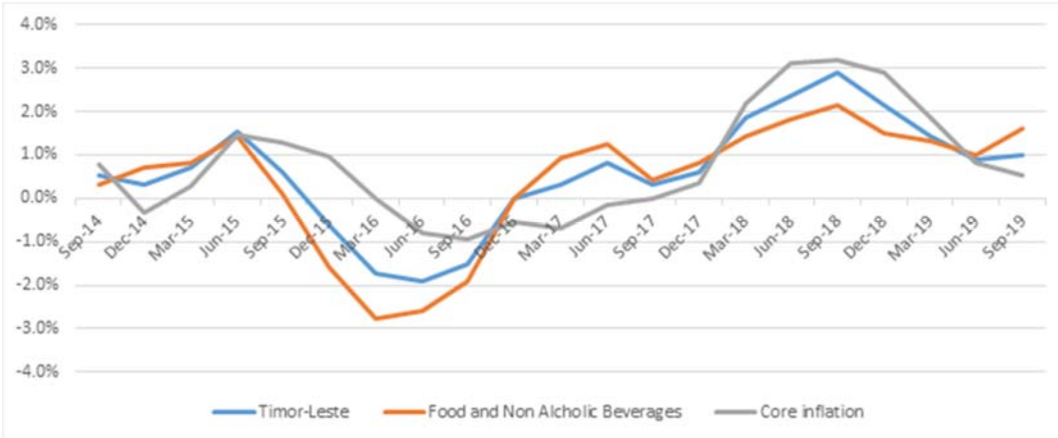
Country	Actual		Forecast	
	2017	2018	2019	2020
World	3.2%	3.6%	3.6%	3.6%
Advanced Economies	1.7%	2.0%	1.6%	2.1%
Emerging and Developing Economies	4.3%	4.8%	4.9%	4.7%
Emerging and Developing Asia	2.4%	2.6%	2.8%	3.1%
Timor-Leste*	0.5%	2.3%	1.0%	2.7%

*Source: IMF World Economic Outlook April 2019. *Ministry of Finance forecast.*

Timor-Leste

With year on year inflation in September of 1 %, 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 decreased 2% year on year in June. This moderates earlier upward swings in food prices. Domestic food prices rose in June, though these remained muted at 1.0% and it is expected that the current world food markets will continue to provide a moderating impact on prices in the near future. A 9.0% increase in education costs will affect annual inflation in Timor-Leste throughout 2019, though this is lower than the 16.6% increase in 2019.

Figure 1: Change in Consumer Price Index Timor-Leste 2014-2019 (%)



Source: Ministry of Finance, National Directorate of Economic Policy and General Directorate of Statistics, 2019

International

Consumer price inflation is set to remain favourable, with global inflation forecast at 3.6% by the IMF. 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. Inflationary pressures have already fallen sharply in China as activity has moderated. 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 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. However, for the period following this, the oil market began to recover reaching an average of $64.8 per barrel from January to August 2019, though this is still lower than average price seen in September 2018 at $81 per barrel. This strengthening recovery has been driven by the production cut by OPEC. The oil price is projected to increase only moderately in the near future.

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 Prices Forecast, international food prices have continued to decline from 2011, though prices started to increase from a low of $74.5 in August 2016, then decline to $67.7 in August 2019. The increasing cost of energy and weather variability could stabilise food prices higher for the remainder of the year. The World Bank is forecasting that food prices will rise marginally throughout the rest of 2019 and 2020, however the increase is small, and overall food prices are expected to remain relatively low. This will benefit poorer households in Timor-Leste.

Figure 2: Commodity Price Indices 2011-2021

Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2019

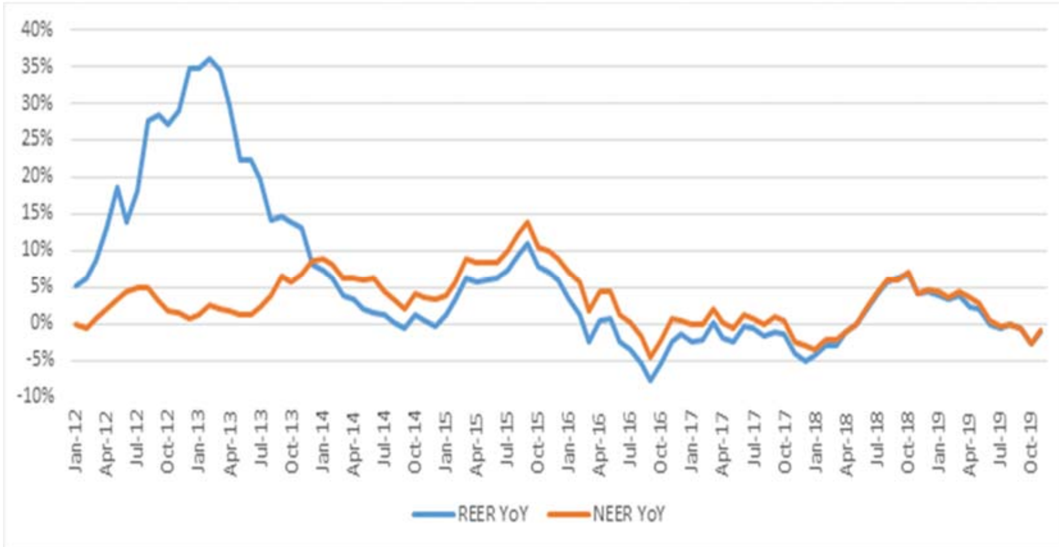
2.2.2.3 Exchange Rates and Competitiveness

Between November 2018 and November 2019 the US dollar depreciated by 1% against a weighted basket of currencies of Timor-Leste's trading partners (the nominal effective exchange rate, NEER). This depreciation makes Timorese non-oil exports cheaper which is good for 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. The REER has depreciated by 1.2% between November 2018 and November 2019, 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 3: Exchange Rate Indices 2012-2019 (%)



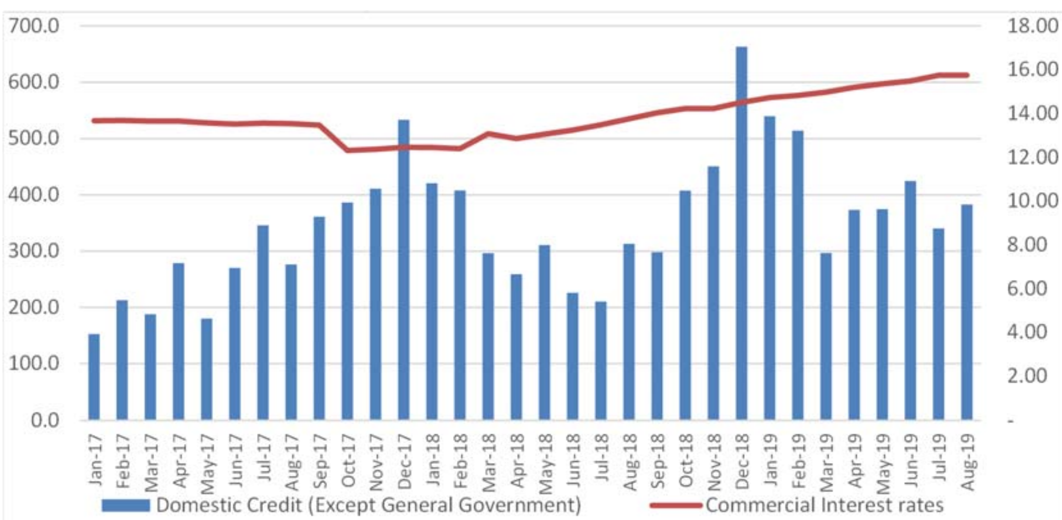
Source: National Directorate of Economic Policy and General Directorate of Statistics, Ministry of Finance, 2019

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 15.75% in August 2019. Total domestic credit, excluding general government, was $383m in August 2019, a reduction from the peak at the end of 2018.

Figure 4: Commercial Interest Rates and Credit



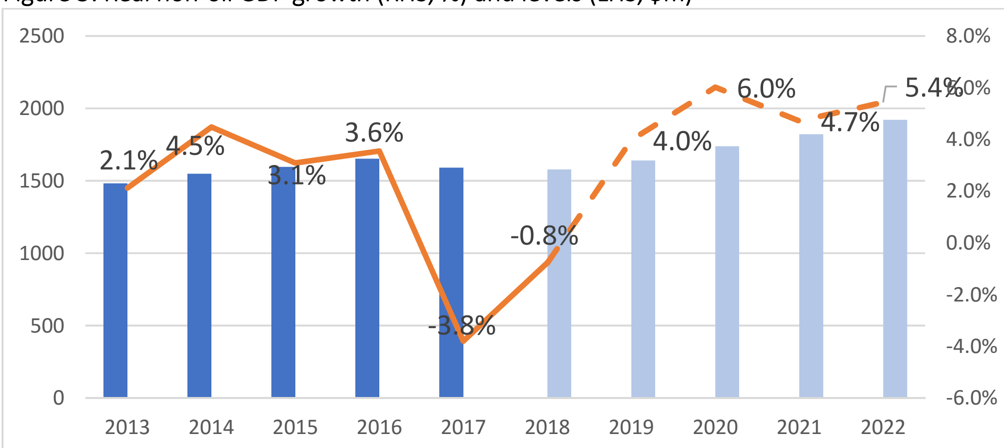
Source: Central Bank of Timor-Leste, 2019. Interest Rate (RHS, %), Credit (LHS, $m).

2.2.4 Economic Outlook

The Ministry of Finance is forecasting non-oil GDP growth to be +4.0% for 2019. With the uncertain economic environment finally ending in 2018, growth is expected to pick up in 2019. Factors contributing to high 2019 growth include a return to normal budgeting procedures and an increase in private sector investment.

For 2020, the expansionary fiscal position is expected to enable high growth of 6.0%, given a budget ceiling of $1.668bn. Over the medium term, the government anticipates high growth rates, driven by private sector-led, sustainable development.

Figure 5: Real non-oil GDP growth (RHS, %) and levels (LHS, $m)



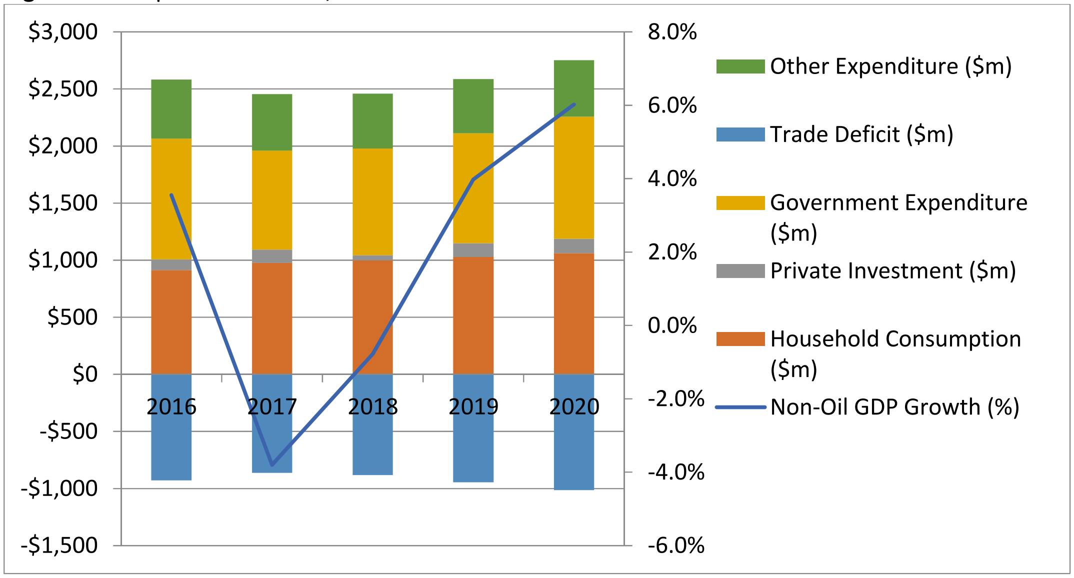
Source: Timor-Leste National Accounts 2000-2017, Economic forecast, General Directorate of Statistics and National Directorate of Economic Policy, Ministry of Finance, 2019.

Living standards are expected to improve with household consumption growing as it returns to the trends seen in previous years. Steadily growing consumption is boosted by a low inflationary environment. Looking forward across the medium-term, this environment is likely to continue given regional growth rates, the world commodity price outlook and exchange rate projections.

Public sector investment is expected to provide a strong contribution to growth. Infrastructure projects, especially in education, health, and water and sanitation will commence. These will improve social capital as well as providing jobs and economic activity during construction. Road and bridge projects continue to be built or improved and with greater momentum in 2020, providing better and lower cost transportation within the country. 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.

Large-scale private sector investments will result in a significant increase in private sector investment. 2020 will see continued construction on the Tibar Bay Port, and the expansion of existing commercial and retail properties 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 6: Components of GDP, 2016-2020



Source: Timor-Leste National Accounts 2000-2018, General Directorate of Statistics and National Directorate of Economic Policy, Ministry of Finance, 2019.

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

2015 $m prices	**2016**	**2017**	**2018**	**2019 f**	**2020 f**	**2021 f**	**2022 f**
Private Consumption	976	1,011	1,037	1,054	1,090	1,127	1,167
Public Consumption	927	873	864	971	1,072	1,110	1,150
Total Consumption	1,902	1,883	1,901	2,025	2,162	2,237	2,317
Private Investment	126	143	70	147	153	197	262
Public Investment	527	401	465	397	425	439	453
Total Investment	653	544	535	544	578	636	715
Other	26	26	23	17	13	10	7
Total National Expenditure	2,582	2,454	2,459	2,586	2,753	2,883	3,039
Exports	53	32	35	34	36	38	41
Imports	(981)	(896)	(916)	978)	(1,049)	(1,099)	(1,160)
Non-oil GDP	1,653	1,590	1,578	1,641	1,740	1,822	1,921

Source: Timor-Leste National Accounts 2000-2018 and Economic Forecasts, General Directorate of Statistics and National Directorate of Economic Policy, Ministry of Finance, 2019. Forecast 2019-2022

Risk and Uncertainty

Forecasts provide a current view on the most likely growth trajectories, but are always uncertain and subject to revision. The main uncertainties in the forecast come from imports and government budget execution. If the new government spending is particularly import-dependent, meaning that much of the new spend goes to goods and services from outside Timor-Leste, the forecasts for future years may be reduced downwards. This depends on the absorptive capacity of the Timor-Leste economy. If there is a large change in execution rates this may have a noticeable impact on the economy, especially given the large percentage of non-oil GDP that the budget makes up.

2.3 National Development and Priorities

In June 2019, Government set the objectives and priorities for 2020 through to 2023. These objectives and priorities are aligned with the Government five-year programme, the SDP and take into consideration the findings from the UN Voluntary National Review (VNR) on SDG implementation in Timor-Leste. The full set of priorities can be found in the *"Guidelines for the preparation of the Budgeting Proposals 2020-2023 of His Excellency, The Prime Minister, June 2019".* The Government has set two (2) overarching objectives for 2020-202

Table 8: Objectives of the VIII Government, 2020-2023

Objectives	Baseline	Key Indicator
Maintain an annual economic growth rate above 7%	2018-0.8%[2]growth	Annual Growth rate of real GDP 7% [3]
Reduce the poverty rate by 10%	41.8% of population living below the national poverty line[4]	31.8% of population living below the national poverty line.[5]

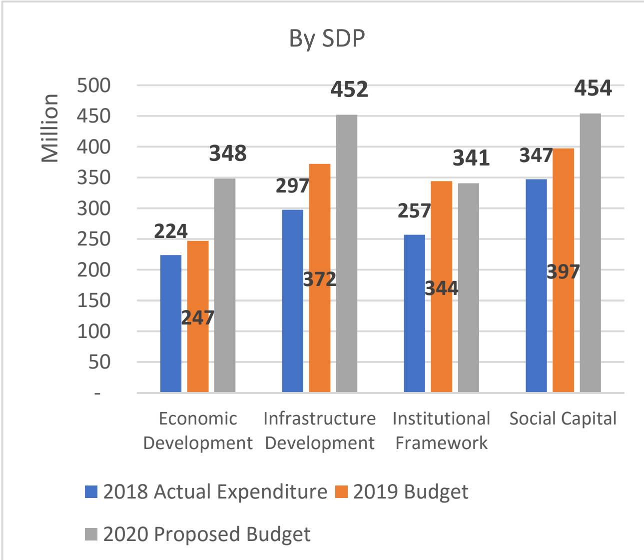
2.3.1 Analysis of the 2020 Proposed General State Budget by Sector

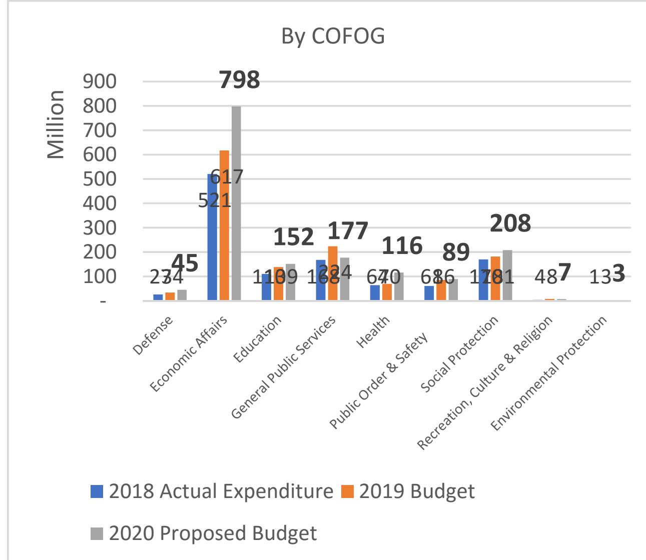
Timor-Leste's Strategic Development Plan is organized around four pillars: Institutional Framework, Social Capital, Economic Development and Infrastructure Development, where the last three have been designed as priority in the VIII Constitutional Government's mandate. The proposed 2020 Budget allocates the largest share to the Social Capital Sector, followed by Infrastructure Development, Economic Development and Institutional Framework and, excluding however loan disbursements.

Following instead the international sectorial and more detailed classification COFOG (see Figure 7), it can be observed that the Economic Affairs sector remains the largest, in line with previous year, followed by Social Protection, General Public Services, Education and Health. 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.

2 National Accounts Timor-Leste 2018, Ministry of Finance
3 Aligned to SDG goal no. 8
4 Timor-Leste Survey of Living Standards (TLSLS) 2014
5 Aligned to SDG goal no. 1

Figure 7: Comparison of 2018 Expenditure, 2019 Budget and proposed 2020 Budget by Sector





*Source: General Directorate Planning and Budget, Ministry of Finance, 2019. *This does not include loans and development partner planned disbursements, but it includes all capital development measures, including allocations through the Infrastructure Fund.*

2.3.2 Government Priorities for 2020

The approved draft General State Budget aims to finance the VIII Constitutional Government's Program for the 2020 fiscal year. Five sectors are defined as priority for the 2020 Budget:

Table 9: Priorities of the VIII Government, 2020

No.	Priority
1	Social Capital- Social Welfare, Social Protection and Citizenship
2	Economic Development- Invest in the Economy and Public Finances of the Country
3	Improve National Connectivity
4	Consolidation and Strengthening of Defence, Security and External Relations
5	Consolidation and Strengthening of Justice, Democracy and Human Rights

The proposed General State Budget allocations aim to reflect, therefore, such priorities. The respective new measures for each priority are described below:

Social Capital – Social Welfare, Social Protection and Citizenship

28.4% of the proposed 2020 proposed budget will be allocated to the Social Capital Sector's Ministries and Agencies, with 9.5% going to Education, 13.0% to Social Protection and 7.3% to Health. New measures in the Social Capital Sector include:

- Construction of housing for veterans
- Investment in water and sanitation
- Construction of Health Centres and Health Posts
- Construction of transmission towers for TV
- Purchase of ambulances
- Construction of schools and classrooms

- Contributions to the social security scheme

The Economic and Infrastructure Development, including the National Connectivity sector covers 50.2% of the proposed 2020 budget. New measures in this sector include:

Economic Development – Invest in the Economy and Public Finances of the Country

These new measures seek to facilitate investment in the private sector, job creation, and support the agricultural sector.

- Expo in Dubai
- Subsidy for cooperative groups
- Subsidy for self-employment targeting women groups in rural areas

Improve National Connectivity – Infrastructure, Logistics

- Purchase of the Nakroma Ferry II
- Provision of new civil aviation services

Consolidation and Strengthening of Defence, Security and External Relations

- PNDS.
- Support to Community Police (Policia Komunitaria)
- Support to Border Police
- Purchase of patrol fleet to protect the maritime borders of Timor-Leste

For exact allocations, see Section 2.5.1.1 on the list of all key measures with corresponding allocations.

2.3.3 Sustainable Development Goals Voluntary National Review

The Sustainable Development Goals are a collection of 17 global goals set by the United Nations General Assembly in 2015 for the year 2030. These goals relate to improving a country's poverty, inequality, climate, environmental degradation, prosperity, and peace and justice. In 2019, Timor-Leste conducted a Voluntary National Review to determine its progress against these goals and recommendations for next steps. The below conclusions were published in June 2019:

- Timor-Leste's achievements as the newest country in Asia are underpinned by its commitment to reconciliation, inclusion and democracy. The country has made the journey from a period of conflict to become a democratic nation focused on state-building and accelerating progress on sustainable development.

- More effort is now required to tackle health and education disparities between municipalities, focus on quality education, and ensure vulnerable women and persons with disabilities are not left behind.

- With one of the youngest populations in the world, and a nascent private sector, making sure there are enough jobs for the large number of young people entering the labour market will require investment in education, skills and the generation of decent jobs. Economic diversification and creating jobs in productive sectors, such as labour-intensive manufacturing, tourism and agriculture, will help grow the non-oil economy.

- Tackling high rates of child malnutrition and food insecurity and improving access to clean water and sanitation are vital and require sustained investment. While the number of stunted children (low height for age) is declining, it's still very high. Accelerating improvements in nutrition will make a huge difference to child learning outcomes and productivity. Progress in improving water and sanitation, a key driver of malnutrition, has been made, however more needs to be done to sustain and scale up these efforts.
- Securing improvements in the justice sector is important for maintaining and achieving progress on all SDGs. Like many countries emerging from conflict, the country is still grappling with how to strengthen the justice sector. The importance of ensuring access for all vulnerable citizens and addressing capacity gaps within the sector was identified as a key priority in all the consultations organised to feed into this VNR report.
- With low levels of public revenue, new forms of financing, technology and technical support are required. One of the key recommendations of the assessment is for the country to develop an integrated financing strategy. This would involve estimating the scale of investments required in public and private financing and form a basis for targets for mobilising resources for the SDP.

2.4 Revenue

2.4.1 Overview of Revenue Projections

Non-oil domestic revenues are expected to regain strength in 2020, reaching $210.5, 5% higher than 2019. Following the stagnation of 2017 and 2018, largely driven by political uncertainty, constrained budgetary spending and weak macroeconomic performance, domestic revenue is now expected to grow positively year-on-year in both 2019 and 2020, pushed by greater private sector activity, political stability and the continuation of government capital projects. The positive trend is expected to continue until 2024, at the macro-economic growth expectations.

Despite the expected positive growth in domestic revenue, Timor-Leste is highly dependent on oil revenue which represents over 80% of total revenue. However, petroleum revenues are expected to decline as production from existing fields draws to a close. 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 and revising the existing ones, revisiting tax policies and legislation that promotes investments and increase revenue collection could considerably improve the fiscal and non-fiscal revenues. It is important to note that the forecasts do not include additional revenue from the aforementioned reforms, as these are still to receive Parliamentary approval.

Table 10: Total Revenue, 2018 – 2024, $million

	2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Revenues	**637.5**	**937.5**	**805.5**	**365.5**	**254.8**	**337.8**	**256.1**
Domestic Revenues	190.7	201.2	**210.5**	221.4	233.2	242.3	256.1
Petroleum Revenues (excl investment return)	446.7	736.3	**595.0**	144.1	21.6	95.6	0.0

Source: National Directorate of Economic Policy and Petroleum Fund Administration Unit, Ministry of Finance, 2019.

2.4.1.1 Domestic Revenues

Domestic revenues in Timor-Leste are composed of tax revenues, fees and charges, interest, revenues from autonomous agencies and ZEESM taxes. Table 11 breaks down domestic revenues into these categories showing actual and forecasted amounts between 2018 and 2024.

Table 11: Domestic Revenue 2018 – 2024, $million

	2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Domestic Revenue	**190.7**	**201.2**	**210.5**	**221.4**	**233.2**	**242.3**	**256.1**
Taxes	127.7	127.1	**133.4**	140.1	147.1	154.5	162.2
of which ZEESM	3.0	3.3	**3.6**	3.8	4.1	4.5	4.8
Fees and Charges	54.7	62.2	**64.9**	68.6	72.6	77.6	83.1
Interest	0.5	0.7	**0.8**	0.8	0.8	0.9	0.9
Autonomous Agencies and Special Administrative Regions	7.7	11.2	**11.4**	11.9	12.7	9.3	10.0

Source: National Directorate of Economic Policy, Ministry of Finance, 2019.

2.4.1.2 Tax Revenues

Tax revenues comprise the largest source of domestic revenues in Timor-Leste, totalling 63% of total domestic revenues in 2020. Tax projections are summarized in Table 13 and are divided into Direct Taxes and Indirect Taxes.

2019 tax collection is expected to be almost flat with respect to 2018. This trend is mainly driven, on one side, by lower expected withholding tax. However, it should be noted however that 2018 was an exceptionally high year in for withholding tax, as several pending payments from the Government to private contractors where settled off. The delay in payments was partly due to duo-decimal budgetary constraints. Considering this, 2019 performance of withholding tax is less negative than it first appears. Other category of taxes are expected to be almost flat with respect to 2018. This excludes lower import duties, driven by lower imports of goods and services in the first half on 2019. On the other side, sales and excise tax are forecasts to perform better than 2019, reflecting greater household consumption.

Forecasts for 2020 see tax revenue grow by 5%. Such positive performance is led by a stable macroeconomic and political environment. Additionally, 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. The positive trend is expected to continue through 2024.

Table 12: Total Tax Revenue, Actuals and Projections 2018 – 2024, $million

	2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Tax	**127.7**	**127.1**	**133.4**	**140.1**	**147.1**	**154.5**	**162.2**
Direct Taxes	54.1	48.0	**50.4**	52.9	55.5	58.3	61.2
Income Tax	17.8	17.8	**18.6**	19.6	20.6	21.6	22.7
Individual Income (Public Sector)	5.3	5.6	5.9	6.2	6.5	6.8	7.2
Individual Income Other	12.5	12.2	12.8	13.4	14.1	14.8	15.5
Corporate Tax	9.4	9.2	**9.7**	10.2	10.7	11.2	11.8

Withholding Tax	26.9	21.0	**22.1**	23.2	24.3	25.5	26.8
Indirect Taxes	73.7	79.1	**83.0**	87.2	91.6	96.1	100.9
Service Tax	3.9	3.8	4.0	4.2	4.4	4.6	4.8
Sales Tax	14.7	17.1	17.9	18.8	19.7	20.7	21.8
Excise Tax	35.2	42.9	45.0	47.3	49.6	52.1	54.7
Import Duties	20.0	15.4	16.2	17.0	17.8	18.7	19.6

Source: National Directorate of Economic Policy, Ministry of Finance, 2019.

2.4.1.3 Fees and Charges

Fees and charges include a wide selection of categories from non-tax Source that contribute to domestic revenue. These comprise administrative fees, utility payments and royalty payments to the Government from natural resource other than petroleum.

2019 total fees and charges is expected to grow by 14% compared to 2018. The increase, however, is manly driven by dividends from BCTL, which are not expected to repeat in the near future. For this reason, 2020 projections will grow on average by 4% with respect to the previous year.

In 2019 and onwards, the principal component of fees and charges will continue to be from electricity payments (60% of the total). Additionally, mining and quarrying revenues are expected to become more sizeable in 2020, following infrastructural developments in south coastal and in land. These forecasts only account for existing agreements, new ones may push revenue expectations higher. Other significant contributions come from transport, property rentals, dividends and social games fees and charges, expected to continue on a stable path.

Growing decentralization of collection activity has also seen the introduction of non-fiscal instruments in the municipalities, as in the case of Dili, Baucau, Ainaro and Covalima, for advertising and parking services.

Projections for outer years are expected to continue on a positive trend, following the improvement and reinforcement of collection mechanisms in line ministries, further decentralized collection and introduction new non-tax instruments.

Table 13: Fees and Charges, Actuals and Projections 2018 – 2024, ($000's)

		2018 Actual	**2019 Proj.**	**2020 Proj.**	**2021 Proj.**	**2022 Proj.**	**2023 Proj.**	**2024 Proj.**
Collecting Ministry	**Total Fees and Charges**	**54,738.2**	**62,215.6**	**64,884.0**	**68,629.4**	**72,585.5**	**77,627.4**	**83,057.1**
Ministry of Finance	Other Non-Tax Revenues of Customs	481.8	817.8	**883.2**	953.9	1,030.2	1,112.6	1,201.6
Ministry of Finance	Customs Service Fees	-	5.4	**5.9**	6.4	6.9	7.4	8.0
Ministry of Finance	Customs Penalties	-	2.9	**3.1**	3.3	3.6	3.9	4.2
Ministry of Finance	Other Customs Duties	-	6.5	**7.0**	7.6	8.2	8.8	9.5
Ministry of Tourism, Commerce and Industry	Commercial License Fees	91.9	139.2	**144.7**	150.5	156.5	162.8	169.3

		2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Ministry of Transport and Communication	Postage Fees	38.9	38.2	**50.0**	60.0	65.0	70.0	75.0
Ministry of Justice	Property rentals	3,361.2	4,164.7	**4,500.0**	4,600.0	4,800.0	5,100.0	5,400.0
Ministry of Public Works	Water Fees	135.5	143.3	**180.0**	200.0	225.0	250.0	300.0
Ministry of Transport and Communication	Vehicle Registration Fees	1,215.2	1,477.2	**1,551.1**	1,628.6	1,710.1	1,795.6	1,885.3
Ministry of Transport and Communication	Vehicle Inspection fees	925.2	889.0	**933.4**	980.1	1,029.1	1,080.5	1,134.6
Ministry of Transport and Communication	Driver Licence Fees	379.7	764.0	**802.2**	842.3	884.5	928.7	975.1
Ministry of Transport and Communication	Franchising Public Transport Fees	264.5	296.9	**311.8**	327.4	343.7	360.9	379.0
Ministry of Transport and Communication	Transport Penalties/Trajectory	143.0	-	**-**	-	-	-	-
Ministry of Transport and Communication	Other Transport Fees	27.8	52.3	**54.9**	57.6	60.5	63.5	66.7
Ministry of Justice	Passport & ID	1,688.4	1,808.5	**1,500.0**	1,600.0	1,700.0	1,800.0	1,900.0
Ministry of Interior	Visa Fees	3,181.7	3,509.5	**3,649.9**	3,795.9	3,947.7	4,105.6	4,269.9
Courts	Tribunals - Fines & Penalties	39.2	481.8	**501.1**	521.1	542.0	563.7	586.2
Ministry of Transport and Communication	Vehicle Inspection Imported	83.1	94.1	**98.8**	103.7	108.9	114.4	120.1
Ministry of Public works	Electricity Fees & Charges	32,960.5	35,936.4	**38,811.3**	41,916.2	45,269.5	48,891.1	52,802.4
Ministry of Transport and Communication	TL Internet Domain Revenue	75.5	77.0	**80.8**	84.9	89.1	93.6	98.3
Ministry of Finance	Dividends, Profits & Gains	4,186.5	-	**2,746.0**	2,746.0	2,746.0	2,746.0	2,746.0
Secretary State for Vocational Training and Employment	Fines & Forfeits	107.9	281.7	**114.2**	114.2	114.2	114.2	114.2
Ministry Petroleum Resource and Minerals	Mining & Quarry Ops. Royalty	1,668.7	1,895.1	**2,000.0**	1,500.0	1,000.0	1,000.0	1,000.0
Ministry of Health	Fines-Health Professionals	13.0	9.3	**9.7**	10.1	10.5	10.9	11.3
Ministry of Finance	Bid Document Receipts - Ministries	35.8	423.7	**440.7**	458.3	476.6	495.7	515.5
Ministry of Finance	Auctions	45.4	480.0	**600.0**	650.0	500.0	500.0	500.0
Ministry of Finance	Sale of Local Produce	-	-	**-**	-	-	-	-

		2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Ministry of Tourism, Commerce and Industry	Social Games Receipts	1,886.0	3,405.0	**3,745.6**	4,120.1	4,532.1	4,985.3	5,483.9
Ministry of Justice	Rent of Government Property	51.4	80.0	**542.4**	542.4	542.4	542.4	542.4
Ministry of Agriculture and Fisheries	Forestry Products	82.0	85.2	**88.6**	92.1	95.8	99.6	103.6
Ministry of Public Works	Sanitation Services Fee	15.6	29.6	**30.7**	32.0	33.2	34.6	36.0
Ministry of Health	Registration of Health Professionals	23.6	26.8	**27.9**	29.0	30.2	31.4	32.6
Ministry of Higher Education	Polytechnic Institute of Betano	42.4	42.3	**44.0**	45.7	47.6	49.5	51.4
Ministry of the Presidency of the Council of Minister	Printing Fee - PCM	418.6	80.0	**88.0**	96.8	106.5	117.1	128.8
Ministry of Health	Pharmaceutical Fee	445.5	46.3	**48.2**	50.1	52.1	54.2	56.4
Ministry of Finance	BCTL Dividends	-	4,342.1	**-**	-	-	-	-
Ministry of Finance	Returned TPOs from Prior Years	-	8.3	**-**	-	-	-	-
Ministry of Finance	Other Non-Tax Revenue	387.8	1.3	**1.3**	1.3	1.3	1.3	1.3
Ministry of State Administration	Dili Municipality - Advertising Revenue	203.9	220.9	**231.9**	243.5	255.7	268.5	281.9
Ministry of State Administration	Ainaro Municipality - Advertising Revenue	-	3.6	**3.7**	3.9	4.0	4.2	4.4
Ministry of State Administration	Covalima Municipality - Advertising Revenue	0.5	9.3	**9.6**	10.0	10.4	10.8	11.3
Ministry of State Administration	Baucau Municipality - Advertising Revenue	-	6.2	**6.4**	6.7	7.0	7.2	7.5
Ministry of State Administration	Dili Municipality - Parking Fee	25.6	29.2	**30.7**	32.2	33.8	35.5	37.3
Ministry of Health	Administrative Sanctions and Fines	5.0	5.0	**5.2**	5.4	5.6	5.8	6.1

Source: National Directorate of Economic Policy, Ministry of Finance, 2019.

2.4.1.4 Interest

Interest reflects interest payments received from cash held in Government funds. Recent growth in interest rates and cash balances held by the government, interest receipts represent a larger portion of total revenue, expected to reach $0.727m in 2019, compared to $0.756m in 2020.

Table 14: Interest Receipts, Actuals and Projections 2018 – 2024, $

	2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Interest Receipts	530,494.9	727,046.0	**756,127.8**	786,373.0	817,827.9	850,541.0	884,562.6

Source: National Directorate of Economic Policy, Ministry of Finance, 2019.

2.4.1.5 Autonomous Agencies

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 2018 and 2019, new Autonomous Agencies have started collecting revenue, including IADE, AIFAESA, SENAI and SERVE. The Port of Dili generates the majority of revenues, it collection for outer years is however uncertain and might decline once the Tibar Port becomes operational. Other significant contributions are expected to derive from the National Communication Authority (ANC), whose receipts will grow thanks to a larger base for collection and new revenue following the activation of the spectrum fee; the National University; ZEESM fees and charges and the National Logistic Centre.

Table 15: Autonomous Agencies and Special Administrative Region, Actuals and Projections 2018-2024, ($000's)

	2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Autonomous Agencies Revenues	**7,735.6**	**11,198.0**	**11,382.0**	**11,858.0**	**12,699.3**	**9,330.5**	**9,987.2**
TRADEINVEST - Investment Registration Fee	20.0	-	**0.0**	-	-	-	-
CLN - Sale of Local Product	79.0	300.0	**312.0**	324.5	337.5	351.0	365.0
ANC - Licensing Fee	-	1,240.5	**1,290.1**	1,341.8	1,395.4	1,451.2	1,509.3
APORTIL - Port Charges & Fees	4,091.9	4,213.0	**4,547.6**	4,774.9	5,013.7	1,000.0	1,000.0
ANATL - Aviation Service Fees	-	-	**0.0**	-	-	-	-
IGE - Receipts	287.2	481.3	**500.6**	520.6	541.4	563.1	585.6
SAMES - Receipts	218.6	312.0	**320.0**	350.0	370.0	400.0	420.0
UNTL - National University Fees	1,160.3	1,762.0	**1,895.4**	2,260.7	2,626.0	2,991.3	3,356.7
HNGV - Hospital & Medical fees	264.8	375.2	**390.2**	405.8	422.1	438.9	456.5
Tribunals - Administrative Fees	-	28.3	**29.4**	30.6	31.8	33.1	34.4
Bamboo Center Tibar – Revenue	11.6	705.9	**220.0**	242.0	266.2	292.8	322.1
AMRT - Fees	2.3	3.0	**3.1**	3.2	3.4	3.5	3.6

	2018 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
IADE Service Fees	53.8	29.5	**18.2**	23.2	19.7	19.7	25.7
AIFAESA Fees	150.1	188.9	**196.5**	204.3	212.5	221.0	229.8
SENAI Centre – Revenue	6.4	8.0	**9.0**	10.0	11.0	12.0	13.0
SERVE IP - Revenue	214.9	350.0	**367.5**	385.9	405.2	425.4	446.7
CLN - Sale of Rice	413.0	350.0	**364.0**	378.6	393.7	409.5	425.8
ZEESM - Fees and Charges	761.7	850.4	**918.4**	991.9	1,071.2	1,156.9	1,249.5

*Source: National Directorate of Economic Policy, Ministry of Finance. *ZEESM revenue includes fees and charges only, tax revenue is presented separately in table 11.*

2.4.2 Petroleum Revenues and the Petroleum Fund

The Petroleum Fund remains the principal source of financing for the state budget each year. Withdrawals from the Fund are guided by the ESI. The ESI represents the maximum amount that can be appropriated 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 percent of the Petroleum Wealth, which comprises the balance of the Fund and the Net Present Value of future petroleum revenue.

The Government can withdraw an amount from the Petroleum Fund in excess of the ESI where it provides to Parliament justification why that is in the long-term interests of Timor-Leste. Government withdrawals in excess of the ESI have been justified on the grounds of economic development. Withdrawing more than the ESI, by definition, depletes the purchasing power of the Fund.

2.4.2.1 Calculating Petroleum Wealth and the ESI for 2020

Table 16 shows the estimated Petroleum Wealth and the ESI from 2018 and onwards, assuming that withdrawals from the Fund are equal to the projected withdrawals in this budget book.

Table 16: Petroleum Wealth and the Estimated Sustainable Income (ESI)

	2018*	2019*	2020 Budget	2021	2022	2023	2024
Estimated Sustainable Income (PWx3%)	**550.4**	**529.0**	**536.8**	**526.7**	**493.6**	**458.9**	**429.3**
Total Petroleum Wealth (PW)	**18,345.8**	**17,633.6**	**17,891.8**	**17,556.3**	**16,453.9**	**15,296.3**	**14,310.3**
Opening PF Balance			17,067.9	17,307.3	16,342.3	15,202.5	14,310.3
Net Present Value of Future Revenues			823.9	249.0	111.6	93.8	0.0

*Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019. *ESI for 2018 & 2019 figures as estimated in Budget 2018 and Budget 2019.*

The Petroleum Wealth for Budget 2020 is estimated to be $17,891.8 million. Accordingly, the 3% ESI is estimated at $536.8 million for 2020. This is about $7.8 million higher than the estimate for the ESI 2020 in Budget 2019. The key assumptions behind the calculations and the differences with Budget 2019's estimate are discussed below.

Table 17: Key Assumptions behind the ESI Calculation

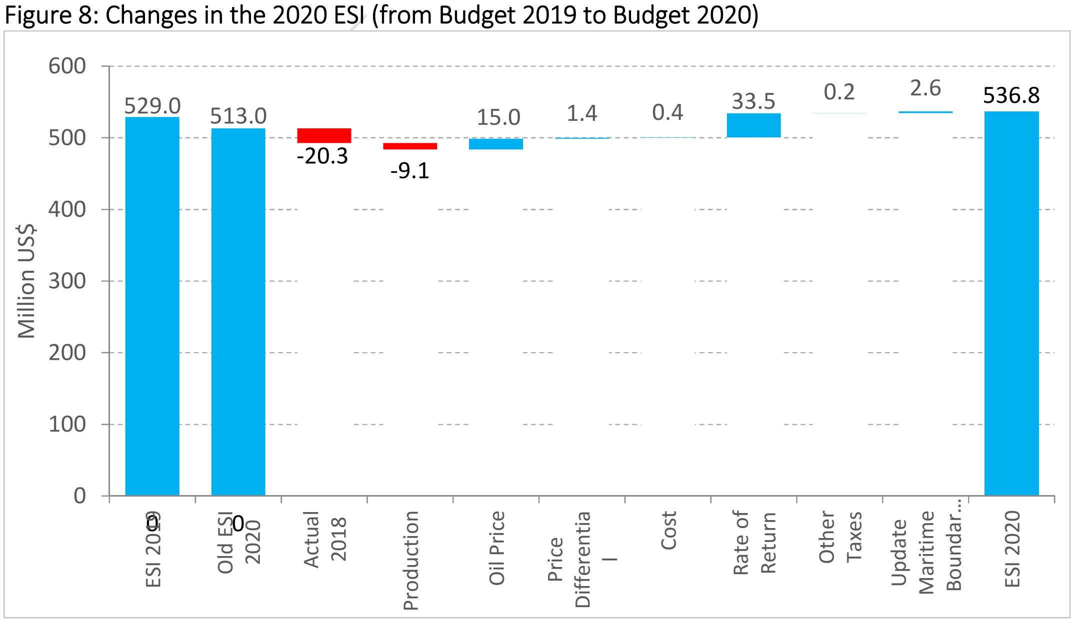
Asset recognition	Forecast petroleum revenues are included only for projects with approved development plans. Bayu-Undan (BU) is the only operating field.
Petroleum Reserves and Production Forecasts	Project operators provide production estimates. The Operator provided 3 forecasts scenarios; low, base, and high. Average Low-Base case production is used for ESI 2020.
Oil price forecast	Brent crude oil has been shown to be the best indicator of the price of BU liquid products (condensate and LPG). ESI for Budget 2020 is prepared using the average of Energy Information Agency (EIA) low case and reference case for Brent in its Annual Energy Outlook (AEO) for 2019, released in January 2019.
Prices for specific petroleum products	BU produces condensate, Liquefied Petroleum Gas (LPG) and Liquefied Natural Gas (LNG). Forecast assumptions for each product are derived from historical differentials observed with Brent. 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	Central estimate of future capital and operating costs as provided by project operators.
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 percent cash, 55 percent bonds, 35 percent equities and 5% in alternative.

Source: Petroleum Fund Administration Unit, Ministry of Fnance, 2019.

Changes in the ESI from 2019 to 2020

Figure 8 shows the key incremental changes in the current estimate of the 2020 ESI relative to the estimate in Budget 2019. A higher expected investment return in 2019 is the main driver of the increase in the 2020 ESI, along with changes to the oil price forecast and the expected revenues as the result of the settlement of the maritime boundaries.

Figure 8: Changes in the 2020 ESI (from Budget 2019 to Budget 2020)



Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

Actual 2018 data

The 2020 ESI that estimated in October 2018 was based on forecasted data for the remainder of 2018. Actual history is now available for all of 2018 and that actual history is used in the current forecast of 2020 ESI. The actual net petroleum revenues collected in 2018 was $446.7 million, after deducting a total amount of $63.3 million of a tax overpayment in FY 2011-2013 by Kitan field contractors. Actual revenues were 15 per cent higher than the estimated $389.4 million. The actual withdrawal in 2018 was $982.5 million, which is the same as assumed. The higher petroleum revenue was offset by the negative investment returns realised in 2018 of minus 2.6 per cent or equivalent to -$459.9m which is much lower than the estimated return of 1.7% or equivalent to $283.4 million. As a result, the actual closing balance of the Fund at the end of 2018 was $15,803.6 million compared to the estimated $16,489.6 million. As the result of this change, the ESI 2020 decreased by $20.3 million.

Production

The latest Bayu-Undan's production forecast for both liquids and gas are lower than Budget 2019 as shown in Figure 9. Following the previous year, the average of the low and the base forecasts was adopted for petroleum production.

Figure 9A and 9B show the latest available Operator's revised petroleum production forecasts in three scenarios; low, base and high. Figure 9C and 9D compare the liquid (condensate and LPG) and gas (LNG) production forecast used in the current Budget 2020 estimate with the forecast used for the Budget 2017 until 2019. For period 2019-2022, the liquids (condensate and LPG) and the LNG production forecasts are approximately around 16% lower compared to the forecast used in Budget 2019. The BU 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. Despite this, the Bayu-Undan Infil Well (BUIW) project in mid-2018 has helped to maintain the production level. This results in a US$9.1 million decrease in ESI for 2020.

Figure 9: Bayu-Undan Production Forecast in the 2020 ESI

Figure A. BU Liquids Forecasts for B2020

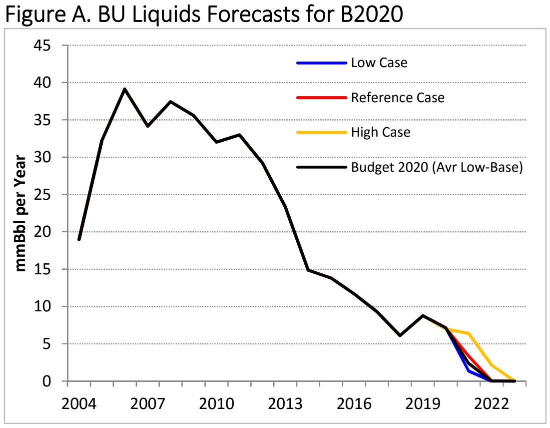


Figure B. BU Gas Forecasts for B2020

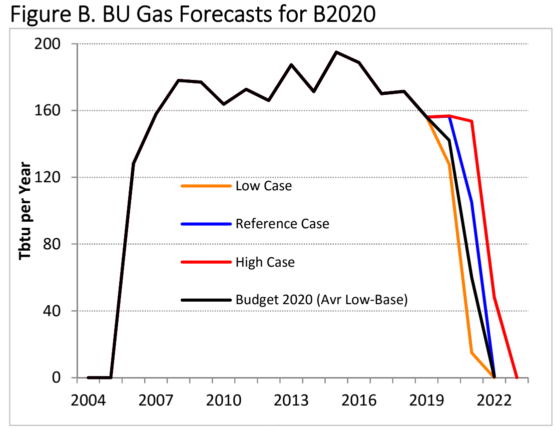


Figure C. BU Liquids, B2017-19 vs. B 2020

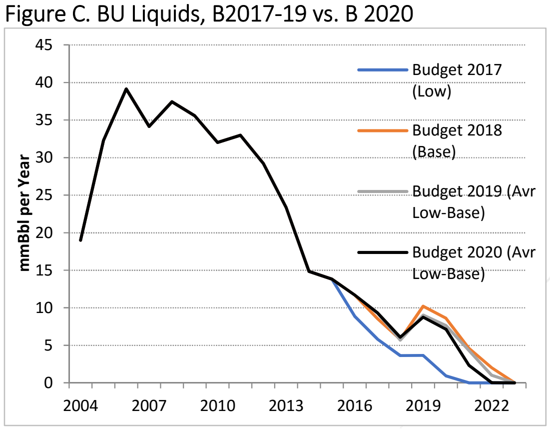
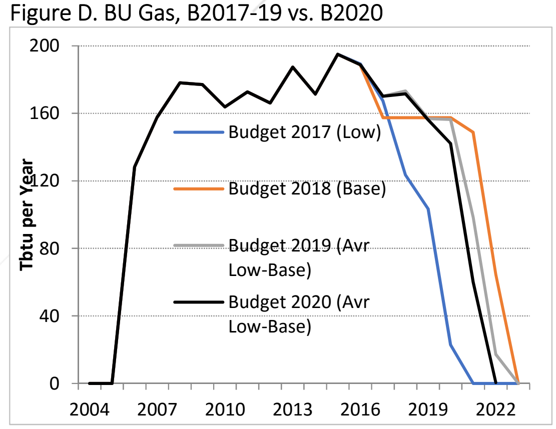


Figure D. BU Gas, B2017-19 vs. B2020



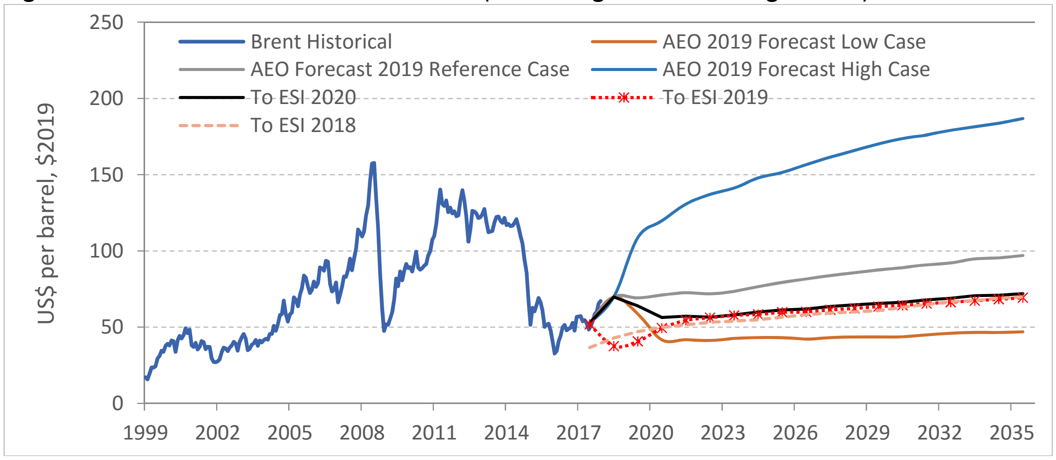
Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

Oil prices

The methodology for projecting future oil prices is based on the average low –base price case of the Brent oil prices forecast by the US Government's Energy Information Administration (EIA). Figure 10 shows that the oil benchmark forecast used for ESI 2020 is now slightly higher for the period 2020-2021 compared to the forecast used for ESI 2019. The actual average Brent benchmark price from January to August 2019 was $64.8 per barrel. Applying the weighted average of the actual price and the average EIA low-base prices for the remainder of the year, the 2019 price is $66.2/barrel, compared to $44.8/barrel used in Budget 2019.[6] The 2020 price is revised up from $54.2 to $61.6 per barrel. The prices for the remainder of the forecasting period until production ceases in 2022 is averaging about 6% higher than the prices used in ESI 2019. The change in Brent benchmark forecast results in a US$ 15.1 million increase in the ESI 2020.

[6] The EIA's Short-term Energy Outlook released in August shows its reference (base) scenario where the expected average Brent price for 2019 is $63.4/b and $62/b in 2020. Bloomberg's future prices for Brent for 2019 averages $65/barrel and $62/barrel in 2020.

Figure 10: Oil Price Forecast in the 2020 ESI (from Budget 2019 to Budget 2020)



Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

Production price differentials (liquids and LNG)

There are several petroleum products (condensate, Liquefied Petroleum Gas (LPG) and Liquefied Natural Gas (LNG)) which come from the Bayu-Undan project. As in previous years, the prices for liquids products (condensate and LPG) are forecast by applying a differential to the forecasted Brent benchmark price based on the historical relationship between the benchmark and the Bayu-Undan products price. The relationship between liquids product prices and the Brent benchmark price has been relatively stable, with condensate averaging about 95 percent and the LPG averaging about 71 percent of the benchmark between 2008 and 2017.

Over time, the price differentials (either above or below Brent) used in the ESI 2020 results in a relatively higher forecast of Timor prices than the price differentials used in ESI 2019. The result of these new price differentials is an increase in ESI of US$ 1.4 million.

Production costs

Forecasts of production costs from the operator (COP) for period 2019-2022 are around 13% lower than last year forecasts. The result of these new costs projection is an increase in ESI of US$0.4 million.

Rates of return and discount rate

Under Annex 1 of the Petroleum Law Fund, the discount rate used in the NPV calculation of future petroleum revenues must be the expected rate of return of the Petroleum Fund portfolio. The expected long-term nominal return on the portfolio is now 3.8 percent for period 2020 onwards. This is slightly lower than previous year's ESI assumption of expected return at 3.9 percent and will slightly increase the NPV of future petroleum revenues.

The expected return for the year 2019 changed from the long-term nominal return expectation of 3.9% nominal to 11.1% nominal to reflect the strong returns for the year to date. The Fund's benchmark performance in 2019 as at 24 September showed a positive return of 9.76%. The end year return will depend on the market movements in Q4. The higher return for 2019causes a higher estimate of the Fund's opening balance in January 2020, which resulted in the ESI 2020 increasing by US$ 33.5 million.

Other Taxes

Other taxes include wage taxes and tax collections from subcontractors and exploration drilling i.e. for research and drilling, has been awarded both in the former Joint Petroleum Development Area - JPDA (e.g. JPDA 11-106) and in on/offshore of Timor-Leste Exclusive Area-TLEA (e.g. PSC TL-S0-15-01, PSC TL-OT-17-08 and PSC TL-OT-17-09). These taxes are forecast for Budget 2020 based on an analysis of recent collections and taking into account exploration work commitments. This has increased ESI 2020 by $0.2 million.

Update on the Maritime Boundary between Timor-Leste and Australia

The new treaty establishing permanent maritime boundaries in the Timor Sea between Timor-Leste and Australia which was signed on 6 March 2018 and then ratified by both Parliaments of each country in August 2019. The Maritime Boundaries Treaties (MBT) entered into effect on 30 August 2019 when both governments agreed and exchanged the diplomatic notes in Dili. Under the MBT all related petroleum titles and activities in the area formerly known as the Joint Petroleum Development Area (JPDA), which now mostly fall within TL's sovereign waters. Under the key principle of *Conditions Equivalent* term, a Transitional Arrangement process took place between the States (TL and Australia) including the contractors whose business were affected, with the objective to transpose all existing contracts under the former JPDA Fiscal Regime and those partially under the Australian Petroleum Fiscal Regime to 100% Timor-Leste Fiscal Regime.

Australia's former petroleum entitlement of a 10% revenue share under TST framework will be paid to Timor-Leste as of September 2019 onwards. During the Transitional Arrangement, all contractors' direct taxes (eg corporate income taxes, withholding taxes, wage taxes, and so forth) will be 100% subjected to Timor-Leste's Taxation Act with the relevant adjustments made to the specific areas of operations and specific phases of activities, including as referred to in each Production Sharing Contracts (PSCs) and fields.[1] The ESI model is adjusted for these changes accordingly.

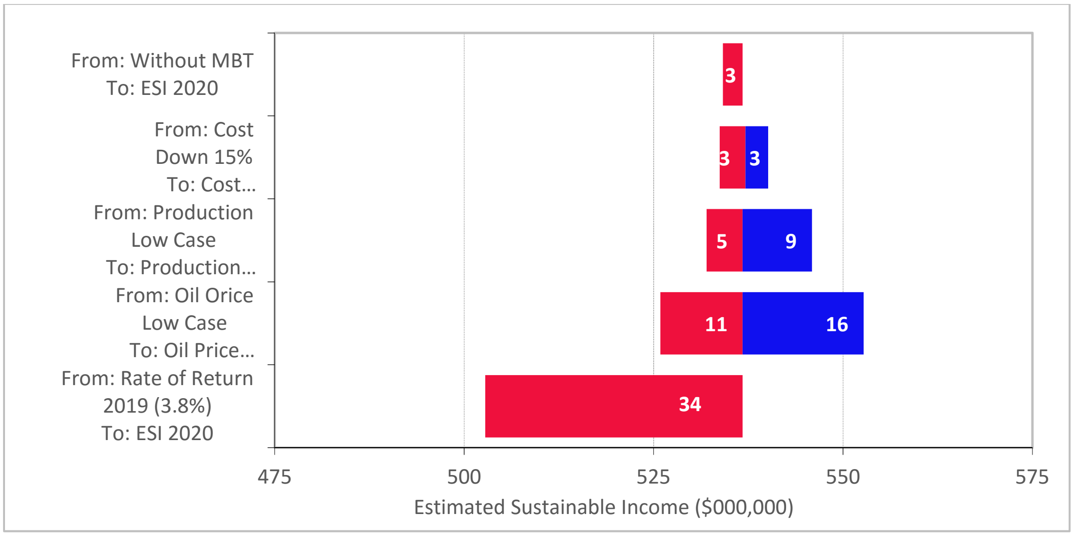
This resulted in the ESI 2020 increasing by $2.6 million.

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 inherently subject to significant uncertainty. Figure 6 shows how 2020 ESI would change if some key assumptions were changed individually. Increases in ESI are shown in blue, and decreases are shown in red. The sensitivity analysis starts with the 2020 ESI of US$536.8 million and shows by how much ESI would change if a different assumption for each key variable was used. Each sensitivity calculation is briefly described below.

Figure 11: Sensitivity Analysis – Estimated Sustainable Income, $million

[1] Eg for Bayu-Undan field the applicable Taxation law is Bayu-Undan Contractors Act (ToBUCA) which regulates the taxation matter of the petroleum activities carried out by contractors and subcontractors in connection with the Bayu-Undan project falling within the former JPDA PSCs 03-12 and 03-13. During the Transitional Arrangement processes a few amendments were made to the ToBUCA and Tax Stabilization Act and Taxes and Duties Act, for example all direct taxes will be 100% subject to TL's taxation act, however, the Additional Profit Tax (APT) rate is reduced from 22.5% to 21.5% to provide ***conditions equivalent*** taking into consideration that the 10% share from Australia was not subject to APT and all indirect taxes related to services provided by sub-contractors to BU field will be maintained at 90% TST framework as agreed under fiscal package for BU project. For other areas of operations such as Kitan and Kanase, the application of 90% indirect taxes would be changed or lapsed after Decommissioning and the commencement of first production, respectively. This means that after the decommissioning phase and possibly entering into a redevelopment phase, Kitan's indirect taxes will be levied at 100% and the same rate will also be applied to Kanase once the first production starts.



Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

1. *The calculated ESI 2020 is sensitive to the Rate of Return used in 2019 to estimate the Fund's starting balance in 2020.* If the long-term expected investment return of 3.8% is used in 2019 instead of the assumed 2019 return of 11.1%, the ESI would decrease by $34 million.

   The ESI also depends on the discount rate used to calculate the NPV of future petroleum revenues, which represents the long-term expected return on the Petroleum Fund. For example, if a discount rate in 2020 of 5.0% is used instead of 3.8%, the calculated ESI 2020 would drop by $0.3 million.

2. *The calculated ESI 2020 is somewhat sensitive to the production forecast.* As noted above, the ESI is now using the average Low-Base production forecast. If the Low case (P90) forecast is used the ESI would decrease by $5 million, while if the Base case (P50) was used the ESI would increase by $9 million.

3. *The calculated ESI 2020 is sensitive to the forecast of oil prices.* As noted above, the forecast of future Brent prices, which is used to forecast prices for Timor petroleum prices, is based on the average of the AEO Low and Reference (Base) Cases. If instead EIA's Low or Reference forecast of Brent prices is applied, ESI would be approximately US$ 11 million lower or $16 million higher.

4. *The calculated ESI 2020 is less sensitive to the costs' forecast***.** If the costs change by 15% up or down, the ESI would change by $3 million up or down.

5. *The calculated ESI 2020 is not overly sensitive to changes in the forecast of other key components of ESI***.** For example the impact of the recent MBT is small. This is understandable given it only considers BU field which assumed to cease in 2022. The 10% Australian entitlement is approximately less than $90 million.

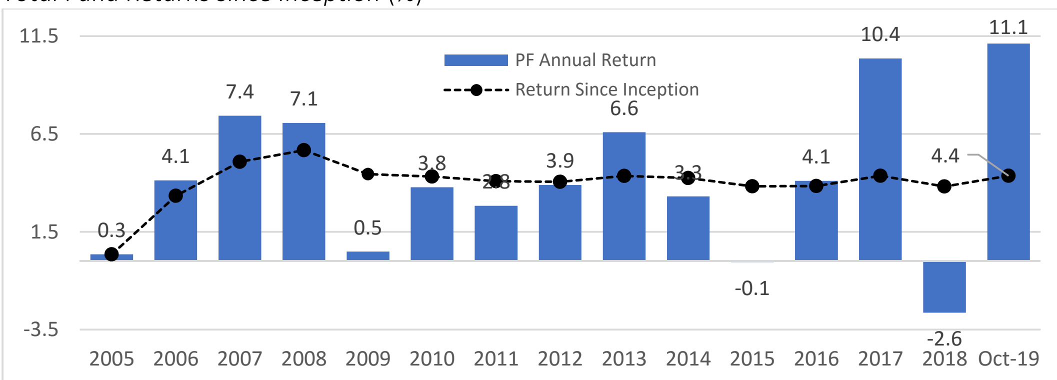
2.4.2.2 Petroleum Fund Management and Projections

The Petroleum Fund is currently invested 5% in cash, 55% in Government bonds, 35% in equities and 5% in petroleum related operations through a private debt placement in Timor GAP E.P.

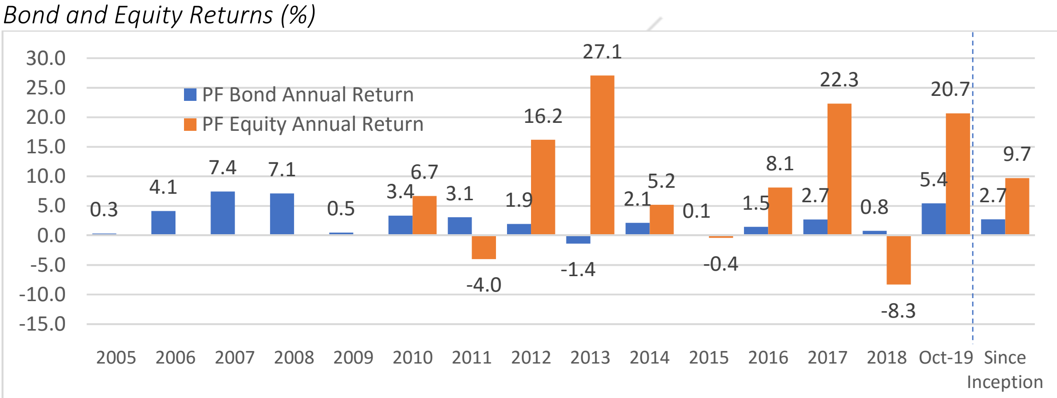
The investment in equities was progressively implemented and completed in June 2014. The Fund's return since inception to October 2019 is 4.4 per cent per annum, which is 2.3 per cent in real terms after accounting for US inflation. Equities have fulfilled their growth role. Figure 12 shows the equity portfolio has boosted the Fund's performance by returning 9.7 per cent per annum since the first investment in stocks in 2010. This compares to the bond portfolio's average annual return of 2.7 per cent over the corresponding period[7].

Figure 12: Petroleum Fund Investment Returns

Total Fund Returns since Inception (%)



Bond and Equity Returns (%)



Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

The ESI framework is designed to preserve real wealth but is challenged when withdrawals are persistently in excess of the ESI. In addition, investment returns over the next decade are likely to be lower than previously projected. That expectation is primarily driven by lower bond yields, which act as a drag on the return forecasts for bonds. This is captured in our central estimate of a real return of 1.8 per cent over the next 10 years. It is unlikely that that the Fund's current asset allocation will provide a real return of 3 per cent.

The Investment Advisory Board (IAB) advised the Minister of Finance in May 2018 to continue with the Fund's existing asset allocation. The expected return from bonds is very low by historical standards and equities are required for the Fund to earn a suitable return over the long-term. However, targeting a 3 per cent real return would require a significantly higher equity allocation and the additional risk did not appear suitable for Timor-Leste, at least for the time

[7] Please see the Petroleum Fund Annual Report for 2018 for more detailed discussion on the performance of the Fund.

being. The Board reviews the Fund's asset allocation each year to account for any new information, including expectations about withdrawals and future oil revenues.

Updated projections for the Petroleum Fund

Table 18 shows an update of petroleum revenues. The revenues in 2018 amounted to $446.7 million. As of October 2019, petroleum revenue is $667.2 million, which already exceeds the projection of $343.7 million in the Budget 2019. Oil prices were higher than estimated, averaging about $64.8 per barrel from January to October. Accounting for this and actual revenues received, the expected total revenue for 2019 is revised up to $736.3 million.

Under the current assumptions, the revenue is projected to continue to decline from $595.0 million in 2020 to $95.6 million in 2023.

Table 18: Petroleum Fund Revenues 2018-2024, $million

	2018 Actual	2019 Proj.	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Petroleum Fund Revenue	**-13.2**	**2,460.6**	**1,236.0**	**771.6**	**609.8**	**645.9**	**516.9**
Petroleum Fund Investment Return	-459.9	1,724.3	**641.0**	627.4	588.2	550.3	516.9
Total Petroleum Revenue	**446.7**	**736.3**	**595.0**	**144.1**	**21.6**	**95.6**	**0.0**
FTP/Royalties	190.6	350.4	**311.9**	73.3	0.8	0.0	0.0
Profit oil	53.4	84.1	**47.2**	17.5	1.3	0.0	0.0
Income Tax	113.2	119.3	**84.0**	0.0	0.0	0.0	0.0
Additional Profit Tax	117.4	145.8	**121.7**	24.3	0.0	0.0	0.0
Value Added Tax	9.6	5.7	**9.9**	9.6	3.7	95.6	0.0
Other Tax Payments	-37.4	31.0	**20.4**	19.5	15.8	0.0	0.0

Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

The new Maritime Boundaries Treaty and with the acquisition of a 56.56% of participating interest in the Greater Sunrise JV through the Timor GAP E.P will allow Timor-Leste to influence the decision on the upstream and downstream development of the GS. This potential revenue will be included in the estimate of the present value of the petroleum revenues when the fields are declared proven and approved for development.

The Fund's balance is $17,815.2 million as of October 2019. This is an increase of $2,011.6 million from the start of the year. Investment income after expenses for the year to date is $1,764.3 million. Equities have posted gains of 20.7% as at October, while bonds recorded returns of 5.4%. Taking into account the realized returns and considering the market movement in the last two months, the expected investment income for 2019 is assumed to be 11.1%. This translates to an expected income of $1,724.3 million.

There has only been $420 million of withdrawals for the year until October. The Fund balance is expected to be $17,067.9 million by the end of 2019 after deducting the estimated withdrawal of $1,196.4 million in 2019 adopted by Parliament.

The Fund is forecast to decline each year, falling to $13,409.9 million by the end of 2024. Petroleum revenues and investment income are not expected to offset withdrawals. These are central forecasts and considerable variation must be expected. Investment income is by its nature volatile. In some years, like 2017, the Fund will outperform expectations; in other years like 2018, the Fund will incur losses. 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.

Table 19: Estimated Petroleum Fund Savings, $million

	2018 Actual	2019 Proj.	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Opening PF Balance	**16,799.3**	**15,803.6**	**17,067.9**	**17,307.4**	**16,330.4**	**15,202.5**	**14,310.4**
Petroleum Revenue (Exclud PF Interest)	446.7	736.3	**595.0**	144.1	21.6	95.6	0.0
Petroleum Fund Interest, Net	-459.9	1,724.3	**641.0**	627.4	588.2	550.3	516.9
Total Withdrawals	982.5	1,196.4	**996.5**	1,736.6	1,749.6	1,538.0	1,417.4
Closing FP Balance	**15,803.6**	**17,067.9**	**17,307.4**	**16,342.3**	**15,202.5**	**14,310.4**	**13,409.9**

Source: Petroleum Fund Administration Unit, Ministry of Finance, 2019.

2.5 Expenditure and Development Partner Commitments

Total expenditure in the 2020 budget is $1,841.5m (including donor funded activities of $173.5 million and loans of $73.0 million). The total 2020 State Budget 13.9% higher than that allocated for 2019. This is mainly because the Government plans to commence large social capital and economic development programmes in 2020.

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 Europe Union Budget Direct Support. Since 2016, the Infrastructure Fund is an autonomous agency under the CFTL. Compared to the allocations for the 2019 State Budget, allocations for 2020 have increased: CFTL by 14.5%. However, HCDF has decreased by 53.8% and loan disbursements have decreased by 14.8%.

Table 20: Expenditure by Fund, $million

	2018 Actual	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Combined Source Budget	**1,343.9**	**1,681.3**	**1,841.5**	**2,276.6**	**2,127.2**	**1,892.2**	**1,770.7**
Government Expenditures by Fund	**1,172.7**	**1,482.0**	**1,668.0**	**2,193.7**	**2,091.9**	**1,878.5**	**1,757.0**
CFTL (excl. loans)	**1,119.0**	**1,375.0**	**1,574.5**	**2,100.0**	**2,023.9**	**1,818.0**	**1,708.0**
HCDF	14.5	20.0	**13.0**	13.5	14.1	14.6	15.2
Borrowing/Loans (disbursements)	39.2	87.0	**73.0**	80.2	53.9	45.9	33.8
Europe Union (Direct Budget Support)	-	-	**7.5**	8.6	5.0	2.8	-
Development Partner Commitments	**171.2**	**199.2**	**173.5**	**82.9**	**35.3**	**13.7**	**13.7**

Source: National Directorate of Budget and Development Partners Management Unit, Ministry of Finance, 2019.

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 21.

Total allocations in the CFTL will increase by 14.5% in 2020 compared to the 2019 State Budget.

The Goods and Services allocations for many ministries and agencies have also increased, with the allocation for the category as a whole 24% higher than in the 2019 State Budget.

The allocation for Capital and Development has increased by 32.5% in 2020 compared to the 2019 State Budget. The Government will ensure that the exisiting key infrastructure projects are continued be developed at a good rate, in line with its program and priorities, while monitoring and revising costs.

Table 21: Breakdown of CFTL expenditure, $million

	2018 Actual	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total CFTL Expenditure	**1,119.0**	**1,375.0**	**1,574.5**	**2,100.0**	**2,023.9**	**1,818.0**	**1,708.0**
Recurrent	**814.3**	**1,029.8**	**1,127.1**	**1,172.2**	**1,219.1**	**1,267.9**	**1,318.6**
Salary and Wages	197.2	214.2	**235.6**	245.0	254.8	265.0	275.6
Goods and Services	304.6	452.9	**561.8**	**584.3**	**607.6**	**632.0**	**657.2**
Public Transfers	312.5	362.7	**329.7**	342.9	356.6	370.9	385.7
Capital	**304.7**	**345.3**	**447.4**	**927.8**	**804.8**	**550.2**	**389.4**
Minor Capital	7.8	31.5	**31.5**	32.8	34.1	35.5	36.9
Capital and Development	296.9	313.7	**415.8**	894.9	770.7	514.7	352.5
Infrastructure Fund (excl. loans)	291.3	279.4	**238.3**	710.3	578.6	314.9	144.8

Source: National Directorate of Budget, Ministry of Finance, 2019.

Salaries and Wages

The allocation for Salaries and Wages ($235.6 million) increases 10% in the 2020 State Budget compared to the allocation for 2019. This is due to resulting cost increases from changes in pay structures, special regimes for civil servants and new recruitment.

Key Measures

- $13.8 million for the changes in the remuneration structure as a result of the approved organic laws.
- $3.0 million to all municipalities to fill positions in their local government structure.
- $936,000 to F-FDTL for the recruitment of 600 new members .
- $730,000 to the Public Service Commission for the internal promotion for civil servants.
- $700,000 to the Ministry of Finance for payments to its employees under the Special Regime.
- Other increases in salaries are due to the promulgation of the new organic laws which have caused internal restructuring as well as created new positions that will be filled up with the 2020 State Budget.

Goods and Services

The CFTL Goods and Services budget for 2020 ($561.8 million) is set to increase by 24% compared to the allocation in the 2019 State Budget. The increase in 2020 is due to the biggest being electricity operation, maintenance, debt of the fuel.

Key Measures

- $166.4 million to the Ministry of Public Works towards fuel and maintenance of electricity generators in Hera and Betano. This includes to pay for the debt of fuel supply $60.6 million, 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.
- $31.1 million to the Whole of Government for the Counterpart Fund. This will contribute to the continued implementation of key counterpart funding projects. This includes partial allocation for the purchase of Nakroma II ferry.
- $8.0 million to the Whole of Government for legal services. This fund enables the state to defend itself in various legal cases.
- $6.9 million to Public School for the School for the School Feeding Program.
- $4.98 million to SAMES for acquisition of medications and pharmaceutical goods to help improve the quality of health services provided throughout the country.
- $3.0 million to the Whole of Government for new provisions for civil aviation.
- $2.8 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.
- $2.5 million to the Whole of Government for the population and housing census. This will be beneficial for the targeting of social sector and economic development programmes in the future.
- $2.1 million to the Prime Minister Office for Timor-Leste’s participation in the Dubai Expo.
- $1.0 million to the Whole of Government for participations in events of the Community of Portuguese Speaking Countries (CPLP) and the CPLP Games.

Public Transfers

Public Transfers comprise all of the money the Government spends on public grants and consigned payments. The allocation for this category will decrease in 2020 to $329.7 million, an decrease of 9.1% compared to the 2019 State Budget.

Key Measures

- $91.4 million to Ministry for National Liberation Combatants Affairs for veteran pensions and housing.
- $63.8 million given to the Ministry of Petroleum and Mineral to invest in the development of Timor Gap.
- $41.3 to the National Institute for Social Security (INSS) for the Contributory and Non-Contributory Regime.
- $22.6 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.

- $15.2 million to the Whole of Government for the provision of pensions for permanent civil servants under the contributory regime.
- $11.3 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. million to the Whole of Government to cover loan repayments.
- $8.0 million to the Whole of Government to support church activities through the Episcopal Church Conference.
- $6.0 million to the Ministry of State Administration for the National Program for Village Development (PNDS)
- $6.0 million to National Commission for elections. This expenditure provides subsidy to political parties to continue the follow-up and strengthen the democratic process in Timor Leste.
- $5.5 million to Whole of Government for pension payments for former leaders and former members of sovereign bodies.
- $4.3 million to the Ministry of Education, Youth and Sport and the Secretariat for Youth and Sport, to provide support for various sporting events and youth activities throughout the year.
- $4.0 million to the Whole of Government for recapitalising and payment of fees for the service of Central Bank of Timor Leste (BCTL).
- $4.0 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.
- $1.9 million to Private Schools for the School Feeding Program.
- $1.7 million to the Secretary of State for Social Communication to provide subsidy for Radio Television Timor-Leste (RTTL) no Tatoli.
- $1.5 million to the Whole of Government for the g7+ secretariat. The work of this secretariat ensures that the voice of fragile states (including Timor-Leste) is heard and acted upon by the international community.
- $1.0 million to the Whole of Government for recapitalising and payment of fees for the service of National Commercial Bank of Timor Leste (BNCTL).
- $1.0 million to Secretary State for Cooperatives for subsidy to cooperative groups.
- $800,000 to the Ministry of Education, Youth and Sport for concessions for private schools and CAFÉ schools.
- $800,000 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.
- $500,000 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.
- $250,000 to the Secratariat of State of Equality and Inlcusion for providing rotating capital to rural women, with the aim to promote women entrepreneurship.
- $200,000 to the Secretariat of State of Art and Culture for the preservation of the cultural identity.

Minor Capital

Minor Capital includes expenditures on vehicles, furniture and other movable assets. The 2020 budget ($31.5 million) for this category reflects a 0% decrease as compared to the 2019 State Budget ($31.5 million).

Key Measures

- $4.0 million to the Ministry of Finance for the acquisition of IT equipment for an additional backup data centre and X-rays machines etc.
- $3.4 million to the Ministry of Public Works for the purchase of a current transformer, prepaid meters and other equipment.
- $3.2 million to the Ministry of Education, Youth and Sport for the purchase of desks and chairs for schools.
- $1.8 million to the Ministry of Defense of the purchase of communication, security and other equipment.
- $1.7 million to Ministry of Health to buy ambulances and multifunctional vehicles, operational vehicles for monitoring and evaluation.
- $1.3 million to the Ministry of State Administration for the purchase of election information system and equipment for the PNDS.
- $800,000 to the National Police of Timor-Leste for the purchase of security and other equipment.

Capital and Development

The 2020 allocation for Capital and Development (CD) increases 32.5% compared to the allocation for 2019. This is driven by an increase to ministries for capital projects such as in health, education and agriculture. The district development programmes have also received an infusion of capital development budget in 2020 which has been directly allocated to the municipalities. This is the first time municipalities get their own CD budget allocation. As shown in Table 22, Capital and Development allocations under the CFTL are broken down into $238.3 million for the Infrastructure Fund, $6.0 million for the District Development Programs, and $171.6 million for other Capital and Development projects across line ministries.

Table 22: Capital and Development Expenditures, $milion

	2018 Actual	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Capital and Development	**296.9**	**313.7**	**415.8**	**894.9**	**770.7**	**514.7**	**352.5**
Infrastructure Fund (excl. loans)	291.3	279.4	238.3	710.3	578.6	314.9	144.8
District Development Programs	4.2	7.8	6.0	6.2	6.5	6.7	7.0
Ministries / Agencies	1.4	26.5	171.6	178.4	185.6	193.0	200.7

Source: National Directorate of Budget, Ministry of Finance, 2019. 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, a total of $4.63 billion has been approved and allocated to the IF to finance 22 programs, including the Public Private Partnerships projects (PPPs) and the external loans. Since 2016, the Infrastructure Fund has 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 a sustainable energy. Many projects relating have already been completed in previous years. Other important infrastructure will be required to support the modernization and growth of the Timor-Leste's economy, including digital infrastructure, transport and logistics infrastructure for trade, as well as creation of broader framework for supporting industrial development.

The total budget for the Infrastructure Fund (excluding loans) in 2020 is $239.4 million for 21 programs. Out of this $238.3 million is the capital development budget. The VIII Constitutional Government has changed the policy of the threshold of the Infrastructure Fund for investments above US$ 5,0 Million. Therefore, the new projects with the total budget less than $5.0 million will be financed through the line ministry not the Infrastructure Fund.

The 2020 IF budget allocation for 21 programs, including roads and bridges has a biggest share in the Portfolio (52.9%) and the remaining budget for 2020 has been allocated to the power sector (6.1%), Information system program (6.0%), Tasi Mane program (6.9%), and other programs for health, education, public buildings, security and defence, rural and urban development financial support system.

Table 23: Infrastructure Fund budget and projection, $milion

	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Total Infrastructure	**366.5**	**311.3**	**790.5**	**632.6**	**360.8**	**178.6**
Total Infrastructure (excluding loans)	**279.5**	**238.3**	**710.3**	**578.6**	**314.9**	**144.8**
Agriculture	2.5	**2.6**	18.4	30.2	21.0	6.6
Water and Sanitation	3.7	**3.0**	41.7	30.6	11.7	4.0
Urban and Rural Development	9.5	**7.1**	8.0	5.0	3.0	0.0
Public Buildings	3.1	**8.4**	37.5	54.9	43.4	27.6
Education	1.0	**3.8**	34.0	37.4	30.8	19.5
Electricity	15.3	**14.5**	6.0	7.8	1.2	0.0
Informatics	2.9	**14.3**	26.9	1.0	2.9	3.1
Health	1.1	**0.7**	4.9	9.5	3.7	1.9
Security and Defence	3.3	**3.5**	28.1	21.8	6.2	0.0
Social Solidarity	0.5	**0.5**	1.3	0.8	0.6	0.0
Tasi Mane	60.6	**16.5**	312.1	257.9	111.4	70.3
Airports	12.5	**10.9**	5.8	12.8	10.3	0.0
Preparation of Designs and Supervision	3.9	**10.0**	15.5	1.0	0.0	0.0
Roads	127.4	**120.2**	146.3	94.2	60.0	5.0

	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
Bridges	10.0	**5.9**	8.8	1.9	2.8	3.0
Ports	2.2	**1.1**	4.6	5.5	1.3	0.8
Tourism	0.3	**0.5**	1.3	1.9	1.2	0.0
Financial System and Supporting Infrastructure	3.9	**5.3**	3.4	3.0	3.0	3.0
Youth and Sport	2.8	**1.8**	2.3	1.5	0.3	0.0
Maintenance and Rehabilitation	13.0	**7.8**	3.4	0.1	0.0	0.0
Loans Program	**87,0**	**73,0**	**80,2**	**53,9**	**45,9**	**33,8**

Source: Major Projects Secretariat, the Ministry of Planning and Strategic Investment, 2019.

2.5.1.3 Expenditure by Loan Financed Projects

Expenditure on loan-financed projects in 2020 is expected to reach $73.0 million, as presented in Table 24. This is a 16.1% decrease compared to the allocation in the 2018 State Budget as no significant new loan projects will be initiated and many existing projects are coming to an end. A detailed description of these projects is presented in Section 2.6.3.3.

Table 24: Expenditure on Loan Financed Projects, $million

	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2020 Budget
Loan Expenditure	**73.0**	**80.2**	**53.9**	**45.9**	**33.8**

Source: Ministry of Finance and Ministry of Planning and Strategic Investment, 2019.

2.5.1.4 Human Capital Development Fund

The purpose of the HCDF is to finance expenditures on scholarships and capacity development in line with the Strategic Development Plan of Timor-Leste. For the 2020 budget, the HCDF is broken down into four major programs: Vocational Training, Technical Trainings, Scholarships and Other Types of Training.

Table 25 summarizes the budget appropriations for HCDF by program. The total 2020 budget is $13.0 million, 35% lower than the allocation for the 2019 State Budget.

Table 25: Human Capital Development Fund by Program, $million

	2018 Actual	2019 Budget	2020 Budget	2021 Proj.	2022 Proj.	2023 Proj.	2018 Actual
Total HCDF (by Program)	**15.7**	**20.0**	**13.0**	**13.5**	**14.1**	**14.6**	**15.2**
Vocational Training	1.5	2.7	0.7	0.7	0.8	0.8	0.8
Technical Training	0.4	6.4	1.5	1.6	1.6	1.7	1.8
Scholarships	12.5	8.7	9.4	9.8	10.2	10.6	11.0
Other Training	1.3	2.2	1.4	1.5	1.5	1.6	1.6

Source: Secretariat for Human Capital Development Fund, 2019.

2.5.2 Ministry Allocations

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

Table 26: Proposed Allocation to Line Ministries, $000

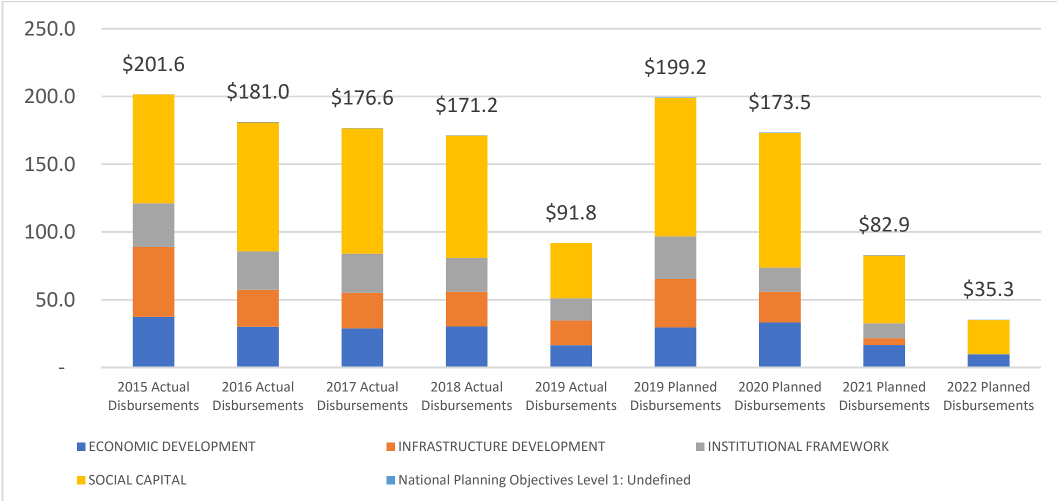
SDP Sector	Ministry	2020 Proposed Budget('000)
Economic Development	Ministry of Agriculture and Fisheries	**17.299**
	Ministry of Mineral Resource and oil	**87.528**
	Ministry of State, Coordinator of Economic Affairs	**1.690**
	Ministry of Tourism, Commerce and Industry	**8.493**
	Secretariat of State for Vocational Training Policy and Employment	**4.591**
Infrastructure Development	Ministry of Planning and Strategic Investment	**17.978**
	Ministry of Public Works	**229.514**
	Ministry of Transport and Communications	**10.787**
Institutional Framework	Appropriations for all of Government	**113.842**
	Minister of State for the Presidency of the Council of Ministers	**4.227**
	Ministry of Defence including FDTL	**38.456**
	Ministry of Finance	**30.159**
	Ministry of Foreign Affairs and Cooperation	**25.270**
	Ministry of Interior including PNTL	**48.522**
	Ministry of Justice	**18.253**
	Ministry of Legislative Reform and Parliamentary Affairs Including SECS	**7.753**
	Ministry of State Adminstration	**20.514**
	Prime-Minister	**1.922**
Social Capital	Ministry of Education, Youth and Sports Including SEJD	**96.975**
	Ministry of Health	**58.413**
	Ministry of Higher Education, Science and Culture Including SEAC	**7.210**
	Ministry of National Liberation Combatants Affairs	**101.008**
	Ministry of Social Solidarity and Inclusion	**57.510**
	Secretariat of State for Youth and Sport	**7.464**

Source: General Directorate of State Finance, Ministry of Finance 2019.

2.5.3 Development Partners' Commitments

The graph below shows steadily declining rates of donor support from 2015 until 2018, starting with a 10% decline from 2015 to 2016, which then steadied to decreases between 2% and 3% in 2017 and 2018 respectively. This decline is scheduled to be reversed in 2019, this is an encouraging sign of deepening donor support. It is also important to note that forward year estimates show a sharp decline in development partner non-lending assistance, however, two points should be noted: (i) development partner multi-year indicative future spending tends to be underreported; (ii) the Aid Transparency Portal collects information at the project level, meaning that if funds have not yet been committed to a project they will not be included in the analysis.

Figure 13: 2015-2022 Non-lending Donor Disbursements, $milion



Source: Aid Transparency Portal, report generated on 11 September, 2019.

Table 27: Planned Disbursements by SDP pillar and sub pillar for 2019-2020, $milion

SDP	SDP Sub-pillar	2019 Planned	2020 Planned	2 year total
Social Capital	Education and Training	44.7	44.2	88.9
	Health	35.0	28.0	63.0
	Social Inclusion	16.6	15.5	32.1
	Environment	5.1	3.9	9.0
	Undefined	0.7	7.7	8.4
	Culture and Heritage	0.2	0.1	0.3
Subtotal		**102.1**	**99.4**	**201.5**
Economic Development	Agriculture	14.9	18.1	33
	Rural Development	7.6	8.8	16.4
	Undefined	2.8	1.2	4.0
	Private Sector Investment	2.6	1.5	4.1
	Tourism	1.6	3.6	5.2
Subtotal		**29.5**	**33.2**	**62.7**
Infrastructure Development	Roads and Bridges	23.8	18.6	42.4
	Sea Ports	8.1	1.2	9.3
	Water and Sanitation	3.3	2.8	6.1
	Airports	0.7	0.1	0.8
Subtotal		**35.9**	**22.7**	**58.6**
Institutional Framework	Public Sector Management and Good Governance	20.5	12.5	33.0
	Security	8.4	4.4	12.8
	Justice	1.9	0.8	2.7
	Defence	0.4	-	0.4
	Foreign Affairs	0.1	0.1	0.2
Subtotal		**31.4**	**17.8**	**49.2**
SDP Undefined		0.3	0.3	0.6
TOTAL		**199.2**	**173.5**	**372.7**

Source: DPMU, Ministry of Finance, September 2019.

2.5.3.1 Policy Developments

On the 4th of July 2019, government led the organization of the annual Timor-Leste Development Partners Meeting. The event focused on the importance of Deepening Coordination for Financing Development. One of the main topics of discussion was the Foreign Aid Policy - Policies and Procedures Governing Non-lending Assistance. The policy calls on donors for greater alignment to government programs and priorities. In addition, it clearly states Government preferences in terms of how assistance should be provided.

One of the objectives of the policy is to encourage development partners to work directly with Government and to align their activities with greater specificity, i.e. at the annual action plan level, the Government sub-program level, and the SDP sub-pillar level. The government hopes that this will gradually result in improved coordination, an increase in knowledge transfer, and improved accounting for development partner funded activities in the budgeting and planning processes over the next coming years.

2.6 Financing

2.6.1 Definition of Financing

The total budgeted expenditure for 2020 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) which is financed by withdrawals from the Petroleum Fund (PF), loans and use of the cash balance (Treasury and RAEOA/ZEESM) and Europe 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, 2020-2024, $million

	2020	2021	2022	2023	2024
Total Financing	**920.8**	**1,445.6**	**1,365.1**	**1,177.3**	**1,071.6**
Excess Withdrawals from PF	**459.7**	1,209.9	1,256.0	1,079.1	988.1
Use of Cash Balance	**380.6**	**146.9**	**50.1**	**49.6**	**49.7**
Use of Treasury Cash Balance	254.3	50.6	50.1	49.6	49.7
Use of RAEOA/ZEESM Cash Balance	126.3	96.3	0.0	0.0	0.0
Borrowing /Loans (disbursements)	**73.0**	80.2	53.9	45.9	33.8
Europe Union - DBS	**7.5**	8.6	5.0	2.8	0.0

Source: National Directorate of Budget, General Directorate of Treasury and Petroleum Fund Administration Unit, Ministry of Finance, 2019.

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 (domestics and ESI) is a position that maintains fiscal sustainability, and 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 as it makes clearer what is fiscally sustainable.

The ESI is equal to 3% of the net petroleum wealth and is $536.8 million in 2020. Further details on the ESI and petroleum wealth can be found in Section 2.3.3 of the Budget Book. The Government plans to withdraw $459.7 million in excess of the ESI. 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 Loans

To meet development financing needs, the Government has explored possible additional sources of financing through external borrowing offered by multilateral and bilateral agencies. The main objective is to provide alternative financing for the development of strategic infrastructures as highlighted in the Strategic Development Plan (SDP) at minimum long-term cost, while meeting the national development goals.

Terms of Loans

At present, external loans are provided by international multilateral banks such as the Asian Development Bank (ADB) and the World Bank (WB), and bilateral agency of International Cooperation Agency of Japan (JICA). By creditor category, ADB is currently the major lender to Timor-Leste and its loans accounts for nearly 70% of the total loan amount followed by WB and JICA. Below are the terms of the loans.

Table 29: Terms of Loans

Creditor	Currency	Original Amount $m	Grace Period (year)	Initial Amortization (year)	Completion Year	Interest rate 2018
ADB	$, SDR	270.28	5.4	20	2044	2.08%
WB	$, SDR	75.20	6	20	2042	2.50%
JICA	JPY	52.78	10	20	2042	0.70%
Total		**398.26**				

Source: Loan Unit, Ministry of Finance, June 2019.

These loans carry considerable degree of concessionality and compare favourably to the opportunity cost of withdrawing funds from the petroleum fund. A key advantage is that the financial cost of concessional borrowing (1.96%) is currently lower than the annualized return on the Petroleum Fund since inception (4.3% as of August 2019) ensuring that the future debt repayments remain well within the country's capacity to pay.

Table 30: Cost of Borrowing VS PF Investment Return

Description	2012	2013	2014	2015	2016	2017	2018	Aug 2019
Cost of borrowing (effective rate)				1.02%	1.42%	1.68%	2.06%	1.96%
PF Investment Return since Inception Annualized	4.1%	4.4%	4.2%	3.8%	3.8%	4.4%	3.8%	4.3%

Source: Loan Unit and Petroleum Fund Adminisration Unit, Ministry of Finance June 2019.

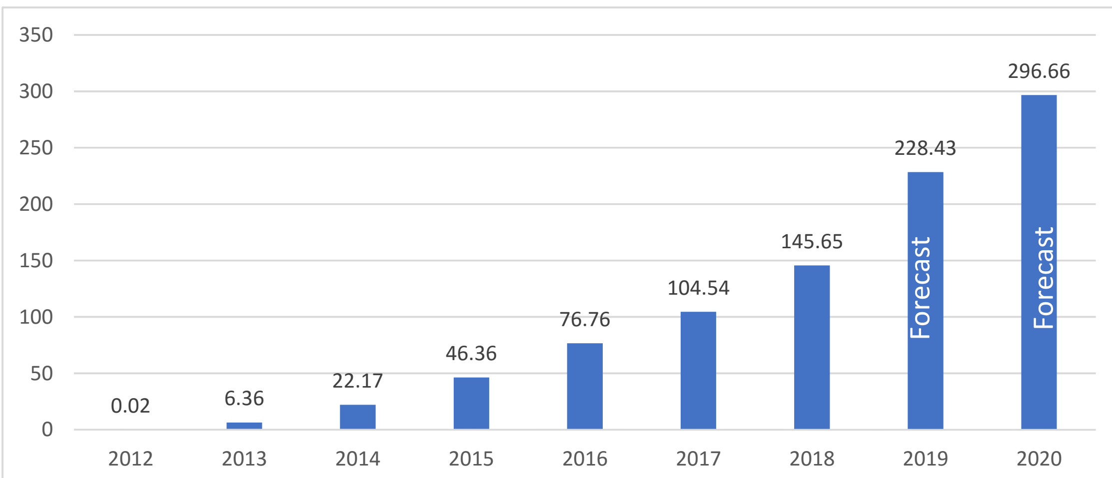
2.6.3.1 Portfolio Management

The management of public debt plays a critical role in determining the sustainability of fiscal policy. Due to change in methodology[8], Timor-Leste's debt carrying capacity is now rated higher than previous by the International Monetary Fund (IMF) article IV assessment held in 2019 increased from weak to medium; thus, risk of external debt distress was also lowered from medium to low.

Changes in External Debt Stock

Over the fiscal year, the stock of external debt increased by 40% from $104.54m to $145.65m. This increase is due to $41.11m of new disbursements from multilateral and bilateral institutions including ADB, WB and JICA for ongoing and new projects. Interest repayments for the period increased from $1.51m in 2017 to $2.58m as at end of 2018. This amount is relatively small compared to the amount the Government currently owes to these lenders.

Figure 14: Stock of External Debt, $milion



Source: PPPLU, Ministry of Finance June 2019.

Given the stages of project progress, it is expected that disbursement will continue to increase in 2019 despite a slight decline in 2020.

Debt Indicators

Timor-Leste's debt ratios increased over the years, marginally. Despite this, total public debt remain sustainable over the years reflecting the Government's prudent management of the debt.

Table 31: **External Debt Indicators for the period 2012-2018, % of GDP and Revenue**

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[8]In evaluating debt sustainability, Ministry of Finance is utilising a method jointly developed by the World Bank and International Monetary Fund, known as Low Income Country Debt Sustainability Analysis (LIC-DSA). As set under the new guidelines, a country's debt carrying capacity is classified into one of the three categories: weak, medium and strong based on its composite indicator score (CI).

	2012	2013	2014	2015	2016	2017	2018
Total Debt to GDP							
External Debt to GDP	0.00	0.11	0.55	1.47	3.02	4.20	5.58
Total Debt Service to Revenue							
External Debt Service to Revenue	0.02	0.04	0.07	0.12	0.28	0.69	1.27
External Debt Service to GDP	0.00	0.00	0.00	0.01	0.02	0.05	0.08
In millions of US Dollar, unless otherwise indicated							
Memorandum items							
External Debt	0.02	6.36	22.17	45.33	75.72	104.38	145.65
External Debt Service	0.03	0.06	0.11	0.21	0.55	1.31	2.19
GDP	6,661.70	5,637.60	4,041.61	3,092.63	2,503.59	2,487.42	2,611.79
Revenue	135.88	151.10	170.23	173.69	200.51	188.84	171.89

Source: Loan Unit, Ministry of Finance June 2019.

External Debt to GDP - The size of external debt to GDP during the period was relatively small when compared to the debt burden threshold and benchmarks as established under the debt sustainability frameworks for low income countries[9]. While the ratio constantly increased marginally from 0.11%in 2013 to 5.58% in 2018, the values are far below 40%. This marginal increase was due to an increase in disbursement and external downward growth trend in GDP. While there was a slight recover during 2017-2018, the percentage increase in external debt was still higher than GDP growth, hence, higher external debt to GDP ratio.

Debt Service to Revenue – The debt service to revenue ratio started to increase more than two times in 2015. This increase was primarily due to an increase in debt service payments while revenue declined from 2017-2018. Repayment of principal started in September 2017 for ADB loan 2,857. Despite the increase from 0.69% in 2017 to 1.27% in 2018, this percentage of debt service to revenue is still well-under the threshold 18 percent.

Debt Service, Actuals and Forecasts – Annual debt service is calculated on each loan to cover the repayment of principal, interest and other miscellaneous charges on a debt for a particular period.

Table 32: Debt Service by Institution and Type of Payment, $million.

Donor	Debt Service	2018 Actual	2019 Actual	2019 Proj.	2020 Proj.	2021 Proj.	2022 Proj.	2023 Proj.	2024 Proj.
ADB	Principal	0.54	2.43	2.6	**3.70**	4.15	11.93	14.12	14.12
	Interest	1.65	2.41	2.7	**4.37**	7.13	5.13	5.49	5.32
	Charges	0.12	0.08	0.2	**0.12**	0.03	0.00	0.0	0.0
WB	Principal	0.0	0.83	0.8	**0.83**	1.41	2.75	2.75	2.75
	Interest	0.71	0.83	1.1	**1.77**	1.92	1.89	1.82	1.75
	Charges	0.0	0.0	0.0	**0.0**	0.0	0.0	0.0	0.0
JICA	Principal	0.0	0.0	0.0	**0.0**	0.0	2.57	2.57	2.57
	Interest	0.06	0.04	0.0	**0.00**	0.00	0.01	0.35	0.33
	Charges	0.04	0.02	0.0	**0.02**	0.01	0.0	0.0	0.0

[9] Further reference on this subject: "Guidance Note the Bank-Fund Debt Sustainability Framework for Low Income Countries" , February 2018.

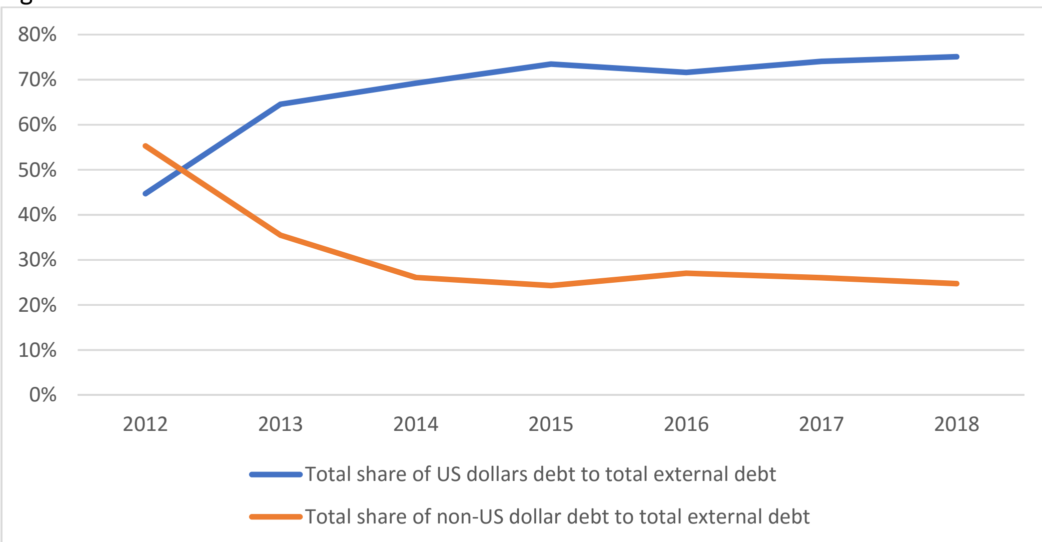
Total	**3.13**	**6.63**	**7.5**	**10.81**	**14.65**	**24.28**	**27.10**	**26.84**

Source: Loan Unit, Ministry of Finance, June 2019.

Risk Indicators

Foreign Exchange Risk – Complying with the loan policy note, the US dollar has remained the dominant currency in the Government's external debt portfolio. Given the country's highly dollarized economy, the large share of US dollar currency debt in the portfolio 75% in 2018 cushioned the Government from extreme exchange rate movements. The policy to retain a larger share of US dollars debt continues at least in the short to medium term.

Figure 15: US Dollars Debt VS Non-US Dollars Debts



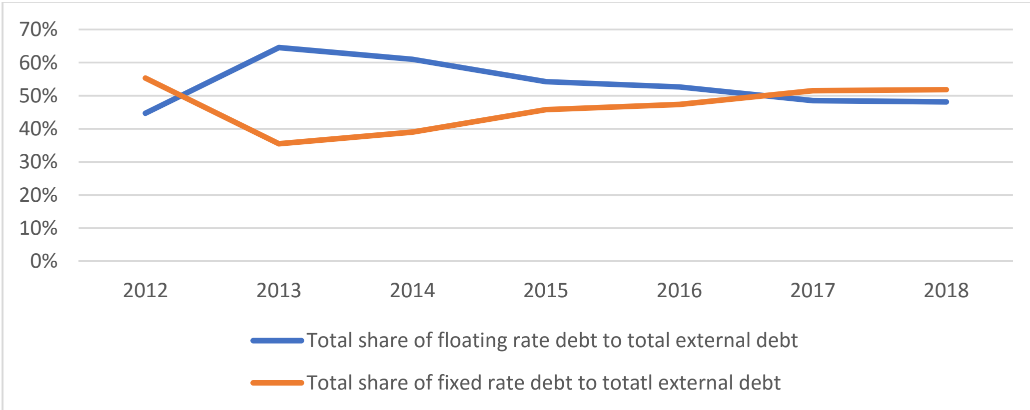
Source: Loan Unit, Ministry of Finance, June 2019.

Interest rate risk – From 2013, the total share of fixed rate debt started to increase until it comprised the majority share of the debt portfolio, in 2017 and 2018 consecutively. The change occurred as a result of the ability of the Government in managing interest rate risk independently by converting the priority for disbursement from variable rate to fixed rate taken into account market interest rate fluctuation.

The cost of borrowing is expected to continue to rise as Timor-Leste is now classified as a blend country[10] and is slowly being phased out from concessional financing by its external creditors. To limit the exposure to interest rate shocks, there needs to expand the use of more concessional financing from bilateral loan providers.

Figure 16: Fixed vs floating

[10] Being a blend country, Timor-Leste has a limited access to concessional lending with a fixed interest rate.



Source: Loan Unit, Ministry of Finance, June 2019

2.6.3.2 Current Project Status

There are currently 15 ongoing road projects funded by concessional loans of which 6 projects had already been completed. These include roads connecting Tibar-Liquica/Tibar-Gleno, Manatuto-Laclubar junction and Solerema-Ainaro corridor. Other projects that most likey to be concluded by 2019/2020 are roads from Laclubar junct.-Natarbora, Manatuto-Baucau, and Dili-Manatuto bringing the total numbers of projects completion to over 60% by end the year.

Total capital contribution made by this investment is $365 million which is by a ratio of total investment, concessional loans accounted for approximately 62%. Of this, $126 million has been disbursed leaving a balance of $103 million to be spent for next 1-2 years in accordance with project construction periods. On the other hand, state contribution to the overall budget of Civil Works contract was $136 million with an estimated remaining $31 million for further disbursement.

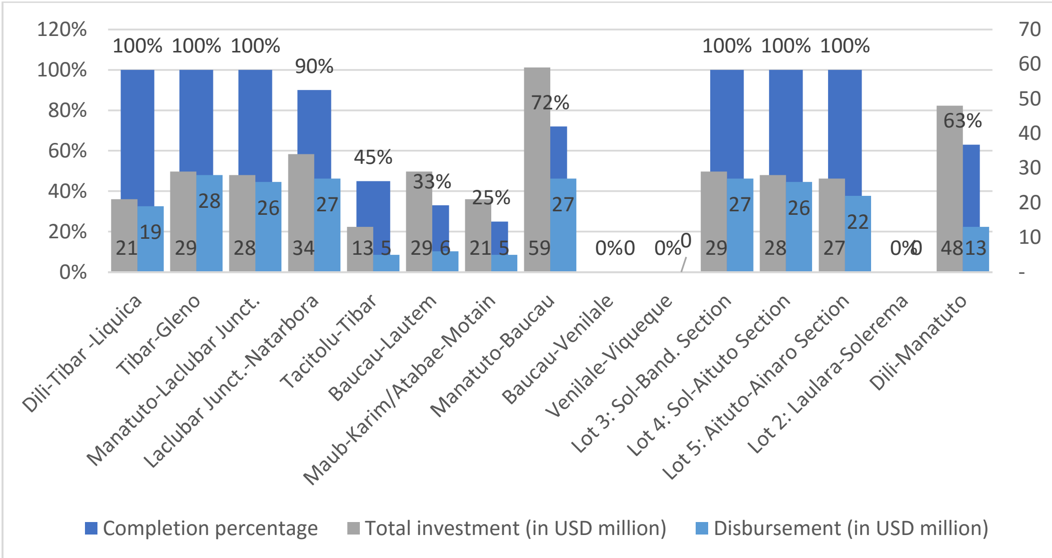
New projects includes road section from Baucau-Venilale/Venilale-Viqueque and Laulara-Solerema. The key challenges in the implementation of these projects were mainly relating to the release of social safeguard documents by relevant line ministries including delay in environmental licensing and resettlements and payment delays. As for the latter, it explained the trends as illustrated in the graph below for road section Dili-Manatuto and Manatuto-Baucau. While projects progress was relatively high, disbursements were significantly low relative to the contract amounts.

Table 33: Total Investment in Civil Works, $million

Source of Fund	Total Investment in Civil Works	Disbursement as at April 2019	Contract Balance
Loan Fund	229	126	103
State Contribution	136	105	31
Total	**365**	**231**	**134**

Source: Loan Unit, Ministry of Finance, June 2019.

Figure 17: By Project, Civil Works Progress as of April 2019, Disbursement, and Contract Price



Source: Loan Unit, Ministry of Finance, June 2019.

It is important to note that there is about $40 milions loan saving from ADB ongoing loan-funded projects. The cost reduction increases year by year as a result of the number of participating bidders also increases in the public procurement; hence, bringing down the prices by approximately 40% . This includes surplus in civil works, consulting services and unallocated loan contingencies. By projects, Baucau-Lautem/Maub-Karim/Atab-Motain contributed over $25m in saving while other projects such as Manatuto-Natabora, Baucau-Viqueque, Manatuto-Baucau, and Tacitolu-Tibar accounted for the remaining balance.

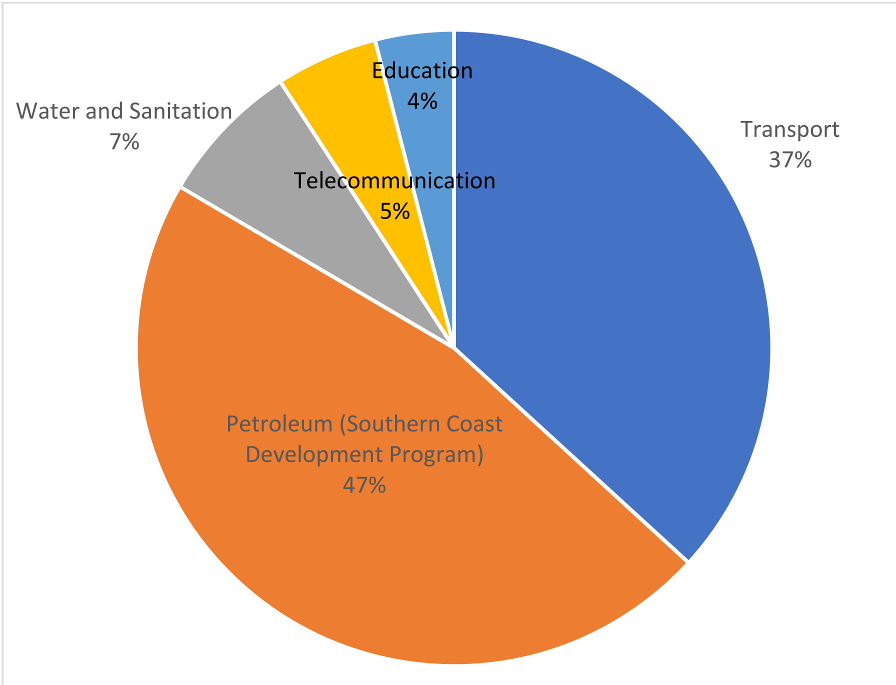
As a borrower, the Government can decide whether to fully utilise the saving or simply cancel the amount by complying with public debt law No.13/2011 and other relevant laws. For this purpose, the Government has already requested ADB to maximise the use of some of this saving to fund for the construction of three (3) bridges: Seical Bridge, Borouai causeway and Malailada causeway with a total estimated cost at $14 million a long Baucau-Lautem road section and mitigate the pressure on the state budget.

2.6.3.3 Future Loans

Infrastructure development would remain to play a key role in the country's economic development success in the medium term. New strategic sectors such as water, education, telecommunication, and petroleum should receive concessional financing. This would help unleash the growth potential of other key economic activities; hence, inclusive economic growth and poverty reduction.

In this respect, annual loan ceiling is required for parliamentary approval, in the context of the State Budget Law, prior to implementing all these programs. The amount is set according to project cost estimates and debt sustainably analysis. On the DSA, based on the Ministry of Finance internal analysis, the country's external debt stock to GDP remained relatively low in 2018, which is 5.58%. IMF staff completed the country's 2019 article IV consultation by stressing the need for making effective use of concessional borrowing for continued investment in infrastructure. In light of all the above, the Government is therefore, proposing a ceiling of $750 million for new concessional foreign loans to be negotiated in 2020.

Figure 18: Sectoral Allocation of Proposed Loan Ceiling for 2020



Source: Loan Unit, Ministry of Finance, June 2019.

2.6.4 Use of Cash Balance

Total cash balance that will be used to finance 2020 State Budget is $380.6m. This cash balance is from the Consolidated Fund of Timor-Leste (CFTL) at the end of 2019 that is forecast to be of $254.3m million and $126.3m cash balance from RAEOA/ZEESM. On the other hand, there is no forecasted rollover of cash balances for the HCDF from 2019.

Table 34: Use of Cash Balance in 2019, $million

Total	**2020**
HCDF Rollover	**0.0**
Drawdown of Cash Balances from the Treasury Account	**254.3**
Cash Balance from RAEOA/ZEESM	**126.3**

Source: General Directorate of Treasury and Secretariat for the Human Capital Development Fund, 2019.

2.6.5 Direct Budget Support

Timor-Leste has been receiving Direct Budget Support (DBS) from the European Union since 2014. The latest agreement was signed in 2016 under the 11th European Development Fund. The maximum contribution of the budget support component is $30 million for five years (2016-2020).

EU DBS is considered as a financing for 2020 State Budget because it uses Government system (the money is in a Treasury sub-accunt) and on-budget, where the money is used directly by the beneficiaries ministries for the public financial management program (Ministry of Finance), Malnutrition (Ministry of Health) and decentralization (Ministry of State Administration).

Total amount of DBS for 2020 State Budget is $7.5m, that is distributed to Ministry of Finance ($3.9m), Ministry of Health ($2.2m) and Ministry of State Administration ($1.4m).

In this context, 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.

In 2019, it received a first tranche of $3.1 million. The second tranche of $6.7 million was received on 19 September 2019. Out of this, $3.8 million was distributed to the Ministry of Finance, $2.2 million to the Ministry of Health and $559,951 to the Ministry of State Administration. Ministry of Finance has executed $4.0 million (national technical assistance, international technical assistance, overseas travel, incidental costs, social security, transfer to Ministry of Health and Ministry of State Administration) over the first three quarters of 2019.

2.6.6 Public Private Partnership

2.6.6.1 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 7 years and started out by establishing a PPP Policy, PPP legislation and a dedicated PPP and Loans Unit under the 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 includes a requirement that all PPP projects undergo both a pre-feasibility study and a full-fledged feasibility prior to proceeding to the procurement phase.

DL 8/2014 stipulates the formation of PPPLU, a PPP facilitation agency under the Ministry of Finance to take on the task of managing and implementing the PPP Project Cycle in coordination with line ministries and Council for Administration of Infrastructure Fund (CAFI). An important role of the PPPLU 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 that will allow for development of small to medium scale PPPs. One Sector that have high potential for this is the Tourism Sector.

2.6.6.2 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 another one in early **Feasibility Stage** (Affordable Housing).

Tibar Bay Port PPP 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. Concession Agreement was signed in June 2016 while financial closing was reached in August 2018. The project is currently in construction phase with construction yard and offices have been installed, general design already approved, detailed design on-going, dredging and reclamation on-going while preparation of next work items including equipment tendering is on-going. Currently, it is estimated that commencement of operation will happen in August 2021.

Tibar Bay Port PPP project involved the provision of Viability Gap Funding (VGF) of $129.5 million in 2016 (recorded as 2016 expenditure) for earthwork, construction and equipment purchase. Private sector contribution to this project is around $155.0 million meaning that the Government's VGF contribution stood at about 45% of total project cost.

To hold the VGF until disbursement, the Government was contractually required to deposit the full amount in an Escrow Account. For this purpose, a three party Escrow Agreement was reached between the Government, Timor Port SA and the United Overseas Bank (UoB) of Singapore in November 2016. First disbursement from the Escrow Account has occured on August 20th, 2019.

The Escrow Account is earning interests. As of 16th September, 2019, interest earned amounted to **$5.41m**, deposited in the Escrow Interest Account. The Escrow Agreement stipulated that the interest earned can only be transferred to the Government after the closing of the account and/or termination of the Escrow Agreement.

Medical Diagnostics - PPP

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**. Previously, the Feasibility Study and Transaction Structuring Report (TSR) have been approved by CAFI on 11 July 2019 after clearance from the Ministry of Health in June 2019. The TSR recommended that the project upgrade imaging and laboratory diagnostic services 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 selected facilities and 10 years operation period. Potential bid parameter and bid evaluation criteria have also been recommended.

Dili Water Supply - PPP

Dili Water Supply PPP project is currently in the finalization of FS phase II where options for PPP modalities selected during the phase I (lease, reduced-risk lease and management contract) were examined in greater detail from the technical, financial, economic and legal perspectives. The main objective of the on-going study is to provide information and analysis that will enable the government to decide whether and how to involve the private sector in the water supply services for the capital city. However, recent change in government policy regarding reform of the sector will likely make this project difficult to turn into a PPP project. Hence, no further budgetary allocation has been made for this program.

Affordable Housing

The affordable housing project is in the process of finalizing its pre-feasibility study awaiting site identification and formal designation from National Directorate of Land, Property and Cadastral Service (DNTPSC – Portuguese Acronym). Upon adjustments to several conceptual parameters based on available sites, results will be re-submitted to the Minister of Public Works for clearance. Subsequent step is to secure CAFI approval before the project can proceed to Feasibility Study phase where deeper analysis of the technical, legal, commercial as well as social and environmental terms are conducted.

2.6.6.3 New Initiatives

Tourism is thought to be one of several strategic sectors with potential to further diversify Timor-Leste's economy. Due to its close linkages to other sectors, improvement to the tourism sector requires wide range of intervention, e.g. in transport infrastructure, water and sanitation, agriculture, health infrastructure and education and training.

3 2020 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 2020 ESI

4.3 ESI Report: Transfers from the Petroleum Fund in Excess of ESI 2020

Supporting documents will be presented separately

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MINISTRY OF FINANCE

Torre Ministerio das Finanças, Aitarak-Laran , Díli, Timor-Leste

Website - www.mof.gov.tl