

SM/13/274  
Correction 4

November 22, 2013

To: Members of the Executive Board

From: The Secretary

Subject: **Democratic Republic of Timor-Leste—Staff Report for the 2013 Article IV Consultation**

The attached corrections to SM/13/274 (10/15/13) have been provided by the staff:

**Typographical Errors**

**Page 4, para. 1, line 3:** for “decade of independence.” read “decade as a sovereign nation.”

**Page 29, Table 1, line 1:** for “US\$6.4 billion” read “US\$6.3 billion”

**line 3:** for “US\$5,820” read “US\$5,463”

**line 4:** for “US\$14,00” read “US\$1,175”

**line 14:** for “In percent of non-oil GDP” read “In percent of GDP”

Questions may be referred to Ms. Hunter, APD (ext. 38877.)

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## CONTEXT

1. **Timor-Leste has made substantial progress in overcoming the difficult challenges it has faced as a sovereign nation.** A number of key milestones have been achieved as it enters its second decade [as a sovereign nation of independence](#). The 13 year UN presence was concluded successfully in 2012 and parliamentary and presidential elections were held in mid-2012, with Prime Minister Xanana Gusmão re-elected to head a coalition government. A Strategic Development Plan (SDP) to guide Timor-Leste to upper middle-income status and a significant reduction in poverty by 2030 started in 2011. Timor-Leste is a founding member of the g7+ group of 18 fragile and conflict-affected countries and has taken a leadership role, pioneering the *New Deal* approach that is consistent with its SDP (Box 1). Developmental partners including the IFIs and bilateral donors have worked collaboratively with the Timorese authorities on policies and operational reforms required to achieve the goals of the SDP and New Deal.

2. **Nevertheless fragilities remain.** Timor-Leste is one of the most natural resource dependent countries in the world with large developmental needs. Oil revenues have been used to promote development but reserves with production agreements will end in 2024 and many uncertainties persist over potential production from new fields (Box 2).<sup>1</sup> Diversification is crucial to generate much needed employment and poverty reduction. The government has scaled up expenditures with the aim of kick starting the non-oil sector and developing forward and backward linkages from oil production. However, higher spending has faced significant capacity and absorptive constraints and has led to inefficiencies, the emergence of rent seeking behavior, and persistently high inflation that hurts the poor and undermines long-term growth.

3. **Governance frameworks are in place but policy implementation capacity is limited.** There is a relatively strong governance framework that promotes accountability with an active civil society. A well regarded Petroleum Fund (PF) has assets equivalent to over two times GDP and is compliant with the Extractive Industries Transparency Initiative and the Santiago Principles with firm parliamentary oversight. Oil revenues are solely channeled through the PF and withdrawals are limited by law to the Estimated Sustainable Income (ESI) that is calculated as 3 percent of estimated oil wealth—although excess withdrawals are allowed under certain circumstances. Under this fiscal rules based approach, expenditures are constrained by the ESI and non-oil revenues. Given full dollarization, this serves as the nominal anchor. Policy making is conducted by a small technocratic elite but implementation capacity is weak, constraining the effectiveness of policies and outcomes.

## RECENT DEVELOPMENTS

4. **The non-oil economy has grown rapidly averaging over 12 percent from 2008 to 2011 allowing per capita incomes to steadily increase.**<sup>2</sup> Domestic demand was driven by the rapid

<sup>1</sup> Production is mainly gas although some liquids are produced. For simplicity, oil is used here to denote the sector.

<sup>2</sup> GDP data for 2012 have yet to be released. The authorities projected non-oil growth of 10.6 percent (in the 2013 Budget Book). Staff expects a downward trend in the growth momentum due to a significant under-spending on

(continued)

**Table 1. Timor-Leste: Selected Economic and Financial Indicators, 2009-14**

GDP at current prices (2012):	US\$6.3 <del>6.4</del> billion					
Population (2012):	1.1 million					
GDP per capita (2012):	US\$5,643 <del>5,820</del>					
Non-oil GDP per capita (2012):	US\$1,175 <del>1,400</del>					
Quota:	SDR 8.2 million					
	2009	2010	2011	2012	2013	2014
				Est.	Proj.	
(Annual percent change)						
Real sector						
Real total GDP	-6.7	-1.4	7.3	5.7	-3.2	-6.9
Real non-oil GDP	12.8	9.5	12.0	8.3	8.1	8.0
CPI - Timor Leste (annual average)	0.1	4.5	11.7	13.1	10.6	9.5
CPI - Timor Leste (end-period)	1.1	8.0	15.4	10.8	10.4	8.5
(In percent of <del>non-oil</del> GDP, unless otherwise indicated)						
Central government operations						
Revenue	62.6	64.9	66.5	69.1	59.7	63.6
Domestic revenue	2.8	2.3	1.9	2.2	2.4	3.3
Petroleum revenue	51.3	55.3	59.7	62.9	53.4	56.1
Grants	8.5	7.3	4.9	4.0	3.9	4.2
Expenditure	31.3	27.0	23.8	22.1	23.5	26.5
Recurrent expenditure	12.0	12.0	8.8	10.7	10.8	11.1
Capital expenditure	10.8	7.6	10.1	7.3	8.8	11.2
Donor project	8.5	7.3	4.9	4.0	3.9	4.2
Overall balance	31.3	37.9	42.7	47.0	36.2	37.1
Non-oil overall balance (in percent of non-oil GDP)	-79.8	-78.3	-87.5	-73.7	-65.2	-56.7
(Annual percent change, unless otherwise indicated)						
Money and credit						
Deposits	38.7	9.8	8.9	26.2	21.2	21.7
Credit to the private sector	1.1	5.9	21.1	20.5	21.2	21.7
Lending interest rate (percent, end-period)	11.2	11.0	11.0	12.2	...	...
(In millions of U.S. dollars, unless otherwise indicated)						
Balance of payments						
Current account balance 1/	1,287	1,676	2,340	2,738	2,105	1,819
(In percent of GDP)	39.0	39.8	40.4	43.5	34.3	32.1
Trade balance	-320	-277	-349	-639	-731	-829
Exports 2/	15	29	25	33	37	42
Imports	335	306	374	672	769	871
Services (net)	-774	-961	-1,415	-921	-1,004	-1,118
Petroleum revenue	1,692	2,331	3,461	3,960	3,273	3,183
Overall balance	39	156	55	422	-194	122
Public foreign assets (end-period) 3/	5,627	7,303	9,765	12,652	14,419	16,748
(In months of imports)	58	65	63	91	93	96
Exchange rates						
NEER (2005=100, period average)	95.4	89.3	84.2	86.4	...	...
REER (2005=100, period average)	105.2	102.3	105.6	118.1	...	...
NEER (2005=100, end-period)	89.3	86.7	86.0	86.5	...	...
REER (2005=100, end-period)	99.1	101.7	114.8	125.8	...	...
Memorandum items:						
GDP at current prices:	3,299	4,216	5,797	6,300	6,129	5,673
Non-oil GDP	827	934	1,128	1,355	1,615	1,901
Oil GDP	2,472	3,281	4,669	4,945	4,514	3,772
Crude oil prices (U.S. dollars per barrel, WEO)	62	79	104	105	104	101
Petroleum Fund balance (in millions of U.S. dollars)	5,377	6,897	9,303	11,768	14,206	16,535
Petroleum Fund balance (in percent of non-oil GDP)	650	738	825	868	880	870
Public debt (in millions of U.S. dollars)	0	0	0	0	44	267

Sources: Timor-Leste authorities; and IMF staff estimates and projections.

1/ Excludes trade in goods and services of entities located in the Joint Petroleum Development Area which are considered non-resident entities.

2/ Excludes petroleum exports, the income of which is recorded under the income account.

3/ Includes Petroleum Fund balance and the central bank's official reserves.

**Table 2. Timor-Leste: Summary Operations of the Central Government, 2009-18 1/**

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
	Staff Proj.				Projections 2/					
	(In millions of U.S. Dollars)									
Revenue	2,064.9	2,737.0	3,853.6	4,351.2	3,659.6	3,609.0	3,499.4	3,632.2	3,764.2	3,556.2
Petroleum revenue	1,691.7	2,331.3	3,461.3	3,959.9	3,273.1	3,183.4	3,044.9	3,150.7	3,221.2	2,962.3
Oil/gas receipts	1,660.2	2,110.2	3,240.1	3,559.1	2,725.7	2,451.2	2,176.7	2,144.7	2,058.5	1,668.4
Interest	31.5	221.1	221.2	400.8	547.3	732.1	868.2	1,006.1	1,162.7	1,293.9
Taxes	43.5	50.2	78.4	98.5	106.7	119.8	140.6	162.1	218.8	255.9
Taxes on income, profits, and capital gains	13.3	18.2	27.8	37.2	42.1	48.8	58.0	67.5	77.7	90.9
Taxes on goods & services	23.9	26.5	34.2	47.9	53.2	59.7	70.7	82.2	128.2	150.0
Taxes on international trade & transactions	6.3	5.5	16.4	13.4	11.3	11.3	11.9	12.3	12.9	15.0
Grants	281.8	309.3	283.9	253.8	239.0	240.8	243.0	242.9	242.8	242.8
Other revenue	47.9	46.2	30.0	38.9	40.9	65.0	70.8	76.5	81.4	95.2
Expenditure	1,032.6	1,137.2	1,379.6	1,389.7	1,439.0	1,503.2	1,579.5	1,575.5	1,571.5	1,567.7
Current expenditure	394.2	506.1	507.7	674.1	660.6	627.6	596.2	596.2	596.2	596.2
Wages and salaries	87.3	91.5	111.6	130.3	126.1	120.4	113.9	114.1	113.9	113.9
Current transfers	94.1	168.7	142.6	215.1	187.7	179.2	169.6	169.9	169.5	169.5
Goods and services	212.8	245.9	253.5	328.7	346.8	328.0	312.7	312.2	312.8	312.8
Subsidies	40.0	30.9	45.5	104.1	106.7	102.4	93.4	85.2	77.7	75.0
Capital expenditure	356.6	321.8	588.0	461.8	539.4	634.8	740.3	736.4	732.6	728.7
Donor project	281.8	309.3	283.9	253.8	239.0	240.8	243.0	242.9	242.8	242.8
Overall balance	1,032.3	1,599.8	2,474.0	2,961.5	2,220.7	2,105.8	1,919.9	2,056.7	2,192.6	1,988.5
Transfer to Petroleum Fund	1,179.7	1,520.3	2,406.3	2,904.9	2,430.5	2,329.1	2,180.8	2,274.5	2,329.8	2,051.1
Non-oil overall balance	-659.4	-731.6	-987.3	-998.5	-1052.4	-1077.6	-1125.1	-1094.0	-1028.6	-973.8
Funded by										
ESI	408.0	502.0	734.0	734.0	842.6	854.3	864.1	876.2	891.4	911.2
Withdrawals above ESI	104.0	309.0	321.0	321.0	0.0	0.0	0.0	0.0	0.0	0.0
Use of cash balance	148.0	-79.4	-67.6	-56.5	166.2	0.0	0.0	0.0	0.0	0.0
Borrowing	0.0	0.0	0.0	0.0	43.6	223.3	260.9	217.9	137.2	62.6
	(In percent of GDP)									
Revenue	62.6	64.9	66.5	69.1	59.7	63.6	60.9	63.4	64.2	60.6
Petroleum revenue	51.3	55.3	59.7	62.9	53.4	56.1	53.0	55.0	55.0	50.4
Oil/gas receipts	50.3	50.1	55.9	56.5	44.5	43.2	37.9	37.4	35.1	28.4
Interest	1.0	5.2	3.8	6.4	8.9	12.9	15.1	17.6	19.8	22.0
Taxes	1.3	1.2	1.4	1.6	1.7	2.1	2.4	2.8	3.7	4.4
Taxes on income, profits, and capital gains	0.4	0.4	0.5	0.6	0.7	0.9	1.0	1.2	1.3	1.5
Taxes on goods & services	0.7	0.6	0.6	0.8	0.9	1.1	1.2	1.4	2.2	2.6
Taxes on international trade & transactions	0.2	0.1	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.3
Grants	8.5	7.3	4.9	4.0	3.9	4.2	4.2	4.2	4.1	4.1
Other revenue	1.5	1.1	0.5	0.6	0.7	1.1	1.2	1.3	1.4	1.6
Expenditure	31.3	27.0	23.8	22.1	23.5	26.5	27.5	27.5	26.8	26.7
Current expenditure	12.0	12.0	8.8	10.7	10.8	11.1	10.4	10.4	10.2	10.2
Wages and salaries	2.6	2.2	1.9	2.1	2.1	2.1	2.0	2.0	1.9	1.9
Current transfers	2.9	4.0	2.5	3.4	3.1	3.2	3.0	3.0	2.9	2.9
Goods and services	6.5	5.8	4.4	5.2	5.7	5.8	5.4	5.4	5.3	5.3
Subsidies	1.2	0.7	0.8	1.7	1.7	1.8	1.6	1.5	1.3	1.3
Capital expenditure	10.8	7.6	10.1	7.3	8.8	11.2	12.9	12.9	12.5	12.4
Donor Project	8.5	7.3	4.9	4.0	3.9	4.2	4.2	4.2	4.1	4.1
Overall balance	31.3	37.9	42.7	47.0	36.2	37.1	33.4	35.9	37.4	33.9
Borrowing	0.0	0.0	0.0	0.0	0.7	3.9	4.5	3.8	2.3	1.1
Transfer to Petroleum Fund	35.8	36.1	41.5	46.1	39.7	41.1	37.9	39.7	39.8	34.9
	(In percent of non-oil GDP)									
Non-oil revenue	45.1	43.4	34.8	28.9	23.9	22.4	20.9	19.2	18.5	17.3
Expenditure	124.9	121.7	122.3	102.5	89.1	79.1	72.8	62.7	53.7	45.8
Non-oil overall balance	-79.8	-78.3	-87.5	-73.7	-65.2	-56.7	-51.8	-43.5	-35.1	-28.4
Funded by										
Borrowing	0.0	0.0	0.0	0.0	2.7	11.7	12.0	8.7	4.7	1.8
Memorandum items:										
Current expenditures (in percent of non-oil GDP)	47.7	54.2	45.0	49.7	40.9	33.0	27.5	23.7	20.4	17.4
Capital expenditures (in percent of non-oil GDP)	43.1	34.4	52.1	34.1	33.4	33.4	34.1	29.3	25.0	21.3
Rice operations (in millions of U.S. dollars):										
Sales	20.4	12.6	1.0	4.6	2.5	2.6	2.8	3.1	3.3	3.8
Purchases	31.8	35.0	2.0	9.4	5.1	5.3	5.8	6.2	6.6	7.7
Petroleum Fund balance (in millions of U.S. dollars)	5,377	6,897	9,303	11,768	14,199	16,528	18,709	20,983	23,313	25,364
Petroleum Fund balance (in percent of GDP)	163.0	163.6	160.5	186.8	231.8	291.5	325.6	366.3	397.9	432.0
Crude oil price (U.S. dollar per barrel, WEO)	61.8	79.0	104.0	105.0	104.5	101.3	95.3	91.2	88.5	86.7
Non-oil GDP at current prices (in millions of U.S. dollars)	827	934	1,128	1,355	1,615	1,901	2,171	2,513	2,928	3,425
GDP at current prices (in millions of U.S. dollars)	3,299	4,216	5,797	6,300	6,129	5,673	5,748	5,730	5,860	5,872

Sources: Timor-Leste authorities; and IMF staff estimates.

1/ This presentation of government operations as well as the related comments in the main text of the report do not follow the GFSM 2001 format. Accepted international standard, and IMF best practices use the GFSM 2001 for international comparability purposes. Deviations from GFSM 2001 are included in this presentation.

2/ Staff projections incorporate the Yellow Road budget envelope.