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Road To Doha: An Ambitious Agenda for The Next Decade Through Reinvigorated and Innovative Financing for Development of the Asia-Pacific Least Developed Countries

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Excellencies, distinguish participants

It is a great pleasure for me to have this opportunity to share Timor-Leste's view on this very important session.

I will briefly outline three things in my intervention:

First, an overview on the financial sector development in Timor-Leste;

Second, challenges and opportunities for sector development;

Third, key actions required to underpin preparation for LDC graduation.

Key information on the overview of financial sector development in Timor-Leste include:

- Tax revenue to GDP ratio is around 12 percent, which is below 15 percent of the minimum threshold to provide basic service.

- Government's main revenue is from oil and gas. The inflow of this revenue started in 2005 and all the revenues are saved in a sovereign wealth fund, called Petroleum Fund.

- The Petroleum Fund has been growing since its establishment, with the current balance of over $19 billion. The growing balance is driven by the inflow of revenue from oil and gas, returns from investment, and the prudent withdrawal to finance Government annual expenditure.

- The Petroleum Fund accounts for over 80 percent of financing source for Government annual expenditure.

- Average total Government and recurrent expenditures to GDP in the last five years (2016-2020) is 91 percent and 59 percent, respectively.

- Average fiscal deficit to GDP in the last five years is 35 percent, which was predominantly financed by excess withdrawal from the Petroleum Fund.

- Loan to GDP ratio in 2020 was 26 percent, where all the loans are project base loans to finance infrastructure development. On the other hand, Government yet to issue bonds.

- Development partners support to GDP was around 11.8 percent in 2020.

Two KEY CHELLENGES with regards to financing for development that I would like to share with you are:

1. Institutional capacity constraint

   Despite substantial improvement on institutional capacity development has been made, capacity constraint remains a challenge. Particularly on:

   - implementation and oversight mechanism of SDGs and local development agenda;

   - rationalization, prioritization, and absorptive capacity of public expenditure towards achieving development agenda targets in medium to long-term horizon;

   - domestic resource mobilization - limited capacity of revenue collection agencies to collect more revenue;

   - inefficient service delivery, including in finance sector due to limited e-services, and limited capacity to underpin private sector development for economic diversification and employment creation.

2. Fiscal sustainability concern

   The Petroleum Fund provides a buffer and a strong fiscal anchor to the Government. However, fiscal sustainability concern is mounting due huge financing development needs, the continued excess withdrawals to finance the growing fiscal deficits – especially in the recent years, and the downward trend of petroleum revenue.

With regards to the opportunities, I would like to flag 5 key opportunities

1. Integration of SDGs to country's development agenda

   Timor-Leste has adopted SDGs into its development agenda framework. The alignment of SDGs and the Strategic Development Plan (SDP) and the roadmap for implementation set opportunity and clear guidance for programs and priorities to be financed in the next decade.

2. Implementation of Fiscal Reform

   The ongoing implementation of the Fiscal Reform presents a great opportunity for the country to increase tax revenue to 15 percent of GDP by 2023 and to correct economic distortions for more private sector investments. The reform that also focuses on improvement of Information Financial Management System will contribute to digital financial services, such as online tax service and payment, and transfer of cash to beneficiaries of social assistance programs.

3. The Petroleum Fund

   Existence of the Petroleum Fund presents two great opportunities for the Government to mobilize resources to finance development:

   First, in the short to medium term, the Government can use the Petroleum Fund to finance development needs, but it should be done in prudent and sustainable manners.

   Second, Government could protect and ensure sustainability of the Petroleum Fund by leveraging the fund for a more loan mobilization from institutional bilateral and multilateral financial institutions. Given the fund generates an average investment return of 3 percent, comparing cost of borrowing and the opportunity cost of investment return is a key policy guidance and principle.

4. Low debt to GDP ratio

   Risk of debt distress is very low, as debt to GDP in 2020 was 26 percent and the country has the Petroleum Fund with a balance of over $19 billion. This presents an enormous space for the Government to mobilize more loan resources to finance development needs.

5. Foreign aid policy

   Country's new foreign aid policy that was approved by Government and development partners in the 2019 Timor-Leste development partners meeting provides a great opportunity to strengthen partnership for efficient grants resource mobilization to finance development in Timor-Leste, guided by the principle of country-owned, country-led, and using country system.

7 KEY ACTIONS REQUIRED FOR MOBILIZATION OF FINANCIAL RESOURCES TO UNDERPIN TIMOR-LESTE'S PREPARATION FOR LDC GRADUATION.

1. INTRODUCE INNOVATIVE PARTNERSHIP

   Business as usual in partnership may no longer relevant to support preparation for LDC graduation and beyond. Innovative partnership that puts private sector as the centre of cooperation for economic diversification, domestic resource mobilization, and promotion of trade could be a policy and strategic option that need to be considered.

   Moreover, there is also a need to adjust and improve the existing coordination and dialogue mechanisms between Government and development partners for external resource mobilization (grants and loans).

   Innovative coordination mechanisms that need to be promoted and established are:

   i) Promoting a regular dialogue between the Government, private sector and financial institutions.

   ii) Strengthening development partners meeting – on quarterly and annual basis.

   iii) Reactivating and integrating SDGs and SDP sectoral working groups.

   iv) Engaging private sector and development partners in the ongoing Government's reforms.

2. RESTRUCTURING FINANCIAL LANDSCAPE

The current financial landscape that is highly dependent on withdrawal from the Petroleum Fund and limited resources mobilized from taxes to finance the great development needs are unsustainable for the country.

The Government has shown its commitment to address the issue through Fiscal and Public Financial Management Reform. Ensuring sustainability of the Petroleum Fund, accessing more concessional resources from bilateral and multilateral financial institutions at sustainable level to finance strategic investments, improving compliance and tax base for more domestic resource mobilization, and efficient use and management of grant resources are policies that should be implemented with high commitment, consistent and within a proper timeframe.

The restructuring financial landscape needs to involve the following elements

i) Ensuring Sustainability of the Petroleum Fund
   To ensure Petroleum Fund sustainability, the Government should be consistent with the schedule of *"front-loading fiscal policy"* implementation that will conclude in 2024, adopting a fiscal rule on limiting "excess withdrawal" to 60 percent of Estimated Sustainable Income (ESI), tapping up on more concessional resources for strategic investments, and setting up a fiscal rule on the fund balance threshold, where excess withdrawal will not allow if the balance has hit the threshold.

ii) Accessing more external concessional resources

iii) Consistent with the implementation of Fiscal Reform agenda to achieve the target of 15 percent of domestic revenue to GDP by 2023

iv) Promoting the use of new deal principles of "country own, country led and using country system" for efficient use of external grant resources

v) Rationalization of expenditure under prudent fiscal policy framework

   In the short term, more resources should be allocated for mitigation and prevention of COVID-19 and economic recovery measures, and expenditures strategies for medium to long-term should focus on investing in people, infrastructure, technologies, and strategic sectors, such as agriculture and tourism for a resilient and competitive economy, and inclusive and sustainable development.

3. PROMOTING PRIVATE SECTOR INVESTMENT TO DIVERSIFY THE ECONOMY

   i) Improving business environment
   ii) Diversifying the economy with agriculture, tourism, extractive industry and manufacturing

4. MORE FISCAL SPACE FOR HUMAN CAPITAL DEVELOPMENT

Rationalization of expenditure to give more fiscal space for human development – particularly to education, health, and food security based on public expenditure review (PER) and medium-term expenditure framework (MTEF) are critical.

5. ENHANCING PUBLIC SERVICE DELIVERY WITH E-GOVERNMENT

Institutional capacity constraint is a structural challenge that need to be transformed. Promoting e-government for all government services across the country and integrating/interfacing all information systems will correct distortions in public service delivery and improve economic efficiency.

6. PROMOTING EVIDENCE-BASED POLICY MAKING PROCESS

Policies would be efficient and well targeted if they are designed and made based on proper data and analysis. Thus, evidence-based policy making process is important for the Government on LDC graduation and beyond – to evaluate preparation for LDC graduation and monitor implementation of SDG and SDP.

7. NATIONAL COMMITTEE FOR LDC GRADUATION

- To prepare for a smooth graduation.
- Identify and exploit international support measures, such as financial and trade facilities.