The Government of Timor-Leste has plans for saving and investing their petroleum revenue (described in Chapter Four). The aim of this chapter is to provide insights from research participants about those plans, to compare those insights and results to the Government’s plans, and to explore the research outcomes in the context of the state of Timor-Leste’s institutions (described in Chapter Three) and the challenges of managing natural resource wealth (described in Chapter Two). East Timorese Government officials make decisions that affect three aspects of petroleum revenue management. Those three aspects are explored in this chapter, and they are: the amount of revenue Timor-Leste has at its disposal (revenue potential); how much revenue is available in the future (sustaining natural resource wealth); and whether the revenue that is not spent is managed well (investing petroleum revenue).

This chapter uses some data (quotes) from the semi-structured interviews, but is primarily based on the results of Part Two of the Point*Wizard interviews (as explained in Chapter Five). This chapter explores the relative importance of six administrative choices in petroleum revenue management that cover the three aspects of petroleum revenue management. Figure 6.1 shows the relative importance of those six criteria (decisions), or petroleum revenue management decisions (as a mean percentage of participants’ relative preferences). This research enhances understanding of the choices available to, and made by, the decision-makers who manage Timor-Leste’s petroleum revenue by illuminating those decisions with the opinions of a wider range of East Timorese people. In particular, identification of the relative importance of those administrative choices provides a focus for the decision-makers.

### 6.1 Revenue potential

The first section of this chapter explores participants’ opinions about two decisions that may affect the amount of petroleum revenue that is available to the Government of Timor-Leste. The first is a decision about whether Timor-Leste funds its budget deficit by withdrawing from the Petroleum Fund or taking a loan from an international financial institution. The second decision is about the optimal time to exploit the Greater Sunrise petroleum field. These criteria (decisions) were included in the Point*Wizard interviews and presented to participants because the semi-structured interviews revealed that issues surrounding maritime boundaries and the exploitation of Greater Sunrise, and internationally financed loans, are important to research participants. Both decisions could bring Timor-Leste great wealth but political and other issues...
impact on these decisions. Thus, the basis on which such decisions are made is worthy of investigation.

![Figure 6.1 The relative importance of six petroleum revenue management criteria (%)](image)

### 6.1.1 Avoiding debt

Timor-Leste’s state budget currently has multiple funding sources, which were described in Chapters Three and Four. Timor-Leste generates only small amounts of domestic revenue. Some revenue is generated from autonomous agencies (such as airports and ports) and Timor-Leste receives some donor (bilateral and multilateral) funds. These funding sources, added together, do not meet Timor-Leste’s budgetary demands. Thus, Timor-Leste has resorted to exploitation of its natural resources as a source of state revenue. In theory, Timor-Leste has another option to fund its budget gap; to seek a loan from an international financial institution.

To date, Timor-Leste has not taken a loan from an international financial institution and, for the time-being, the Government of Timor-Leste has a policy of remaining debt-free. However, a loan from an international financial institution is an option for Timor-Leste. Such a loan may have conditions attached to it, meaning that Timor-Leste may lose some autonomy over its budget expenditure decision-making. However, if the interest earned on the Petroleum Fund is greater than the interest that must be paid to an international financial institution for a loan, it may make financial sense for Timor-Leste to take a loan.

A choice between these two options, as noted in Chapter Five, is not necessarily realistic. In reality there are more than two options and the choices are more complex. For example, the Government might choose to do both (take a loan for a particular project for example). Given that Bayu-Undan, the petroleum field currently being exploited, produces enough revenue to sustain Timor-Leste (forever, if it only withdraws a sustainable amount), such a plan (to take a loan whilst continuing to exploit) would make greater amounts of revenue available to Timor-
Leste than they need. The vices or virtues of this kind of borrowing will not be explored (as it is not the topic of this thesis), but opinions about such decisions will be. Presenting this choice to participants revealed their opinions about taking a loan from an international financial institution, and illustrated the importance of this decision and the issues surrounding it.

Figure 6.1 showed that the criterion (decision) of ‘How budget expenditure is financed’ was the most important of all the petroleum revenue management decisions to participants, having 21.2% of participants’ relative priority. Participants’ responses indicate this decision is the most important decision in terms of how Timor-Leste’s petroleum revenue is saved and invested. This criterion (decision) is 2.6 times more important than ‘which currency petroleum revenue is invested in’. ‘How budget expenditure is financed’ is also 1.4 times more important than ‘whether petroleum revenue is invested offshore’, and significantly more important (1.2 times) than ‘whether petroleum revenue is spent sustainably’.

The results of the ranking of the categories (options), and the comments that participants made during the interviews, indicate that participants’ opinions about ‘How budget expenditure is financed’ derive from their thoughts on whether Timor-Leste should take a loan from an international financial institution. The participants’ ranking, provided in Figure 6.2, of the categories (options) in this criterion (decision) show that, by far, the majority of participants (79%) preferred to finance budget expenditure by withdrawing revenue from the Petroleum Fund, rather than borrowing from an international financial institution. Given the clarity in category choice combined with the ranking of this criterion (decision) it is clear that avoiding debt is very important to participants overall.

Further analysis of the results shows a distinction between the preferences of participants with a decision-making role and those East Timorese external to the decision-making process. Nine out of ten East Timorese participants that do not have a decision-making role preferred to withdraw revenue from the Petroleum Fund. That is, 90% of East Timorese participants preferred to avoid taking a loan. Decision-makers were less adamant than the non decision-makers; only seven of eleven (64%) decision-makers preferred to finance the Budget by withdrawing from the Petroleum Fund.

Box 6.1 (on page 145) provides some of the comments made by participants, in either the semi-structured interviews or the Point*Wizard interviews, about the option of taking an internationally financed loan. The comments are divided into demographic groups which illustrate that the non decision-making East Timorese participants are passionate about this

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143 There were 24 participants in the sample, but the three foreign advisers who do not have a decision-making role were not included in these particular results.
issue, and determined to avoid taking a loan. Such loans are sometimes conditional and the participants’ comments show that they want to avoid a situation where they are beholden to anyone from ‘outside’ when making decisions. Xanana Gusmão suggested it was better that Timor-Leste be financially independent. Gusmão explained the frustration of needing donor assistance and being beholden to donor’s conditions as a result:

The tendency of the generosity of donors is a dilemma because it continues to force us to be dependent. Sometimes we think what donors give us is to comply with certain objectives… We feel like we are being restricted in our plans of action. Although there is a feeling [perception] that the Government is made by the Government, although with support, but in reality the money is not actually ours... The dependency of the future of our budget is a reality we can not avoid because at the moment donors don’t give us money for one thing, they divide it up for everything. This is a mechanism that makes their dependency [us dependent]... but if we have the money, we can say no because it is ours. We can decide where to locate funds. It is in that aspect [in this context] that I want to see the funds from oil and gas that will not restrict our own train of thought. (Xanana Gusmão, Citizen of Timor-Leste)

Some of the other comments express the same frustration, of being dependent on others for revenue, but having the desire for financial independence. This appears to be one of the motivating factors behind participants’ desire to avoid taking a loan from an international financial institution.
Box 6.1  Participants’ comments about the option of taking an internationally financed loan

<table>
<thead>
<tr>
<th>Quotes from East Timorese participants (non decision-makers)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Borrow money? No way! (Union Leader Male)</td>
</tr>
<tr>
<td>We can not take a loan. We can not borrow too much money from the bank. (District Health Worker Male)</td>
</tr>
<tr>
<td>Yes, I don't want to take a loan because corruption happens when there is a lot of money… I don't want to use money from debt. Will create problems in the future if we have to pay back. (Male District Community leader)</td>
</tr>
<tr>
<td>Don’t bring debt to your future generations if you want to develop sustainably. Problem is you pay interest. You have risk, but you won’t bring benefits to future generations. (Male NGO)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Quotes from foreign advisers</th>
</tr>
</thead>
<tbody>
<tr>
<td>If we developed Sunrise early and, at the same time, borrowed money for Government equity participation we would not have problems in repaying the loans. (Einar Risa, Commissioner and former Executive Director, TSDA)</td>
</tr>
<tr>
<td>Depends on the interest rate, but a long-term, low interest rate would make debt a profitable alternative. (Male Foreign adviser)</td>
</tr>
<tr>
<td>One thing I would do, because I am not constrained by East Timorese politics, is to decide whether to borrow money. If you want to build schools, etc. and you don’t have the money now then this is an option. Has this worked for other countries? Normally it fails because countries borrow in excess of their need. (Male Foreign adviser)</td>
</tr>
<tr>
<td>In Chad there is the perception that international agencies are behind the management model and this is an issue of sovereignty. The involvement of the World Bank has been questioned in this sense. (Male Foreign Adviser)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Quotes from East Timorese decision-makers</th>
</tr>
</thead>
<tbody>
<tr>
<td>The World Bank would like Timor Leste to save 100% and take a loan to fund their deficit. They argue that this would ensure prudent spending because we would have an obligation to pay the money back whereas revenue from oil did not require hard work or a savings plan to produce… There is no correlation between debt and poverty. I've changed my mind about that. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)</td>
</tr>
<tr>
<td>Borrowing is not that bad because it builds awareness about the need to manage money properly… Borrowing also has conditions… If you take from the Petroleum Fund you don't feel the same responsibility. Some people are scared, but the medicine is actually to borrow for exactly that reason. (Male Decision-maker)</td>
</tr>
<tr>
<td>If there is capacity to manage the loan then why not? (Male Decision-maker)</td>
</tr>
</tbody>
</table>

The option of financing budget expenditure with loans (whilst a Petroleum Fund with substantial amounts of revenue available exists) requires considerable investigation, which is not the purpose of this thesis. However, the results of this research clearly show (even with the opinions of the decision-makers included) that this is one of the most important issues in managing Timor-Leste’s petroleum revenue, and that, for the majority of participants, taking an internationally-financed loan is not a preferred option. By virtue of the fact that participants wanted to avoid debt, we can conclude that the Government’s plan to withdraw revenue from the Petroleum Fund to finance budget expenditure and their policy of remaining debt-free are welcomed by participants. The Government could change this policy, but it would do well to consider the relative importance of this decision, and the opinions of non-decision makers, particularly in regard to their desire for financial independence, as illustrated by the participants’ opinions in this research.
6.1.2 Strategies for exploitation

Another way by which Timor-Leste can increase its revenue potential is to exploit more natural resources. Timor-Leste’s petroleum revenue potential, in terms of where oil and gas are located, and plans for exploration were described in Chapter Three. Based on this information the East Timorese must decide when is the best time to permit exploitation of each of their petroleum fields. With respect to managing petroleum revenue these decisions depend on how much revenue is needed now, and in the future. There may be other reasons why petroleum fields would be exploited sooner or later. This section explores participants’ opinions about the decision of when to exploit petroleum fields using the Greater Sunrise field as an example.

The Greater Sunrise petroleum field is the most well known of Timor-Leste’s petroleum fields because it was central to the maritime boundary negotiations with Australia. The Greater Sunrise field is also the most prominent in terms of its potential revenue. The exploitation of Greater Sunrise was used as a criterion in the Point*Wizard interviews because of this prominence. Also, Greater Sunrise is a good example to use to learn what participants think about the decision of when to exploit because it has not yet been exploited. The participants were offered four options of when Greater Sunrise should be exploited. One of the options was ‘In 2010’. At the time the research was conducted, the earliest possible date that Greater Sunrise might be exploited was 2010. If Greater Sunrise were exploited in 2010 it would provide Timor-Leste with a large amount of revenue, therefore participants who preferred this option would effectively facilitate huge reserves of revenue for Timor-Leste. Another choice was to exploit Greater Sunrise ‘In 2025’. The Bayu-Undan petroleum field is expected to cease production by 2025, and thus income would also cease from this field in 2025. Choosing ‘In 2025’ indicates that the participant does not advocate an urgent need to generate further revenue, and their decision may be linked to revenue coming from Bayu-Undan being exhausted. ‘When maritime boundaries with Australia are resolved’ was another choice, but because no date had been set at the time this research was conducted, this choice was not able to include a certain date. Participants who chose this option were effectively prioritising the political aspects of the decision of when to exploit. The other option was ‘After 2055’ and participants who preferred this latest available date were effectively allowing future generations to decide when Greater Sunrise is exploited, and confirming their opinions that current generations have enough revenue now.

Figure 6.1 (on page 142) shows that the criterion (decision) of ‘when Greater Sunrise is exploited’ was second in importance, relative to other decisions about petroleum revenue management, with 19.6% of participants’ relative priority. This criterion (decision) was

144 The Greater Sunrise Agreement was ratified in March 2007, and ensures that the determination of maritime boundaries between Timor-Leste and Australia will not be resolved until, at least, 2057.
marginally less important than ‘how budget expenditure is financed’, thus illustrating that this
decision is also very important to participants. However, ranking of the categories (options) of
this criterion (decision) had a wider spread across participants than the results analysed in the
previous section (6.1.1). Figure 6.3 depicts the results of how participants ranked the categories
(options) of ‘when Greater Sunrise is exploited’. The figure shows that an almost equal number
of participants placed ‘In 2010 (as soon as possible)’ first as ‘When maritime boundaries with
Australia are resolved’ (48% compared with 45%). Thereafter most participants ranked ‘In 2025
(when Bayu-Undan is exhausted)’ second (48%) and few participants prioritised the ‘After
2055’ category (choice), thereby signifying a preference for Greater Sunrise revenue to be
available for expenditure by current generations. Although the first ranking of ‘In 2010’ was
slightly greater than ‘when maritime boundaries with Australia are resolved’, overall the
resolved maritime boundary option held a slightly higher ranking (that is, if first and second or
first, second and third rankings are added). Generally speaking, these rankings indicate the
majority of participants fall into two groups; those who believe maritime boundaries must be
resolved with Australia before exploitation occurs, and those who wish to see Greater Sunrise
exploited as soon as possible.

![Figure 6.3](image)

**Figure 6.3 Rankings of the categories (options) within the criterion (decision) of ‘When
Greater Sunrise is exploited’**

Of the participants who ranked ‘When maritime boundaries with Australia are resolved’ first,
most (60%) ranked ‘After 2055 (when future generations can decide)’ second. This may be
because these participants knew maritime boundaries would not be resolved in the near future
(the Greater Sunrise agreement was not finalised when this research was conducted), or that they did not see a need for revenue from Greater Sunrise to be used by current generations. Of the participants who wished to see Greater Sunrise exploited as soon as possible, 64% ranked ‘in 2025 (when Bayu-Undan is exhausted)’ second, which illustrates that their ranking prioritises the exploitation of Greater Sunrise, regardless of the resolution of maritime boundaries with Australia. These results emphasise a distinction participants’ opinions that is worthy of further analysis.

To clarify the issue, these results were analysed with the demographic details of participants in mind. This analysis revealed that eight of the ten (80%) East Timorese participants that have no role in decision-making ranked ‘When maritime boundaries are resolved with Australia’ first whilst only two of the eleven (18%) decision-makers did. This is a surprising distinction. Most of the East Timorese participants who did not have a decision-making role with respect to petroleum revenue management felt that ‘when Greater Sunrise is exploited’ is inextricably linked to resolving the issue of Timor-Leste’s sovereign rights to a maritime boundary. This result contrasted markedly with the number of decision-makers who ranked ‘when maritime boundaries are resolved with Australia’ first. This contrast is grave, given that the legislative decision to proceed with exploitation of Greater Sunrise has been made since the research was completed, and precedes the resolution of maritime boundaries between Timor-Leste and Australia. The decision-makers have proceeded with a plan that contradicts the opinions of the majority of East Timorese participants in this research.

The comments that participants made during both the semi-structured interviews and the Point*Wizard interviews when considering this issue reveal further context to these findings. Some of those comments are presented in Box 6.2. Participants who prioritised the category (choice) of resolving maritime boundaries before exploitation made comments such as ‘of course’ and ‘maritime boundaries are very [emphasised] important’. These participants also made their choices quickly and boldly implying that they were very clear and strongly adamant that the resolution of maritime boundaries was a priority. The comments of East Timorese without a decision-making role in Box 6.2 indicate the passion of those who prioritise the resolution of maritime boundaries over earlier exploitation of Greater Sunrise. This passion is reminiscent of the passion and determination with which the East Timorese fought for, and overwhelmingly won, Timor-Leste’s independence. These and other comments are evidence that these participants assumed resolution of maritime boundaries might result in Timor-Leste having a larger share of the revenue from the Greater Sunrise field. Thus, it is apparent that participants who preferred to resolve maritime boundaries, rather than exploit Greater Sunrise as soon as possible, came to that decision with financial independence as their goal. However, one

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145 The decision to proceed with exploitation of Greater Sunrise is also dependent on the operating company, Woodside Petroleum Company.
of the two decision-makers that prioritised the resolution of maritime boundaries explained Timor-Leste was not reliant on Greater Sunrise; ‘we have other resources onshore and offshore’ (Male Decision-maker).

<table>
<thead>
<tr>
<th>Box 6.2</th>
<th>Participants’ comments about the option of ‘When to exploit the Greater Sunrise petroleum field’</th>
</tr>
</thead>
</table>

**Quotes from East Timorese participants (non decision-makers)**

My focus is on the determination of maritime boundaries. (Male NGO)

If I were Xanana or Mari Alkatiri I would not exploit it [Greater Sunrise] yet. First, negotiate with Australia to define maritime boundaries. Second, repair our technicians, East Timorese. After we define the maritime boundaries we can start with exploitation. (Fernando ‘Lasama’ de Araujo, Partido Democrático)

They haven’t resolved the maritime boundaries so this is the biggest problem… I think the Australian Government is richer and also smart so they know what belongs to East Timor. (Male District Community Leader)

We need to talk about boundaries first. Our government is too rushed. (Young Male District Veteran)

The second thing is that we need to build a good relationship with Australia to decide the border for the Timor Gap. Before that we are dreaming and 2020 will not come [as we have planned it]. (Male Decision-maker)

**Quotes from decision-makers (East Timorese and foreign) prioritising earlier exploitation of Greater Sunrise**

Greater Sunrise is the basis for a national oil industry… We don’t know what will happen in the future… Maybe in 2055 no one wants to buy gas. (Einar Risa, Commissioner and former Executive Director, TSDA)

There is a window of opportunity to develop Greater Sunrise that is at a critical time in our development stage… The sustainable wealth will be higher if Greater Sunrise comes on line. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)

The sooner you get it the sooner it earns interest. (Male Foreign Adviser)

**Quotes from participants regarding delayed exploitation of Greater Sunrise**

If we start talking about Greater Sunrise we can definitely last 15 years [before exploitation]. Mentalities [of corruption] will fall and retire. The new train of thought. (Xanana Gusmão, Citizen of Timor-Leste)

If it were up to me I would say 10 years from now. Because I need to build the capacity of this country. If we had US$1 billion it could be a disaster for this country. I say ‘could’ not would. (Mari Alkatiri, Former Prime Minister)

If you look at the current capacity of the JPDA including Greater Sunrise within the next 30-40 years we will be self-reliant because in the meantime you have infrastructure development; more diverse industry and more human resources and less reliance on petroleum. So the exploitation of Greater Sunrise is not paramount, it will not determine our survival. (Male Decision-maker)

Exploit Greater Sunrise sooner is important because it is good for East Timorese people so the Government can prepare work for many people and the money they can take from oil. (Young Female)

In contrast, the comments of the decision-makers who prioritise the early exploitation of Greater Sunrise were made based on, or cognisant of, higher economic goals. Participants who suggested Greater Sunrise should be exploited sooner than later included Jose Teixeira (currently Minister of Natural Resources, Minerals and Energy Policy), Einar Risa (the Commissioner and former Executive Director, TSDA) and at least one other foreign adviser. There was also one East Timorese non-decision-maker who expected benefits from the early exploitation of Greater Sunrise. The reasons they prioritise exploitation as soon as possible
revolve around the opportunities that the resulting revenue may present. Such opportunities include establishing a national oil industry, using the revenue to create jobs, and wealth creation through investment in infrastructure and financial investment. Industry market constraints were also given as reasons to prioritise exploitation of Greater Sunrise. None of the participants suggested exploiting Greater Sunrise was necessary in the event that Bayu-Undan supply was interrupted (due to an accident for example). But, more recently TSDA officials suggested that if there was a major shutdown of the facilities which would result in a long term reduction to Bayu-Undan revenue this would be a supporting reason for exploiting Greater Sunrise (Borges and Lobato 2006).

Another factor in the decision of when to exploit Greater Sunrise, expressed by participants, was whether the institutions are strong enough to utilise the revenue well. Some participants recognised there were benefits of delaying exploitation of Greater Sunrise. In the field interviews, both Xanana Gusmão and Mari Alkatiri explained that Greater Sunrise should be exploited when the State has the capacity to manage the revenue that will come from it. Both mentioned corruption as a reason to delay exploitation of Greater Sunrise. Some of their comments are highlighted in Box 6.2. Having a plan in place, as well as the capacity, was also seen as necessary before the most effective use could be made of the benefits from Greater Sunrise. Reasons to delay included hopes that industry would be more diverse, and infrastructure and human resources would develop in the meantime. Revenue from Greater Sunrise could only be put to good use if the capacity to implement the kinds of projects suggested earlier (e.g. establishing a national oil industry) exist. Further, if other industries developed, revenue from petroleum exploitation would not be so crucial to the economy. For these reasons, some participants believed it was not necessary, or more beneficial not, to exploit Greater Sunrise at this point.

In summary, participant responses to the question of ‘when to exploit Greater Sunrise’ did not appear to be based on the desire to increase revenue potential alone. Rather, their reasons for when they thought it best to exploit Greater Sunrise revolved around the political (i.e. resolution of maritime boundaries), the economic (i.e. wanting to make use of the revenue as soon as possible) and the institutional (i.e. needing to build capacity to make the best use of the revenue). The opinions of decision-makers and East Timorese with no decision-making role contrast and, for the time-being, the challenge of achieving both their goals has been won by the decision-makers. That is, the decision-makers have decided that the goal of true independence in the form of resolving Timor-Leste’s sovereign rights to a maritime boundary should be deferred, and the need for revenue to develop the economy has been prioritised.

The Greater Sunrise Agreement was ratified in March 2007 and although it delays the resolution of maritime boundaries between Timor-Leste and Australia for 50 years, the Agreement also guarantees Timor-Leste 50% of the revenue generated by Greater Sunrise. This half-half
agreement is a much better deal for Timor-Leste than the agreement between Australia and Indonesia would have generated. Under that agreement, Timor-Leste would receive only 10% of the revenue generated by Greater Sunrise\textsuperscript{146}. So, in terms of potential revenue, the Greater Sunrise Agreement generates a significantly greater amount of revenue for Timor-Leste than the original agreement ‘bequeathed’ from Indonesia would have. This change in the arrangement indicates that the Government of Timor-Leste’s decision-makers have successfully negotiated a deal which better represents the desire of the participants for financial independence. Despite that, the participant’s desire to resolve their sovereign rights to a maritime boundary has not been met.

This section explored two decisions that may impact on the amount of revenue Timor-Leste has available to it. The results of the research revealed that participants based their decisions, about how the State’s budget deficit should be met and when the Greater Sunrise petroleum field should be exploited, on political, economic and institutional factors. Timor-Leste’s current financial position in terms of meetings its budget needs did not appear to factor in participants’ decision-making. There appeared to be primarily two motivating factors for participants’ decisions; a desire for independence in Timor-Leste’s decision-making and a desire for more revenue to create economic development. Both are worthy higher goals and made in, what participants believe to be, Timor-Leste’s best interest. One group of participants favour the opportunity for Timor-Leste to make its own decisions with no interference from other countries or outside institutions. The majority of this group are East Timorese with no decision-making role. Participants with a decision-making role are open to solutions that bring Timor-Leste economic development, but may trade-off Timor-Leste’s autonomy in decision-making along the way. Thus, there is a gap between the priorities of decision-makers and the other participants. The crisis in 2006 highlighted that the opinions of many East Timorese with no power to make decisions differ from those within Government. These gaps are symptomatic of the problem of a lack of social capital between government and civil society, which Chapter Two showed is a curse that may contribute to poor petroleum revenue management. The issue of maritime boundaries has been deferred, for the time being, but the option of taking a loan from an international financial institution will remain and continue to be debated within, and between, government and civil society.

\textsuperscript{146} Greater Sunrise sits 20\% inside the area that was known as Zone of Cooperation A (now the JPDA) under the agreement between Indonesia and Australia. Indonesia and Australia shared petroleum revenue from the Zone of Cooperation A equally. Thus, if such an agreement were in place today, Timor-Leste would receive 50\% of 20\% (10\%) of the revenue from Greater Sunrise.
6.2 Sustaining natural resource wealth

This section explores participants’ opinions about the sustainable management of petroleum revenue. Sustainability means different things to different people, as explained in Chapter One. Participants offered their opinions about sustainable petroleum revenue management, and some of their comments are presented in Box 6.3. They expressed concern that petroleum revenue can be wasted (with only short-term benefit) and appeared to acknowledge a responsibility to ensure that the benefits of the exploitation of petroleum resources are shared with future generations (a sense of stewardship). In this regard there is commonality amongst the sentiments expressed by members of NGOs, opposition leaders and government participants. Overall, the views of participants in this research support the idea that sustainable management of petroleum revenue can be achieved in two ways, and that they are not mutually exclusive.

Box 6.3 Participants’ comments about sustainable petroleum revenue management

Ensure [that] what you invest in is something that is going to reproduce something else, that it will manage itself adequately, will achieve efficiency, and achieve returns. Investing in something that is self-managing, self-funding, self-producing. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)

You can invest the money and that investment can produce money. Not to buy weapons, cars, computers. We should invest in ports, airports and roads. (Fernando ‘Lasama’ de Araujo, Partido Democrático)

Sustainability is not only about the means to have money to expend all the time, but about the impact of the money we spend being long term. For example, if you use the money to build a hospital (infrastructure), this has longer-term benefits. The Government must bring benefits to future generations. (Male NGO)

The first thing I need to say is these resources belong to future generations. We are borrowing from future generations. Based on that principle all of the revenue should be preserved. We may use some, but this is the basic principle underlying the way we manage the revenue. We need to analyse which activity in development will have long term impact for future generations. Which sector can replace the petroleum sector when the oil runs out? Health and Education are the priorities... These will have a very strong impact on future generations. (Male NGO)

First, petroleum revenue can be spent on projects or items that, in turn, create an amount of revenue that is either equal to, or greater than the revenue spent (i.e. investing petroleum revenue by spending it). That option, of spending petroleum revenue to achieve sustainable development, is discussed in the next chapter. The second option is to ensure that the amount spent (the amount withdrawn from the Petroleum Fund) is sustainable. When the same amount of revenue is spent each year, expenditure is sustainable. The Government of Timor-Leste has institutionalised this option by providing the decision-makers with the knowledge of what that amount is; Estimated Sustainable Income (ESI). The concept of ESI was explained in Chapter Four and the aim of the following section is to explore participants’ opinions about whether an amount equal to, more than, or less than, the value of ESI should be withdrawn from the Petroleum Fund each year. Whichever way sustainable petroleum revenue management is
achieved, this means that future generations will receive benefits from the petroleum revenue that are similar to the benefits experienced by current generations. If revenue expenditure is unsustainable or unbalanced (e.g. more spent now, less spent later, or vice versa) either the current or the future generation will benefit over the other. Thus, this section also explores what participants said about future generations, and the concept of saving.

What is relevant to this thesis is that the Constitution essentially reflects a concept of sustainability that is similar to some participants’ view of sustainability (expressed with respect to petroleum revenue management). However, the participants’ comments highlight that sustainable petroleum resource management and sustainable petroleum revenue management are two different things. Participants did not make comments about sustainable petroleum resource management, except to say that future generations had a right to benefit from the resources that they were exploiting. Rather, their primary concern is that the management of petroleum revenue is sustainable.

This distinction is important because if, for argument’s sake, a decision was made to preserve all petroleum resources in their pristine entirety for use by future generations, petroleum resource management might be said to be sustainable, but petroleum revenue management would not be. In this scenario no petroleum revenue would be spent on current generations and they would not benefit from Timor-Leste’s petroleum resources. However, the option of preserving some petroleum resources for future generations has not, to my knowledge, received debate in the East Timorese community. For example, Bayu-Undan is currently being exploited and providing petroleum revenue for expenditure by current generations. If that revenue is enough to meet current demand one could argue that the exploitation of Greater Sunrise, and other petroleum fields, is not necessary at this point and that these fields should be preserved for use by future generations. This suggestion would appear to meet the terms of sustainable natural resource management as expressed in the Constitution. Preserving some petroleum resources for exploitation by future generations may also have benefits in terms of sustainable petroleum revenue management because exploiting all the currently known petroleum resources in a scenario in which petroleum revenue was not managed well (e.g. wasted) may result in no benefits for future generations. For the time being, we shall concern ourselves with participants’ view of sustainability based on the assumption that petroleum resources are exploited and sustainable petroleum revenue management is the focus.

6.2.1 Spending a sustainable amount

This section explores participants’ opinions about whether petroleum revenue management is sustainable by reviewing the results of the relative importance of the criterion (decision) of ‘whether the amount of petroleum revenue spent is sustainable’, and the ranking of its categories (options). This criterion (decision) has three annual expenditure amounts as its
categories (options); less than US$100 million, (equal to) US$100 million, and greater than US$100 million. The value of ESI at the time of the research was US$100 million so participants were effectively asked to choose whether the amount of expenditure should be less than ESI (thereby increasing the value of the Petroleum Fund over time), equal to ESI (revenue expenditure is sustainable), or greater than ESI (the balance of the Petroleum Fund would eventually decline to nothing). In deciding how much revenue is spent now participants are, in effect, choosing whether revenue should benefit current or future generations, or both.

The relative importance of ‘whether the amount of petroleum revenue spent is sustainable’ expresses how important sustainable expenditure (in terms of how much revenue is spent) is to participants. Figure 6.1, on page 142, shows that this criterion (decision) has a relative importance of 17%, which means it is 2.1 times as important as ‘which currency petroleum revenue is invested in’. However, ‘whether the amount of petroleum revenue spent is sustainable’ is much less important to participants than ‘how budget expenditure is financed’ and also less important than ‘when Greater Sunrise is exploited’, and ‘the level of Petroleum Fund investment risk’. This result is not surprising, given that participants ranked the category (choice) of ‘After 2055 (when future generations can decide)’ last, in terms of ‘when greater Sunrise is exploited’. The results of this research indicate that, more often than not, when given a choice, participants chose against spending petroleum revenue sustainably. That is, when faced with a trade-off, participants are less concerned about revenue being available to future generations, than meeting their own needs, which is also not surprising given the level of poverty in Timor-Leste today.

However, when participants were asked about spending petroleum revenue sustainably, without being asked to trade-off this issue, it was important. This is illustrated by the results of the participants’ rankings of the categories (options) within this criterion (decision), which very clearly indicate a preference that expenditure should be less than ESI, which means revenue would be available to future generations. Figure 6.4 depicts the participants’ rankings of the categories (options) within the criterion (decision) of ‘whether the amount of petroleum revenue spent is sustainable’. 78% of participants chose ‘less than US$100 million’ (less than ESI) as the amount they preferred to spend each year. This means that, by far, the majority of participants’ choice was to save more for future generations than they themselves had to spend. In picking a withdrawal amount that was less than ESI they were in fact opting for a model in which the value of the Petroleum Fund would continue to grow. Further, 22% of participants ranked ‘US$100 million’ (equal to ESI) second, which means that not one participant ranked ‘more than US$100 million’ (more than ESI) first. These results suggest that the participants would be against a decision by the Parliament to withdraw greater than the value of ESI. One participant suggested spending more than US$100 million would be bad for Timor-Leste;
‘Morally is it bad for the nation. Once you learn that you have it and if you run out it has a psychological effect. At least the elite understand these things’ (Male Decision-maker).

As explained in Chapter Four, the Government of Timor-Leste does not have a policy to ensure that the amount withdrawn from the Petroleum Fund is sustainable, rather they provide the Parliament, which makes the decision of how much to withdraw, with the value of ESI to aid them in their decision-making. If Parliament decided to withdraw greater than the value of ESI, they could do that within the law. Regardless of the level of support, some of the participants indicated they are against the idea of a rule that governs the amount withdrawn from the Petroleum Fund each year. Jose Teixeira explained why rules may constrain fiscal management:

It is important to develop the capacity of people to undertake responsible fiscal management and Parliament should not be bound by what they can and can not spend. It’s not appropriate [to have a withdrawal rule] because the Parliament may act responsibly by spending more one year, and less the next. One-off expenditures can be re-couped in other years through other budgetary savings. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)

Figure 6.4  Rankings of the categories (options) within the criterion (decision) of ‘Whether the amount of petroleum revenue spent is sustainable’

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147 The value of ESI at the time of the research was US$100 million per annum, thus the three categories (options) are effectively less than ESI, ESI, or more than ESI.
Teixeira’s explanation highlights a core challenge for the East Timorese government. Whilst institutional capacity remains weak, the temptation exists to create institutional mechanisms to prevent poor decisions being made. However, having such mechanisms in place might prevent better decisions being made, once capacity is built. Regardless of which model is followed, mechanisms can be changed (either legally or illegally depending on the strength of the institutions of the day). A foreign adviser explained that ‘rules would not prevent the Government from withdrawing funds under pressure as illustrated in other countries.’ To date, Parliament has not made any withdrawals from the Petroleum Fund, but they have agreed that an amount, less than ESI, will be withdrawn from the Petroleum Fund in this financial year. The impact of the decision to use ESI as a guide, rather than a rule, will not be felt until such time as Parliament decides to withdraw an amount greater than the value of ESI. Should such a decision to withdraw an amount that is greater than the value of ESI be taken, this would signify that, either the decision-makers had plans to invest petroleum revenue by spending it (and thus generate benefits for future generations in this way), or they had less regard for future generations’ needs than their own. The following section explores whether future generations’ needs were a factor in the participants’ responses.

6.2.2 Saving for the grandchildren

At the centre of the problem of managing petroleum revenue is the fact that petroleum resources are finite. Once the petroleum resources are exhausted, no more revenue (from the resource itself) will be received. The amount of resources Timor-Leste currently has at its disposal (i.e. the Bayu-Undan petroleum field) would, if managed wisely, produce enough revenue to provide for both current and future generation’s needs. However, if Timor-Leste’s current generation exhausted the resources, and the associated revenue, and that revenue was not used to generate sustainable economic development, Timor-Leste’s future generations would be disadvantaged. This section reveals what participants said, during both the semi-structured and the Point*Wizard interviews, about the concept of saving petroleum revenue, and how future generations factored in their decisions about managing petroleum revenue. The quotes in Box 6.4 indicate that some participants are mindful of the needs of future generations in making decisions about how much petroleum revenue should be saved. Several participants specifically mentioned that (at least some) revenue should be saved for future generations, and some participants suggested that petroleum resources actually belong to future generations.

The comments indicate that these East Timorese understand the concept of saving revenue. Participants gave examples that they, if not others, know how to save money. For example, one participant talked about working and saving money to go to Bali, Indonesia. Another mentioned that people sometimes saved money outside of the country (in Indonesia). A recent newsletter of Timor-Leste’s Central Bank reports that the total private sector commercial bank deposits, as at
June 2006, is over US$1 billion (BPA 2006). Thus there is, at least, a small elite group who earns enough money to satisfy their immediate needs and save some. However, some participants made comments, examples of which are presented in Box 6.5, that suggest that some East Timorese may not understand why some petroleum revenue should be saved for future generations. However, some participants indicated that the problem is not so much whether East Timorese people understand the need to save, but whether they should save (or save as much), if current generations’ needs are not being met.

**Box 6.4 Participants’ comments acknowledging regard for future generations**

The reason we can’t spend it is because it belongs to people in the future. We have a responsibility to future generations. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)

These resources belong to future generations. We are borrowing from future generations… The Government must bring benefits to future generations… Don’t bring debt to your future generations. (Male NGO)

Before no one cared about money because it came from elsewhere. Now we are responsible for our own funds. We must try not always to depend on donors. We need to try to work hard. To do something for ourselves. Take our own decisions. Not under pressure from donors. These are the objectives of the Government now. We are preparing everything for future generations. (Mariano Lopez da Cruz, Former Inspector General)

We should use half for income generation and half to be saved for future generations. (Maria Paixão, Partido Social Democrata)

We will save some revenue and we will use some. The Government wants to save some money, but the opposition wants to spend it. Personally, [joking] I would like to spend it all now so I can do lots of things and the people can see what I have done., but this is not what we are going to do. It needs to be sustainable. (Mari Alkatri, Former Prime Minister)

We should save some of it for the future. (Male Decision-Maker)

**Box 6.5 Participants’ comments about people’s understanding of the concept of saving**

Some don’t understand the need for a fund (to save). Some think we should spend it. They think it is better to create a multiplier effect by spending it, but they don’t understand Dutch disease. Ordinary people just say ‘feed us’. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)

If they have a lot of money, they don’t know how to save/invest. [They spend it on] Cock fighting [which results in] domestic violence… Many people take loans to buy taxi. There are too many, [they] can’t pay [the money] back, then the bank takes their land. (Female NGO)

Many East Timorese live in poverty and are unable to earn enough income to meet their current needs, let alone save money. The frustration of many East Timorese, about why so many of their people live in poverty whilst Timor-Leste’s petroleum revenue is saved, is commonly expressed, and most evidently during the recent crisis and since that time. In April 2007,
Xanana Gusmão is reported to have declared that he would ‘unlock’ the revenue from the Petroleum Fund and put it to use:

Gusmão has promised he will unlock hundreds of millions of dollars in oil revenue held in a New York escrow bank account if he is elected Prime Minister… ‘Democracy will not work if the people are hungry. We have so much money in an account in New York, while here in Timor people are struggling and living in misery.’ (Fitzpatrick 2007:8)

In the semi-structured interviews, Gusmão described what he thought would happen if too much revenue was saved:

If we think only of hoarding it [the petroleum revenue] we will maintain the traditional life where people have food – pigs, chooks, goats, cows, buffaloes – they can not afford to seek medical treatment, the person dies, they kill all the animals at the burial to feed the people that come to cry. The children have no money left because they killed all the animals and they can’t afford to go to school. This is not a good notion of richness. (Xanana Gusmão, Citizen of Timor-Leste)

Both of Gusmão’s comments suggest that he believes meeting the needs of generations now is more important than saving petroleum revenue for future generations. The comments of others express this idea in more subtle ways.

Participants’ responses to the question of ‘how much petroleum revenue should be saved?’ indicated that their primary concern is to satisfy current generations’ needs, because their responses begin by indicating how much should be spent (not saved). That is, their first concern is to satisfy their generation’s needs, and how much petroleum revenue should be saved is a corollary of that (i.e. what was left after the spending decisions had been made). For example, their responses included ‘the proportion of what is spent needs to be determined’ and ‘the percentage [of what will be spent] will depend on the necessity from each sector’. A young bureaucrat explained his vision, for how much to save, as follows:

First, I would look at the amount of revenue and say ‘is it more than what we need to run the institutions of state; to strengthen them and build their capacity?’ Then we need enough to provide the basic services including health and education. Second, if there is any left then we must divide this into two. The first half is for future generations (savings). The other half is used for potential distribution for society; to provide services for them. For example, veterans who are unhappy with the services provided by government, we can provide loans for them through commercial banks. (Male Decision-Maker)

In contrast, the Government of Timor-Leste has designed the Petroleum Fund Law such that 100% of petroleum revenue is saved automatically (initially). Under the Law, the decision to save petroleum revenue comes before decisions about spending it. The amount of petroleum revenue saved and the amount spent are complementary. That is, a decision about one decides the value of the other, but the decision that is made first signifies the priorities of the decision-maker. By saving 100%, and using ESI as a guide for how much to withdraw, the Government
of Timor-Leste signifies that future generations’ needs are a priority, if not equally important to current generations’ needs. Whilst participants who advocate determining current spending needs as a priority, with no framework for saving, signify that future generations will receive whatever is left.

Some participants did propose a framework for saving for future generations. They either suggested a percentage of revenue should be saved, or that only the interest on the Petroleum Fund should be spent (and the capital should be saved). Some of their responses are presented in Box 6.6. The calculation of the portion, which participants suggested should be spent, was not explained, and their responses indicated the figures were arbitrary. Further, not one of the participants distinguished whether the percentage was of current savings or projected total savings, each of which would provide vastly different outcomes. The other option, of preserving the Petroleum Fund’s capital (petroleum revenue receipts) and spending only the interest earned on the Fund, assumes that the investment risk is low, and that the capital is indeed preserved. However, given the current value of the Petroleum Fund, the investment return would not be sufficient to cover the Budget expenditure requirements at this time. Such a proposal would require another source of income to fund the Government budget, in the short-term at least (e.g. to request further donor assistance or take a loan from an international financial institution).

The Government’s plan, of using the value of ESI to guide withdrawals from the Petroleum Fund, attempts to provide some balance between the amount of revenue used by current and future generations. But, realistically, exact balance of spending between current and future generations is impossible, for many reasons. For example, petroleum revenue projections

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148 Kadhim Al-Eyd (participating as Resident Representative of the IMF) proposed that this option (of spending just the interest) could work in the future. Al-Eyd said ‘It is proposed by the World Bank, there be a savings plan such that a specific amount will be set aside. So that in 2025 you will have 67% of the revenue saved and you will then be able to live off that interest.’ (Kadhim Al-Eyd, former Resident Representative, IMF Timor-Leste)

149 Partido Democratico is a political party and Fernando ‘Lasama’ de Araujo is its President.
vary and thus so would the value of ESI, and thus the amount of petroleum revenue available to current and future generations. Further, the value of spending revenue on health and education now, and the benefits that will bring to future generations can not be quantified in a way that is comparable with saving an amount of revenue today. Participants recognised that working out what is the best proportion of saving versus spending will be difficult. One foreign adviser pointed out the simple logic: ‘whatever amount you save for the future means you will constrain current generation spending’. At the same time, there will be no future generations if the current generations’ most basic needs are not met.

Whether petroleum revenue is saved, or spent, participants noted it must be used wisely, not wasted, and that when revenue is spent, it should benefit future generations, as well as current, where possible. In this regard, participants emphasised spending on some budget sectors because of the benefit they would bring to future generations (and this will be discussed further in the next chapter). For example, spending additional revenue on ‘Youth and Sport’ was considered an investment in future generations. Participants made comments, such as ‘Youth are the future generation. Youth are the future of East Timor’ (Female NGO). In this way, youth were considered symbolic of, or an example of, the ‘future generation’ and an example of how spending today may benefit future generations.

This section explored participants’ opinions about the concept of saving petroleum revenue and the place of future generations as decisions about how much petroleum revenue is saved and spent are made. The results indicate that, in theory, participants favour the sustainable management of petroleum revenue and that revenue should be saved for expenditure by future generations. However, the research also suggests that if a conflict of interest between current and future generations’ needs exists, then the research participants might favour their own needs.

Timor-Leste’s constitution only refers to future generations within the context of protecting the environment, and although the Petroleum Fund Law defines ESI, it is only a guide for withdrawals. Thus, the Government of Timor-Leste does not have a policy that would ensure that petroleum revenue is saved for future generations. Based on this lack of a policy, or rule,

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150 Participants expressed a range of expectations about how much revenue Timor-Leste would receive from exploitation of their petroleum resources. Most participants acknowledged that Timor’s petroleum resources would one day be exhausted, but one participant claimed projections for revenue would be much greater than anticipated (because of current oil prices and new geological evidence). Some participants mentioned revenue from Greater Sunrise, but Einar Risa (Commissioner and former Executive Director, Timor Sea Designated Authority) explained it was impossible to estimate how much the Greater Sunrise field would produce because the development plan has not been sighted and it will depend on how much customers, who have not yet been identified, will pay. Further Einar Risa said, ‘...it is difficult to provide these figures [revenue projections] to the public as they do not understand how they can change so much. Even the World Bank and the IMF have trouble understanding why they change so much.’

151 The concept of youth as symbolic of future generations has the potential to limit the vision of the future to a very short time frame. If the youth of Timor-Leste are the future, one could have the impression that petroleum revenue can be spent ‘on future generations’ by spending it now and not saving for the generations to come. This was not, however, directly expressed by participants.
and given the preferences of the participants in this research, until the needs of the current
generation are met, ensuring that petroleum revenue is available to future generations will be a
challenge for Timor-Leste.

6.3 Investing petroleum revenue

Institutionalising mechanisms that ensure some petroleum revenue is saved for future
generations is wise, but establishing a Petroleum Fund and other mechanisms will not
necessarily prevent natural resource wealth waste. Nauru’s natural resource wealth was wasted,
not because it was spent unwisely, but because the investment of its revenue was unwise.
Nauru’s experience illustrates that the act of establishing a natural resource fund is not
necessarily the solution to avoiding the resource curse. If natural resource revenue is not
invested wisely, the revenue will be wasted before there is a chance to spend it. This section
explores decisions about how Timor-Leste’s petroleum revenue is invested financially (as
opposed to being invested through spending revenue, which will be discussed in Chapter
Seven). Participants’ opinions about three aspects of petroleum revenue investment in Timor-
Leste are discussed; the level of investment risk, where revenue is invested, and in what
currency investments are made.

Figure 6.1, on page 142, illustrates that the criterion (decision) ‘level of Petroleum Fund
investment risk’ is quite important, relative to the other petroleum revenue management criteria
(decisions), with 19.1% of participants’ relative priority. This criterion (decision) is almost
equally important to participants as ‘when Greater Sunrise is exploited’, and only slightly less
important than ‘how budget expenditure is financed’. Thus, according to the participants, ‘level
of Petroleum Fund investment risk’ is one of the three most important decisions in terms of
Timor-Leste’s petroleum revenue management. In contrast, the two other decisions, about how
petroleum revenue is invested, are relatively less important to participants. ‘Whether petroleum
revenue is invested offshore’ had 14.9% of participants’ relative priority, whilst ‘which currency
petroleum revenue is invested in’ was much less important, and had only 8.2% of participants’
relative priority.

6.3.1 Level of investment risk

‘Level of Petroleum Fund investment risk’ was the third most important of the six petroleum
revenue management criteria (decisions) and shared 19.1% of participant’s priority (see Figure
6.1 on page 142). The categories (options) within this criterion (decision) distinguished three
different levels of risk by denoting a split between the portion of the Petroleum Fund invested
conservatively (risk-averse investment) and the portion invested in ‘a wider range of
instruments’ (indicating a higher investment risk). This criterion (decision) was included in the
Point*Wizard research to elicit whether participants had a preference for higher or lower risk investment. The categories (options) were ‘100% invested conservatively’, ‘90% invested conservatively, and 10% in a wider range of instruments’, and ‘More than 10% invested in a wider range of instruments’. The Petroleum Fund Law stipulates that, in the first five years, a minimum of 90% of the Petroleum Fund shall be invested conservatively, whilst a maximum of 10% of the Petroleum Fund may be invested in instruments of greater risk (represented by the second category, above).

Figure 6.5 illustrates the rankings of the categories (options) of ‘level of Petroleum Fund investment risk’ preferred by participants. The majority of participants (67%) preferred ‘90% invested conservatively, and 10% in a wider range of instruments’, which reflects the level of investment risk that the Law defines. The Petroleum Fund Law had already been drafted when this research took place. Further, the consultation process had concluded and the East Timorese had had the opportunity to hear of the plans for investing the Petroleum Fund. Participants favoured the approach of investing 100% conservatively, as a second option. Increasing the risk (to more than 10% of the Petroleum Fund invested in a wider range of instruments) was least favoured. The results indicate that participants agree with the level of risk implemented through the Petroleum Fund Law, which is relatively conservative.
The reason the Petroleum Fund Law provides for 10% of the Petroleum Fund to be invested in a wider range of instruments is to limit the risk whilst capacity to manage investments in a wider range of instruments grows. A foreign adviser explained that:

The reason the 90-10 split was proposed was to build institutional capacity in the Central Bank, train people to invest. Further, on average a 90% - 10% split fluctuates less, so they balance each other out. Usually, if one is not doing well the other will be. (Male Foreign Adviser)

The Government and the Central Bank have not yet taken the option to invest any of the Petroleum Fund in a wider range of instruments. The Petroleum Fund is currently invested entirely in US Federal Bonds. As the capacity of the staff of the Central Bank managing the Petroleum Fund grows and investments in other instruments are introduced, the return on investments may increase and is likely to vary more than the relatively constant return on US Federal bonds. This approach is conservative and a desire for conservative financial management is reflected in the results. 83% of participants ranked ‘More than 10% in a wider range of instruments’ last. The comments of the participants also indicate a desire to avoid risk, and a conservative approach to finance management. Some of the comments are presented in Box 6.7.

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<tr>
<th>Box 6.7</th>
<th>Participants’ comments about the level of investment risk</th>
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<tr>
<td>I’m not a gambling person, I want to avoid risk. (Young Female)</td>
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<tr>
<td>I prefer investment [in bonds] as shares are risky. You can lose money. (Maria Paixão, Partido Social Democrata)</td>
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</tr>
<tr>
<td>We will need safe returns on investments in bonds. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)</td>
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Given the low-risk investment strategy currently in place, there has been little debate about investment of the Petroleum Fund to date. Civil society has the opportunity to monitor the Petroleum Fund’s investments via the quarterly reports of the Central Bank. The quarterly reports have, so far, been informative in explaining how the Petroleum Fund investments perform (for example, why the return was less over the period when Hurricane Katrina hit the US), but as the investment portfolio expands and the investment results begin to vary, discussion may increase. Einar Risa explained that, in Norway, there is robust discussion about the results of the investment of their petroleum revenue: ‘When the return is less than average there is an outcry in the media [in Norway]’. Once a portion of Timor-Leste’s Petroleum Fund

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152 Partido Social Democrata is the Social Democrat Political Party.
is invested in a wider range of instruments, it will then be some time before patterns of financial return emerge and East Timorese (with the capacity) build an understanding of the way in which financial markets work. Nevertheless, for the time being the opinions of the participants closely reflect government policy in regard to the level of Petroleum Fund investment risk.

6.3.2 Where to invest

A matter that has been debated publicly is where Timor-Leste’s petroleum revenue is invested. The criterion (decision) of where to invest petroleum revenue was ranked fifth important out of the six petroleum revenue management criteria (decisions), with a 14.9% share of participants’ priority (see Figure 6.1 on page 142). The two categories (options) presented to participants were ‘Overseas’ or ‘In Timor-Leste and Overseas’. The reason this criterion (decision) was included in the Point*Wizard research was because in the semi-structured interviews, some participants expressed concerns that the revenue would be invested in the US Federal Bank and it appeared they thought the revenue should stay in Timor-Leste. Figure 6.6 illustrates the relative rankings of those two categories (options). The majority of participants preferred a model of petroleum revenue management in which all of Timor-Leste’s petroleum revenue is invested offshore. However, during the interviews it was evident that some participants could not distinguish between investing financially and spending petroleum revenue. With comments such as ‘we have to recognise people [East Timorese] own it [the money]’ (Male NGO) in response to this issue, the research suggests that some participants felt that where Timor-Leste’s petroleum revenue was invested was related to the question of how independent Timor-Leste was in managing their petroleum revenue.

Some of the other participants’ comments about where revenue is invested are presented in Box 6.8. They indicate that some participants have little understanding about financial investment. As an example, one participant suggested a terrorist could bomb the bank and take the money. A Foreign Adviser explained that Kuwait and Brunei had successfully invested their revenue offshore, but observed that ‘the problem here [in Timor] is the political one. It will be difficult to explain why the money is being invested outside of Timor.’ Once a distinction between financial investment and investing by spending in Timor-Leste is understood, this problem may be rectified. Einar Risa pointed out there is widespread ignorance of financial investment in Timor-Leste. Risa added that this is not the issue that people should be most concerned about:

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153 The option of investing solely in Timor-Leste was not presented as it would be physically impossible to financially invest large amounts (millions of dollars) of revenue in Timor-Leste at this point; there is no large industry and no stock exchange, etc.
Figure 6.6  Rankings of the categories (options) within the criterion (decision) of ‘Whether petroleum revenue is invested offshore’

Box 6.8  Participants’ comments about where petroleum revenue is invested

Participants’ quotes favouring investing revenue in Timor-Leste (and offshore)
Because not focus only overseas, but internally because we also have to provide funds to develop internally. Yes. [Petroleum revenue should be invested] in banks in Timor so they can use. (Male NGO)
You need to invest money here to provide market confidence. (Male Academic)
We need to have a bank. Can not just keep overseas if something happens it will all be gone. (Male Union Leader)

Participants’ quotes favouring investing revenue offshore
First, implementation. Invest in outside because the risk inside is greater. Because economy; Inflation is high. Much money would be circulating in this country. We can create a strategy to spend more money. Put money inside and terrorism could come to bomb our bank. Its preventative to put outside. This money is the property of Timor-Leste’s people. (Male Decision-maker)
Bruce and Cristino [the Macroeconomics Unit] gave a presentation. The discussion revolved around why revenue would be invested overseas and one of the reasons given was ‘because of war’ (i.e. so that the money can not be used to fund arms in the event of civil disruption). This was giving a bad impression and was misinformation. (Male Decision-maker)
It should be invested offshore (mostly) to avoid economy shocks. (Male Foreign Adviser)
[The priority is] Ensuring the money is invested overseas. (Jose Teixeira, Minister of Natural Resources, Minerals and Energy Policy)
It seems there is not enough guidance on what are the key issues. The key issue is not which bank the money is invested in… I understand that there is no knowledge of international finance, but they should be discussing how this is going to be used. Is it going to be spent on infrastructure in the country or will it be invested overseas? (Einar Risa, Commissioner and former Executive Director, TSDA)

Participants clearly gave much greater priority to the investment of Timor-Leste’s petroleum revenue by spending it, than its financial investment. What petroleum revenue is spent on was the most important criterion (and this is explored in Chapter Seven). However, as Nauruans learned the hard way, if the financial investment of petroleum revenue is not managed well, there will be no petroleum revenue to spend.

6.3.3 What currency to invest in

Which currency petroleum revenue is invested in was the least important of all the petroleum revenue management criteria (with just 8.2% of participants’ priority). The lack of understanding of finance and investment may have had an impact on this ranking. The categories (options) within this criterion (of what currency petroleum revenue is invested in) were ‘US$', ‘Euros’, or ‘US$ and Euros’ and their relative rankings are illustrated in Figure 6.7. The combination of US$ and Euros was slightly more preferred than US$ alone. Some participants explained this preference, saying that a mix of currency might yield a better return if the risk is spread, but one participant noted there is a lack of capacity amongst East Timorese to manage this kind of diversity at this stage. Some of the comments the participants made when choosing this dilemma are presented in Box 6.9.

Presenting the dilemma to participants also generated comments about Timor-Leste’s policy of having the US$ as their currency. The participants’ comments generally indicated their support for the Government’s currency policy. The relatively large preference for investing solely in US$ may also be indicative of the level of ignorance surrounding the concept of what currency to invest in as some of the comments revealed that some participant’s reasons for choosing ‘US$’ was simply because it was Timor-Leste’s currency.

The results of the Point*Wizard research (particularly participants’ comments) reveal that the reason these aspects of the management of Timor-Leste’s petroleum revenue appear to be less important to participants may be related to the level of participants’ understanding of these aspects. Financial investment is a topic that is not widely understood amongst participants, let alone East Timorese in general, and a distinction between East Timorese and foreign advisers’
Figure 6.7  Rankings of the categories (options) within the criterion (decision) of ‘Whether revenue is invested in’

Box 6.9  Participants’ comments about which currency petroleum revenue is invested in

Participants’ comments about which currency petroleum revenue is invested in
We can invest in many currencies, but right now we don’t have the capacity. (Male Decision-maker)
US$ because this is the East Timorese currency (implying that the investment is in Timor). (Young Male District Veteran)

Participants’ comments about the Government’s policy of having a US$ currency
Our currency is US$ and it is international. (Male Union Leader)
If there is a crisis and we have no money its better because the US currency is stronger. (Male District Community Leader)
We are using USD, but if we use our own currency we may become victims of the Dutch disease. (Male Decision-maker)
US$ is important because we are not facing the exchange rate. The US$ is the currency that is being used in the oil and gas sector. It’s easy. (Male Decision-maker)
The US$ currency needs to be preserved. In order to avoid a situation where people are storing local currency under their bed in case the exchange rate dives. The US$ is better for the long haul. (Male Foreign Adviser)
knowledge in this area was evident from their comments. A decision-maker was asked ‘What sort of feedback have you been getting from the community in regards to Petroleum Fund management?’ and her response was ‘None really. In our information sessions the people are generally expats that ask about these things. We have mentioned the Petroleum Fund in presentations, but there have been no questions about it.’ This is another illustration that capacity is a factor for the wise management of Timor-Leste’s petroleum revenue.

Finance and investment management are skills that very few East Timorese have so this is an aspect of petroleum revenue management where foreign advice and input is necessary. For this reason, it is useful that the Petroleum Fund Law provides for decisions about the investment of petroleum revenue to be made by External Investment Managers guided by an IAB. During the semi-structured interviews (before the Petroleum Fund Law was enacted) participants suggested an ‘investment council’ should be created. A foreign adviser suggested investment management of the fund should be contracted out and an East Timorese participant said that although it was important to have international representation on ‘an Investment Committee’, it should be as partners (to make recommendations) and the IMF and the World Bank should observe (rather than direct or participate in) the process. Several participants expressed concern that the revenue be managed independently and that the revenue managers should report to Parliament. In summary, these comments highlight that participants desire independence in their decision-making, but they also demand independent management of Timor-Leste’s petroleum revenue. Both can be achieved under the Petroleum Fund Law; the External Investment Managers provide independent investment advice and the IAB (with both East Timorese and foreign members) is accountable to the Minister for Finance, providing independence (from foreign institutions) in the investment decision-making.

Participants’ thoughts on six decisions about the saving and investing of Timor-Leste’s petroleum revenue were explored in this chapter. Decisions that involved options that might affect Timor-Leste’s independence were the most important to participants. Decisions that involved consideration of financial management, which participants might not be familiar with, held less importance. Their responses were not necessarily based on the amount of revenue that could be generated; political and economic reasons also dictated their reasoning. By and large, participants were conservative in their decision-making, advocating lower risk and more sustainable outcomes. However, the results suggest that faced with a conflict of interest, participants would prefer revenue was spent on current generations. The following chapter explores this question, of what Timor-Leste’s petroleum revenue is spent on, in greater detail.

154 Some foreign advisers made comments about the criteria (decisions) and the categories (options) which revealed the research design did not elicit the level of detail they expected to make some decisions. For example, in regard to level of investment risk, one foreign adviser said ‘it depends how high the risk’, and in regard to the criterion (decision) of ‘whether the amount of petroleum revenue spent is sustainable’ one foreign adviser pointed out ‘more than US$100million’ might be just US$101million (thus it would make little difference as an alternative).