

**Timor-Leste - European Community**

**Country Strategy Paper**

**and**

**National Indicative Programme**

**for the period 2008 - 2013**

The Government of Timor-Leste and the European Commission hereby agree as follows:

- (1) The Government of Timor-Leste, represented by H.E. Dr. Emilia Pires , Minister of Finance and National Authorizing Officer, and the European Commission, represented by H.E.Mr. Juan Carlos Rey Salgado, Head of the European Commission Delegation to Timor Leste hereinafter referred to as the Parties, held discussions in Fiji and Dili from March 2006 to November 2007 with a view to determining the general orientations for cooperation for the period 2008 –2013. During these discussions, the Country Strategy Paper and an Indicative Programme of Community Aid in favour of Timor-Leste were drawn up in accordance with the provisions of Articles 2 and 4 of Annex IV to the ACP-EC Partnership Agreement, signed in Cotonou on 23 June 2000 as revised in Luxemburg on 25 June 2005. These discussions complete the programming process in Timor-Leste. The Country Strategy Paper and the Indicative Programme are annexed to the present document.
- (2) As regards the indicative programmable financial resources which the Community envisages to make available to Timor-Leste for the period 2008-2013, an amount of €63 million is foreseen for the allocation referred to in Article 3.2 (a) of Annex IV of the ACP-EC Partnership Agreement (A-allocation) and of €1.1 million for the allocation referred to in Article 3.2 (b) (B-allocation). These allocations are not entitlements and may be revised by the Community, following the completion of mid-term and end-of-term reviews, in accordance with Article 5.7 of annex IV of the ACP-EC Partnership Agreement.
- (3) The A-allocation is destined to cover macroeconomic support, sectoral policies, programmes and projects in support of the focal or non-focal areas of Community Assistance. The Indicative Programme under Part 2 concerns the resources of the A-allocation. It also takes into consideration financing from which Timor-Leste benefits or could benefit under other Community resources. It does not pre-empt financing decisions by the Commission.
- (4) The B-allocation is destined to cover unforeseen needs such as emergency assistance where such support cannot be financed from the EU budget, contributions to internationally agreed debt relief initiatives and support to mitigate adverse effects of instability in export earnings. The B-allocation shall be triggered according to specific mechanisms and procedures and does therefore not yet constitute a part of the Indicative Programme.
- (5) Resources can be committed within the framework of the present Country Strategy Paper and Indicative Programme upon the entry into force of the 10<sup>th</sup> EDF multi-annual financial framework for the period 2008-2013 of the revised ACP-EC Partnership but not before 1 January 2008. Financing decisions for projects and programmes can be taken by the Commission at the request of the Government of Timor-Leste within the limits of the A- and B-allocations referred to in this document. Financing decisions can also be taken *on the basis of Article 15(4) in conjunction with Article 4(1) (d) of Annex IV to the*

ACP-EC Partnership Agreement for support to non-State actors or<sup>1</sup> on the basis of Article 72(6) to the ACP-EC Partnership Agreement for humanitarian and emergency assistance funded from the B-allocations. Financing decisions shall be taken and implemented according to the rules and procedures laid down in the EC Council regulations on the implementation of the 10<sup>th</sup> EDF and on the financial regulation applicable to the 10<sup>th</sup> EDF and in Annex IV to the ACP-EC Partnership Agreement.

- (6) The European Investment Bank may contribute to the implementation of the present Country Strategy Paper by operations financed from the Investment Facility and/or from its own resources, in accordance with Paragraphs 2(c) and 3 of Annex Ib to the ACP-EC Partnership Agreement regarding the 10<sup>th</sup> EDF multi-annual financial framework for the period 2008-2013.
- (7) In accordance with Article 5 of Annex IV to the ACP-EC Partnership Agreement, the National Authorising Officer and the Head of Delegation shall annually undertake an operational review of the Indicative Programme and undertake a mid-term review and an end-of-term review of the Country Strategy Paper and the Indicative Programme in the light of current needs and performance.  
The mid-term review shall be undertaken in 2010 and the end-of-term review in 2012. Following the completion of the mid- and end-of-term reviews, the Community may revise the resource allocation in light of current needs and performance.  
Without prejudice to Article 5.7 of Annex IV concerning reviews, the allocations may be increased according to Article 3(5) of Annex IV in order to take account of special needs or exceptional performance.
- (8) The agreement of the two parties on this Country Strategy Paper and the National Indicative Programme, subject to the ratification and entry into force of the revised ACP-EC Partnership Agreement and the 10<sup>th</sup> EDF multi-annual financial framework for the period 2008-2013, will be regarded as definitive within eight weeks of the date of the signature, unless either party communicates the contrary before the end of this period.

Signatures

**For the Government of Timor-Leste**

**Prime Minister**

  
**H.E. Kay Rala Xanana Gusmão**

**National Authorizing Officer  
and Minister of Finance**

  
**H.E. Emilia Pires**



**For the Commission**

**Head of Delegation**

  
**Juan-Carlos Rey Salgado**



<sup>1</sup> In order to enable a direct support to the NSA, i.e. without prior NAO agreement (Article 15 (4) of Annex IV), it is necessary to specify in more details in the NIP the types of NSA eligible for funding, the resources allocated and the type of activities to be supported (which must be not-for-profit) (Article 4 (1) (d) of Annex IV).

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## EXECUTIVE SUMMARY

Timor-Leste ratified the ACP-EC Partnership Cotonou Agreement on 19 December 2005 and benefited from an amount of €18 million for the two years remaining under the 9<sup>th</sup> European Development Fund (EDF) with the areas of sustained rural development and institutional capacity building. The country is now included in the programming of the 10<sup>th</sup> EDF and has been allocated an initial amount of € 63 million. There is a good deal of continuity in the approach of this country strategy and the previous strategy under the Asia-Latin America budget line of which the country received development assistance since its accession to Independence in 2002. The framework is based on EU/ACP co-operation objectives (notably the reduction of poverty and integration of developing countries into the world economy), the Government of Timor-Leste's (GoTL) own development policies, an analysis of the political, social and economic situation in the country, and an assessment of past co-operation programmes with the EC and other donors.

Timor-Leste has emerged sovereign recently after a 24 year colonial period of underdevelopment and a struggle to gain independence from Indonesia. It is a young and still very fragile nation as evidenced by the recent serious political and humanitarian crisis which is still far from being over. The latter will only be resolved by addressing its turbulent past and human rights' violations. In terms of identity and nation-building, Timor-Leste will also need to address and to work for constructive relations with its neighbours. The new country needs to address a number of challenges, i.e. to alleviate widespread and structural poverty, particularly in rural areas, to create sustainable livelihoods for its population and to build human and institutional capacities. Timor-Leste is beginning to benefit from substantial off-shore oil and gas reserves, a situation which offers great economic potential but also the danger of mismanagement and corruption.

Following the elections on 30 June 2007 a Government was formed consisting of four political parties that established a platform to bring about the necessary reforms. The programme of the IV Constitutional Government which was approved by the Parliament in September 2007 consists of a two-year national recovery programme and a commitment to prepare and develop a Strategic Plan for Economic Development for Timor-Leste that will run until 2012. Emphasis shall be on economic growth, security sector reform, institution building, supporting the return of displaced people, providing youth employment, vocational training, community development programmes, agriculture, infrastructure and health. The priorities of the new Government are in line with the planned Community support.

### **Main objectives and intervention areas (Indicative programme: € 63 million)**

- 1) **Sustainable rural development:** socio-economic development of the poorer rural areas, in order to achieve sustained poverty reduction and food security and improved service delivery. This supports the GoTL's own sector investment plan for agriculture and rural infrastructure such as rural roads, water supply and electricity. Indicative allocation: € 35 million.
- 2) **Health:** improve the availability, accessibility and affordability of health services to all people in Timor-Leste and the participation of the community and other stakeholders in the implementation of the National Health Plan. Indicative allocation: € 8 million.
- 3) **Institutional capacity building,** which is in line with the GoTL's goal of achieving sustainable national capacity for improved service delivery within the Executive and in the institutions which are responsible for checks and balances. Indicative allocation: € 13 million.
- 4) **Non focal sectors:** Support to the civil society and Technical Cooperation Facility: Indicative allocation: € 7 million.

## PART 1: STRATEGY PAPER

### CHAPTER I: THE FRAMEWORK OF RELATIONS BETWEEN THE DONOR AND THE PARTNER COUNTRY

#### I.1.1. General Objectives of the EC's external policy

In accordance with Article 177 of the Treaty Establishing the European Community, community policy in the sphere of development co-operation shall foster:

- The sustainable economic and social development of the developing countries, and more particularly the most disadvantaged among them;
- The smooth and gradual integration of the developing countries into the world economy;
- The campaign against poverty in the developing countries.

Europe should project a coherent role **as a global partner**, inspired by its core values in assuming regional responsibilities, promoting sustainable development, and contributing to civilian and strategic security

The Union has developed a broad spectrum of external relations tools in the shape of the common trade policy, cooperation under bilateral and multilateral agreements, development cooperation, humanitarian aid and financial assistance as well as the external aspects of internal policies (energy, environment, transport, justice and home affairs, etc).

EU external action including the Common Foreign and Security policy, common trade policy and cooperation with third countries provides a framework both for integrating all EU instruments and for developing gradually a set of common actions based on common positions in the broader sphere of political relations.

Enlargement has entrusted EU with even greater responsibilities, as regional leader and as global partner. It should therefore strengthen its capacity to promote human rights, democracy and the rule of law as well as its capacity to focus on the fight against poverty, both in its neighbourhood and through its multilateral and bilateral policies which are mainly aimed at sustainable development and political stability. Thus, the EU will achieve genuine coherence between its domestic and its external agendas, contributing thereby to global security and prosperity.

#### I. 1.2. Strategic objectives of cooperation with the partner country

The Treaty objectives are confirmed in Article 1 of the *ACP-EU Partnership Agreement*, signed in Cotonou on 23 June 2000 and revised in Luxembourg on 25 June 2005. The overarching objective of the *Cotonou Agreement* is to promote the development of a common strategic approach to poverty reduction, consistent with the objectives of sustainable development and the gradual integration of ACP countries into the world economy. Cooperation between the Community and Timor-Leste shall pursue these objectives, taking into account the fundamental principles set out in Article 2, in particular the encouragement of "ownership" of the strategy by the country and populations concerned, and the essential elements and fundamental element as defined in articles 9 and 11b of the Agreement.

While the Treaty and the Cotonou Agreement provide the legal basis for EC cooperation with ACP countries, the recently adopted *European Consensus on Development* sets the general policy framework at EU level. The primary and overarching objective of EU development policy is the eradication of poverty in the context of sustainable development, in line with the international agenda, and with particular attention for the Millennium development Goals (MDGs). Human rights and good governance are recognised as other important objectives.

In May 2006 the European Commission issued a Communication to the Council, the European Parliament and the European Economic and Social Committee on "**EU Relations with the Pacific Islands – A Strategy for a Strengthened Partnership.**" The Council adopted this Communication in July 2006. The Strategy consists of three components: (i) a strengthened relationship between the EU and the Pacific region to allow for a broad political dialogue; (ii) more focussed development cooperation with a central theme relating to the sustainable management of natural resources, and (iii) more efficient aid delivery.

Better aid effectiveness is essential to achieving poverty eradication. Therefore the EU will advance coordination, harmonisation and alignment. It will promote better donor complementarity by working towards joint multi-annual programming based on partner countries strategies and processes, common implementation mechanisms, joint donor wide missions, and the use of co-financing arrangements. The EU will take a lead role in implementing the Paris Declaration commitments on improving aid delivery and it will capitalise on new Member States' experience to strengthen their role as donors.

Policy coherence for development will advance in a number of areas. The purpose is that all EU non-aid policies make a positive contribution to developing countries' efforts to attain the MDGs.

The principle of concentration will guide the Community country and regional programming. This means selecting a limited number of priority areas of action, through the dialogue with partner countries, rather than spreading efforts in too many sectors. In this context the Community will be primarily active in the following nine areas, keeping into account its comparative advantages in a number of these: trade and regional integration; the environment and the sustainable management of natural resources; infrastructure, communications and transport; water and energy; rural development, territorial planning, agriculture and food security; governance, democracy, human rights and support for economic and institutional reforms; conflict prevention and fragile states; human development; social cohesion and employment.

The mainstreaming approach will be strengthened for four cross-cutting issues: democracy, good governance, human rights, the rights of children and indigenous peoples; gender equality; environmental sustainability; and the fight against HIV/AIDS.

### **I.1.3 Main bilateral agreements with the EU**

Timor-Leste signed the revised Cotonou Agreement in December 2005 through which it became member of the ACP group of countries.

## **CHAPTER II: COUNTRY DIAGNOSIS**

### **II.1. Analysis of the political, economic, social and environmental situation in the recipient country**

#### **II.1.1 Political and institutional situation**

Timor-Leste voted for independence in a UN supervised referendum in August 1999. The subsequent administration of the UN (UNTAET) was too short for ensuring the consolidation of the country's democratic institutions. Security institutions proved to be very fragile.

In 2001, following elections of an 88-member Constituent Assembly FRETILIN (Revolutionary Front for the Independence of Timor-Leste) by virtue of its steadfast advocacy of independence the dominant political party, won short of an absolute majority. On 21 March



2002, a Constitution was approved establishing a republican system of government, and the Constituent Assembly transformed into the National Parliament. On 14 April 2002, East Timorese elected 'Xanana' Gusmão as the country's first president, with 83 per cent of the votes cast, one of the leaders of the pro-independent movement. While his official powers were limited, his personal stature had given him wide influence over the new country's first years of governance. In May 2002, Timor-Leste became formally independent, and the Government, formed by FRETILIN, was sworn in under the leadership of Prime Minister Mari Bim Amude Alkatiri.

Despite considerable progress made in creating the institutions of a modern democracy from scratch, the political situation in Timor-Leste remained fragile. The country's stability has been seriously disrupted for the 1<sup>st</sup> time by riots in Dili in December 2002 following the shooting and killing of two demonstrating students by police. Stability was tested again for the 2<sup>nd</sup> time during a three-week demonstration organised by church leaders in April/May 2005, yet the demonstration remained largely peaceful and showed the police forces capable of restraint and professionalism.

For the 3<sup>rd</sup> time, unrest started again in February 2006, when hundreds of soldiers left their barracks and went on strike. Originating mostly from the western part of the country, the soldiers complained of regional discrimination in the attribution of promotion, which allegedly benefited soldiers originating from the East. In mid-March 594 members of the Timorese armed forces were dismissed. The sackings sparked rioting, arson and violence in the capital, Dili. The security forces disintegrated and fighting between parts of the police and army broke out. Descent into civil war was probably averted only thanks to rapid deployment of international security forces following a request made by the main state institutions to the UN, Portugal, Australia, New Zealand and Malaysia.

On 25 August, the UN Security Council approved a reinforced presence in Timor-Leste, the "United Nation Integrated Mission for Timor-Leste" (UNMIT). UNMIT is now present with a police force of 1,600 officers while the International Stabilisation Force (ISF) led by Australia and New Zealand has a military force of 900 soldiers. Australia and New Zealand did not accept to put the ISF under the UN command.

The security crisis of 2006 proved to be the merger of many unresolved issues such as personality conflicts, regional cleavages (East-West), lack of adequate communication between institutions and with the population, high unemployment and unfulfilled expectations, weak justice system and impunity dating back from the Indonesian occupation as well as from the civil war of 1975.

However, consensus among the Timorese leadership has led to the holding of free and fair Presidential and Parliamentary elections between April and June 2007. Results were accepted by the contending parties although differences emerged from the interpretation of the constitution for the formation of the new Government. Eventually no dispute of the constitution was brought to the Court of Appeal and the former ruling party FRETILIN returned to the Parliament as the new major opposition party.

The relatively peaceful and smooth conduct of the elections in 2007 is seen as an important milestone for the further gradual build up of the country and its structures.

The new IV Constitutional Government has recently set priorities for the short, medium and longer term. Emphasis shall be on economic growth, security sector reform, institution building, supporting the return of displaced people, providing youth employment, vocational training, community development programmes, agriculture, infrastructure, health and solidarity with vulnerable groups.

The country has ratified all major international human rights conventions (cfr Annex 13). TL is in the process of reporting on the implementation of these conventions. It has a constitutionally mandated Ombudsman and Human Rights Commission. The Constitution provides for the fundamental freedoms (freedom of movement, thought, religion, expression, information and assembly and association).

The justice system which is in the early stages of its development is confronted with a number of challenges. It can be regarded as the weakest branch of Timor-Leste's governance architecture due to the lack of sufficient material and human resources in the courts and the low level of capacity among many court actors. For the time being, the judiciary is very much dependent on the international community for judges, prosecutors, lawyers and training. Various efforts have been made to improve the judicial sector, including the appointment of international judicial officers, setting-up a Judicial Training Centre for training and evaluation of court actors. But much remains to be done to translate the governance architecture set out in the Constitution into a well-functioning and fully autonomous judicial system. As long as this is not achieved yet, access to justice for the citizens continues to be severely limited.

Civil society and media play a constructive and increasingly important role. Much like political leaders and Government, civil society has had to make the difficult transition from resistance against the Indonesian occupation to effective participation in nation building. A number of non-governmental organisations (NGOs) undertake useful monitoring, advocacy, education, and advisory services in the areas of human rights (Associação HAK), justice (Judicial System Monitoring Programme), gender awareness (Fokupers, Rede Feto), the environment (Haburas), and international assistance (Lao Hamutuk). As 98 percent of Timor-Leste's population is Catholic, the Church is very influential and could play an active role in conflict mitigation and service provision. The print media in Timor-Leste have grown from non-existent under Indonesian times to several daily and weekly newspapers, but only a small proportion of the population has access to them. National and community radio, on the other hand, reaches a wide audience and provides a popular forum for interactive debate.

Poor outreach on the part of Government may contribute to Timor-Leste's vulnerability. Effective communication and genuine participation are critical to shoring up popular support for the national development process, and for avoiding conflict. Many of the positive and necessary development outputs of the last three years, such as policies, laws, and the completion of institutions, are largely invisible to the electorate. At the same time, service delivery results are mixed. Expectations of prosperity following the restoration of independence were high, but the Government neither had the resources nor the intention to re-establish the paternalistic state maintained by the Indonesian occupation. Yet the first constitutional Government was hesitant to collaborate with civil society and maintained a "statist" style. It did not succeed in engaging constructive critics or in maintaining an effective dialogue with communities. It is hoped that the new Government's intentions to enhance the role of the civil society as well as to improve checks and balances in state institutions will be permanent part of its programme.

While both Portuguese and Tetum are national languages, critical documents are often only published in Portuguese, which only a small fraction of the population understands. Government is increasingly recognising the importance of consultation and information dissemination by using more Tetum and even Indonesian as working languages. In the past extensive public consultations were carried out only for the debate on the petroleum revenue savings policy and the associated Petroleum Fund.

While limited in number, the hard-core militia remaining in West Timor poses a real, if small, risk of externally generated conflict. Since 2002, there have been several incursions by militia

in which Timorese villagers have been killed. More significant than external factors are the lack of national identity and internal fault lines contributing to the risk of renewed violence, including declining income, increasing poverty, high unemployment, and emerging corruption. The rapidly expanding Youth and high youth unemployment have fuelled an expansion in martial arts groups. There are a number of relatively small, but vocal groups who reject the legitimacy of the Government and some former members of the resistance continue to feel disenfranchised. The security forces still lack professionalism and experience. There have also been several serious disruptions between the forces themselves, causing significant public concern. While no one of these factors is likely to ignite serious conflict, their combined effect remains unpredictable.

At present security is largely in the hand of the UN integrated mission (UNMIT) and the International Security Forces (ISF) led by Australia and New Zealand. On the presentation of the UNMIT report to the UN Security Council in September 2007 the newly appointed Minister of Foreign Affairs requested an extension of the UNMIT mandate until 2012 while the current mandate holds only until 2008.

### **LESSONS LEARNED FROM THE 2006 CRISIS**

Until the crisis occurred there was the general assumption that political institutions were more solid, accepted, respected and legitimised than they really were. There has been pressure from some UN security members to downsize and ultimately withdraw the UN peace keeping mission. There has also been a general hurry to withdraw support from Ministries at times when it was still needed. Previous Governments and donors concentrated on the structural build up of institutions thereby neglecting the psychological effect of past conflicts, the importance of veterans, regional differences and the parallel institutions of the traditional society. Aid was provided more to the Government than to other state institutions or civil society organisations.

The centralised process of governance observed by the previous administration brought also centralisation of donors' programmes. The balance between policies towards building state institutions and policies versus outreaching rural communities was often in favour of the first.

Past programmes to support the youth and unemployed people had been designed and a focus had been put on rural development in order to foster growth and create employment. However, the crisis came before such programmes could bear fruits.

Identified underlying causes which contributed to the crisis include among others:

- The failure of the previous government to engage with the people particularly to sustain the sense of national identity that brought Timor-Leste to independence.

In a nation-building context where many of the achievements made have been invisible to the population, two-way communication and transparency are critical and improving the frequency and quality of public consultation builds popular consensus and ownership over the development agenda and reduce the risk of future conflicts.

- The resurfacing of divisions that pre-dated 1999 has highlighted the need to address the past as part of the nation-building process. The demand for justice and accountability for past serious crimes remain a fundamental issue in the life of many Timorese. The need for reconciliation and community healing in relation with these crimes is equally important.

- Poverty and its associated deprivations including high youth and urban unemployment and the absence of any prospect of meaningful involvement in the foreseeable future. While oil and gas has started to transform Timor-Leste's economic prospects, the sector will not directly generate many jobs. Translating petroleum wealth into broad-based development will

depend on sustained pro-poor public expenditures and investments and well-administered public sector programmes designed to deliver quality basic social services, especially targeting vulnerable and marginalised groups. Especially important in this regards are policies and public investments in agriculture which employs around three quarters of the labour force but generate only one fifth of non oil GDP.

The crisis is far from being resolved as many of its underlying factors can only be addressed in the longer term. The new Government will need social legitimacy through the reduction of unemployment and increased communication with the population. Both Government and opposition will need to channel their differences through political parties and political confrontation in the Parliament and the crisis itself has created new potential sources of instability: number of weapons in civil hands, thousands of displaced persons and large numbers of discontented members of the security forces.

Hence the country remains vulnerable to conflicts: The risk of renewed violence is compounded by internal fault lines: declining income, increasing poverty, high unemployment and emerging corruption.

Cfr Annex 1 'The political transition in Timor-Leste'.

### **II.1.2 Economic and commercial situation**

Timor-Leste is one of the least developed economies in the region and is essentially agriculture-based, with over two-thirds of the population living in rural areas, and at least one-third engaged in subsistence agriculture. Agricultural productivity is very low and suffers from insufficient diversification. Figures for 2006 (source: IMF and Timorese authorities) give GDP per capita at USD 375 (non-oil), but it is probably much lower in the more isolated rural areas. Including oil income the GDP per capita rises to more than USD 700. Unemployment is estimated to be 5% nation wide, and 20% in the capital, Dili. About 10,000 young people join the labour market every year. Inflation was estimated at 5.7% at the end of 2006. Due to the crisis in 2006 real non-oil GDP growth is estimated at around minus 1.5%. The country would need a growth of 7-8% in the medium term to ensure a sustained decline in poverty with a population growth rate of well over 3%. GoTL pursues an active policy of avoiding national debt.

A major challenge in Timor-Leste's macroeconomic situation is the huge revenue it can expect from the petroleum and gas reserves in the Timor Sea. At independence, Timor-Leste signed the Timor Sea Treaty with Australia securing 90% of revenues from the "Joint Petroleum Development Area", an arrangement which however excluded most of "*Greater Sunrise*", a larger and more lucrative gas field, due to a difference of interpretation of respective maritime boundaries. After a series of sometimes bitter talks, Australia and Timor-Leste finally signed an agreement on 12 January 2006 on the sharing of natural resources from the Timor Sea, allocating 50% of the revenues outside the Joint Petroleum Development Area (JPDA) to Timor-Leste. The revenues to be obtained under the agreement of the *Bayu Undan* field alone could deliver USD 11 billion in the next 20 years at current oil prices, with an expected USD 10 billion for the *Sunrise* field. Parliament has adopted a strong legal framework for on- and off-shore petroleum production. The Petroleum Law, passed unanimously by Parliament, commits the Government to saving most of its petroleum revenues in a state-of-the-art petroleum fund designed to yield a sustainable income in perpetuity. This legal framework makes Timor-Leste a leading model in the Extractive Industries Transparency Initiative and provides a sustainable resource basis for the development of the country if it can properly invest its revenues and avoid mismanagement.

Over the next years, Timor-Leste faces a rapid expansion in petroleum sector revenues, which risks putting tremendous pressure on its public financial management system. Oil and gas revenues amounted to US\$ 342 million in 2005 and are projected at US\$ 882 million for 2007. The oil and gas revenues (drawn from interests of the petroleum fund) in the central government budget were US\$ 128 million in 2005 and are projected to be US\$ 192 million in 2007. The overall balance surplus is continuously growing as the country is not yet in a position to properly absorb its budget. A properly implemented and rapidly growing budget could boost the delivery of public services and promote growth, and construction activities under the capital development budget could contribute significantly to employment creation. Nevertheless, this new wealth will require careful management. Sound PFM will become even more important. One of the crucial future challenges for the Government is to be able to justify to the population the choices it makes in the use of the growing petroleum revenues, to avoid conflict over use of resources. It is essential that the Government programme continues to be pro-poor, aimed at eradicating malnutrition and hunger, and at creating employment and an environment that is free from corruption.

Against this buoyant outlook for the public fiscal position, the prospects for private sector are discouraging given unpredictable weather conditions for rural production and lack of local micro-credit. Timor-Leste's economy is uncompetitive due to i) small, isolated markets, ii) high costs of transportation, iii) low skills base and iv) poor physical infrastructure and weak or incomplete government institutions and financial and banking sector.

The agriculture sector, which could potentially transform non renewable resources into a sustainable economy, has suffered for lack of resource allocation. Until 2004 agriculture received 2.1% of the total budget. During the period 1999-2004 a total of \$72.5 Million was spent by donors and Government on programmes within the sector. Donors contributed 92% of the total programme. It was only from 2005-06 that the sector was allocated 4.7% of the total budget. The 2006 Sector Investment Programme envisaged total expenditures of US\$ 67 Million of combined sources for a 5 year period. The new Government is budgeting about US\$ 22 million of Government resources for 2008 alone giving high priority to the sector.

### **Structure of public sector finance and main sectoral policies**

The public financial management system in Timor-Leste has made steady progress since the restoration of independence. Under the new Government efforts are being placed to deconcentrate and decentralise functions and responsibilities, most notably in the area of finance so as not to undermine efficient service delivery. In addition to a general shortage of technical skills at all levels, the GoTL lacks seasoned managers. The GoTL therefore wants to move beyond the transitional substitution of international for local expertise and focus on an integrated approach to government-wide institution building that relies on three pillars: skills and knowledge, systems and processes and attitudes and behaviour.

In the Fiscal year 2005-06, the financing of the public sector has continued to privilege the social sectors with education and health being allocated 32.5%. Of these, primary education received 45.9% and hospitals expenditures were allocated 38.2%. Agriculture has been increased to 4.7% while security has been kept at 20.1%.

### **Trade structure**

Timor-Leste is not at present a member of the WTO. However, it is a member of the World Customs Organisation (WCO). It has asked for observer status with ASEAN and its free trade agreement called AFTA. Since 2006, Timor-Leste has also become member of the ASEAN Regional Forum (ARF).

As regards the Pacific region, Timor-Leste is not party to any agreement with the rest of the Pacific ACPs at this point in time. It has observer status at the Pacific Islands Forum (PIF),

but is not a member of the Forum Secretariat or any of the other regional co-operation/integration organisations. Timor-Leste also decided for the time being not to take part in the negotiations between the EC and Pacific ACP for an Economic Partnership Agreement (EPA).

The main natural endowments of Timor-Leste are marine and fish resources, untouched environment (eco-tourism) and agriculture. However, the general economic environment places huge constraints on optimal trade conditions.

Timor-Leste has a narrow export base, and what little trade there is exists mostly in agricultural produce, e.g. green coffee beans. There is a huge trade deficit (mostly with Indonesia) which expanded to USD 133 million in 2006, amounting to about 20% of GDP. Non-oil exports rose to USD 9 million, of which USD 8 million was coffee. Coffee export revenues are however expected to rise over the medium term in response to higher international prices and improved marketing.

High local price levels make labour costs in Timor-Leste lose the normal competitive advantage of an LDC and reduce the country's attractiveness to foreign investors. This combined with insecurity make Foreign Direct Investment (FDI) in the productive sector limited – FDI received until now is USD 1.7 billion and 94% of that is destined for the oil and gas sector.

The local private sector is more involved in subcontracting, public investments or investments made by donors within the cooperation programme. Very little investment is made by the private sector.

To encourage inward investment and FDI there is a need to improve the enabling environment. The GoTL intends to improve the investment law prepared by the first Government and to further opening the economy by substantially decreasing taxes and custom duties. There is the intention to increase further commercialisation of agriculture and the production of marketable surpluses for domestic and export markets. Increased agricultural productivity and improved rural livelihoods translate into increased demand for off-farm goods and services. This requires increased private investment that leads to diversification of the economic base.

The benefits to Timor-Leste of the membership of the Cotonou Agreement are potentially significant but likely to appear only in the medium to longer term. However, to realise them, Timor-Leste will have to start to prepare itself now, studying the issues at stake and beginning to develop its capacity in trade. The Ministry for Development in Timor-Leste, responsible for trade, is conscious of its need for institutional capacity-building, both in terms of personnel, skills, and systems and also the preparation of a Trade Policy coordinated at inter-ministerial level (cfr Annex 2 "Development of trade in Timor-Leste").

### **Private Sector Development**

The country's economy is dominated by the private sector which accounts for two thirds of GDP. Excluding oil and gas, the private sector already accounts for 60% of the GDP. However the agriculture sector provides employment for three quarters of the country's labour force with very low productivity and represents only 32% of GDP. Generation of non-farm employment, which at present absorbs only a total of about 60,000 people, needs to be accelerated in order to absorb the 10,000 new entrants into the labour market every year.

Cfr Annex 3: Timor Leste at a glance.

### II.1.3 Social situation, including decent work and employment

The most recent comprehensive poverty data available still remains the national household and village survey conducted in 2001. Timor-Leste's Human Development Index 2004 is at 0.512, ranking it at 142 out of 177 countries with data (Human Development Report 2006). As outlined above, its economy is dominated by agriculture. Its GDP per capita is low (375 USD), and poverty is more pronounced in rural (46%) than in urban areas (26%), and may have increased since the recent crisis of April/May 2006. Wealth distribution is unequal (Gini coefficient 0.37). Lack of non-farm income increases the vulnerability of households, and malnutrition is a key issue. Women are important producers in the farms, but their access to land rights is very much limited by tradition. In general, land tenure is uncertain, given that out of 200,000 land parcels, only about 25% have undergone some form of registration.

About 70% of the urban population has access to relatively safe drinking water and electricity, while in rural areas only 51% of the population has access to safe drinking water. Electricity in rural areas is provided for a limited time at night and only to about 11% of the population.

The total fertility rate (live births per woman) was 7.8 in 2003, possibly the highest in the world. The annual population growth is over 3%. Social services delivery is improving only gradually, and social indicators remain among the lowest in the region, including gender-related indicators.

In general Timor-Leste has succeeded in increasing primary school attendance (75%), but the level of education is low by regional and international standards, and the quality of teaching is poor. The percentage of students attending secondary school is only around 20% and the adult literacy rate is estimated at 50%. Girls are more likely than boys to drop out of school and at least 55% of women aged 15-60 years are illiterate compared with less than half of men. A proliferation of private universities (17) which sprang up from private initiative at independence are not contributing very much to making adequate use of teachers and facilities for a tertiary student population of about 10,000.

Health indicators are still among the lowest for Asia. Maternal mortality is alarming with an estimated 660 deaths per 100,000 live births. Under-five child mortality caused by infections, premature births and low utilisation of skilled assistance is at around 130 per 1,000 live births (it has been reduced from 160 per 1,000 since 89-93). One in every eleven babies does not survive the first birthday.<sup>2</sup> It is estimated that 12% of children are wasted, and that 45% of the under five children are underweight. Malaria and Tuberculosis are widespread while there are recurrent dengue epidemics. Prevalence of HIV/AIDS is low, but increasing. Access to essential health services among the poor and those from remote areas is limited. Health standards are also compromised by a lack of food. Many rural households go short of food during the lean months from November to February. Currently 64% of the population suffer from food insecurity.

Since the April/May 2006 political and security crisis the country still has a high number (about 100,000) of internally displaced persons (IDPs), most of whom are staying with host families in the districts while the remainder are living in camps in and outside of Dili. In 2007, the Government phased out emergency assistance in the districts. Government, UN and donors agreed not to stop the food distribution during the elections. The Government intends to phase out the free distribution but has not yet taken a decision. WFP is still providing food for 70,000 displaced people due to the volatility of the security situation.

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<sup>2</sup> Health Sector Strategic Plan 2008-2012, Ministry of Health, September 2007

#### **II.1.4 Environmental situation**

Timor-Leste’s economy is heavily dependent on its natural resources. Land, water, forests and coastal zones provide a livelihood, or are the major source of income, for at least three-quarters of the population. They are the basis for social and economic security and growth. Mineral and petroleum deposits are expected to provide a significant source of income and foreign revenue for many years to come. Finally, many of Timor-Leste’s resources – for example, its pristine coastal ecosystems, its stands of sandalwood and its remaining primary forests – are a world heritage in need of protection. Besides the stocks of oil and gas in the Timor Sea and onshore gas, Timor-Leste is endowed with modest fishery stocks, and forestry resources. The rainfall pattern – particularly in the north with long dry periods followed by intensive, short rainfalls – is conducive to erosion, which has been further increased in many areas by deforestation and over-grazing. The new Government is aware of the need to develop its resources in a sustainable way, avoiding short to medium term benefits that could jeopardize the longer term future. The GoTL is also aware that the development of these resources will depend for the time being mainly on private sector initiatives and investments. The main efforts in environmental conservation so far have been concentrated on building a strong information data base on the resources, on preparing legislation and on preparing community management mechanisms. Despite some efforts, there are still problems of deforestation, land degradation, loss of biodiversity, urban pollution and waste management, and there is a need for reinforced regulatory framework and monitoring if this trend is to be reversed. The Commission’s rural development programme will address a number of these issues, in particular the sustainable development of natural resources.

It will also address the country’s vulnerability to natural disasters. Timor-Leste, like most of the Pacific Island countries, is exposed to natural disasters due to the vagaries of weather (extensive periods of drought and short and intensive rainy seasons), floods and land-slides, exacerbated by climate change, which together with heavy reliance on a limited range of economic sectors worsen the country’s vulnerability to external circumstances. NGOs and international organisations have already contributed to developing disaster risk reduction in Timor-Leste in various ways: capacity building, enhancement of public awareness about disasters through workshops, implementation of Community Based Disaster Risk Management (CBDRM) programmes in collaboration with rural communities and local authorities in some districts, and provision of relief assistance to affected communities affected by natural hazards. As a result, while the main concern of local communities’ remains production of sufficient and adequate food for their families, they are also aware of natural hazards that they are exposed to. On the other hand, the district government has limited capacity and resources, and is not able to fully assist the affected communities in responding to and preparing for a natural hazard.

An upturn in economic activity and increase in private investment has the potential to lead further to environmental degradation which will weaken the very foundation of Timor-Leste’s sustainable development, impacting negatively on agriculture, tourism, and food security, thereby increasing poverty.

At present, Timor-Leste is almost totally dependent on imported petroleum products and domestically produced firewood to meet its energy requirements and there is no National

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<sup>3</sup> One of the most difficult problems for strategic analysis of Timor-Leste is that the destruction of previous archives and of most administrative systems and structures has meant that economic and social statistical data are incomplete, or totally lacking - see main text and Annex 1 for further commentary.



Energy Policy. An energy policy that provides the basic Road Map for movement towards the objective of stable, secure and sustainable sources of energy is of great importance for the country.

It is essential that GoTL and donors take into consideration measures to mitigate and adapt to climate change effects.

Cfr Annex "Timor-Leste environment profile"

### **II.1.5 The country in the international context**

Geo-politically, Timor-Leste is situated between two large and powerful neighbours, Australia and Indonesia, and hence needs to actively develop links with them. Relations with Australia are improving, following an agreement on the sharing of oil and gas resources in the Timor Sea and the maritime boundary. With regard to Indonesia, mostly questions about past human rights' violations and the remaining border demarcation need to be addressed in a realistic manner. GoTL is pursuing an active policy of reconciliation with Indonesia. There are regular consultations at ministerial level, and in March 2006 both countries set up the Commission of Truth and Friendship (CTF) to establish agreed-upon facts regarding the events prior to and immediately after the 1999 referendum, with a view to further promoting reconciliation and friendship, even in the face of internal and international criticism that the terms of reference of that Commission do not comply with international standards on denial of impunity for serious crimes.

Another important regional power is China. China's growth has boosted trade in the region including ASEAN countries and the Pacific (Australia). As China is not part of the OECD, its support to Timor-Leste has been sometimes regarded with concern by other international players.

Timor-Leste was accepted into the ACP group of countries in 2003. Parliament completed the ratification process of the Cotonou Agreement on 19 December 2005. The country has observer status in the Pacific Islands Forum (PIF), the regional organisation which gathers the 14 small islands developing states scattered across the southern and central Pacific and Australia and New Zealand. The Forum is also the occasion for a formal dialogue with external political players, including the EU.<sup>4</sup> The Forum's permanent secretariat (PIFS) is entrusted with policy advice, coordination of regional cooperation and executive tasks in the areas of security, governance and trade and economic integration. The PIFS General Secretary functions as Regional Authorising Officer (RAO) for the Regional Indicative Programme (RIP) in favour of the Pacific ACP and provides technical support to the Pacific ACP's participation in EPA negotiations, in which TL does not take part at the moment. However, TL is under the 10<sup>th</sup> EDF for the first time eligible for support through the Pacific RIP. TL has for the time being no plans to become a full member of PIF. Instead, there is a priority to achieve full membership of ASEAN. In July 2005, as a first step, TL was admitted as participant to the ASEAN Regional Forum (ARF). In January 2007 TL signed the ASEAN Treaty of Amity and Cooperation (TAC).

With the accession to the Cotonou Agreement, TL is now sharing the features of the ACP group of countries using Portuguese as official language (PALOP) which comprises Angola, Cape Verde, Guinea-Bissau, Mozambique and São Tomé e Príncipe and which is characterised by a shared identity based on history, culture, language and heritage. TL will therefore also be included in a new framework of EC/PALOP cooperation under the 10<sup>th</sup> EDF.

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<sup>4</sup> During the latest Pacific Forum in October 2007 in Tonga this dialogue has been upgraded to a regular political dialogue.

On 20 May 2002 TL became the eighth member state of the **Comunidade dos Países de Língua Portuguesa (CPLP)**, a multilateral forum set up in 1996 with three general objectives: to deepen mutual friendship, political-diplomatic articulation and cooperation amongst its members, to foster technical cooperation in various sectors (education, health, public administration, justice, culture etc) and to promote and disseminate the Portuguese language. The members are the five PALOP countries, Brazil, Portugal and TL. A memorandum of understanding between PALOP/Timor-Leste and the European Commission on the modalities of operation will be signed in November 2007.

Cfr also Annex 13 "TL and its accession to international conventions".

## **II.2. Poverty reduction analysis**

With a per-capita GDP of USD 375, Timor-Leste is among the poorest countries in the world. The 2001 Poverty Assessment documented considerable inequality. There is a significant difference in poverty between urban and rural areas, and across geographic zones. Fourteen percent of the population in the urban areas of Dili and Baucau live below the poverty line, compared to 26 percent in other urban areas and 46 percent in rural areas. Eighty-six percent of poor people live in rural areas, where households experience insufficiencies in rice and corn approximately four months per year, on average. Among rural households, poverty tends to be worse in the highlands, which explains why poverty and other indicators of well-being are worse in the central and western regions than in the less mountainous east. Poverty is highest in households in which the head of household is engaged only in farming (49 percent), as opposed to wage employment (19 percent) or a household business (17 percent).

Although gradual progress has been made since the restoration of independence, Timor-Leste lags behind the rest of the region in achieving the MDGs (cfr Annex 6).

Two out of every four adults in Timor-Leste are illiterate. Access to education has increased dramatically over time, especially for the poor, with net primary enrolment rates reaching about 75 percent. More poor children and more girls are in school now compared to the situation under the Indonesian occupation. However, net lower secondary school enrolment is only 33 percent. About one child in ten never goes to school.

Health indicators are only improving gradually. The mortality rate for children under five has declined from 160 per 1,000 live births in the period 1989-1993 to 130 per 1,000 in the period 1999-2004. Infant mortality is disturbingly high with 88 infant deaths per 1000 live births. HIV/AIDS prevalence is very low, but the population is dangerously unaware of the risks. Considerable interaction between high-risk groups such as sex workers and homosexuals and otherwise low-risk groups create clear bridges to the broader population. Four out of five women have never heard of HIV/AIDS, with the ratio only slightly lower for men. Access to water and electricity is limited, particularly in rural areas, which disproportionately affects poor people. In urban areas, around 70 percent of the population has access to electricity and safe drinking water, whereas in rural areas, access rates are 51 percent for drinking water and 11 percent for electricity. Forty-six percent of the population has no exposure to mass media.

Population growth and movement create formidable challenges for service delivery. At 7.8 children per woman of child-bearing age, Timor-Leste has one of the highest fertility rates in the world. The corresponding population growth rate is estimated at well over 3 percent. If this rate is maintained, the current population of 925,000 is expected to double in 17 years. Moreover, there has been significant urban migration in the last five years, especially to Dili. In rural areas, some people have left the coastal plains where they were relocated by the Indonesian administration to return to ancestral homes in more remote, highland areas. These

factors present tremendous challenges to the delivery of services in health, education, and infrastructure, and enhance the risk of serious environmental degradation.

The combination of a rapidly expanding population, inequality, and slow growth indicate that poverty is likely to increase in the medium term. Timor-Leste faces a *combination* of sluggish growth, rising inequality, and a rapidly expanding population. Unless measures are taken to stimulate growth outside the petroleum sector, non-petroleum GDP growth will at best keep up with population growth, seriously limiting Timor-Leste's chances to achieve the poverty reduction MDG by 2015. In the areas of education, health, and gender, however, the Government is making steady progress toward achievement of the MDGs.

### **Youth**

Providing a future for Timor-Leste's rapidly growing youth population is one of the country's principal challenges. More than 60 percent of the population is under the age of 18, and 25% is between the age of 18 and 29 with this proportion projected to grow. Urban youth unemployment actually stands at 50%. Many youth lack basic skills, as net secondary school enrolment rates are only 33 percent. Encouragingly, rural youth see activities in agriculture, fisheries, and forestry as promising professions, but there is an unmet demand for vocational training. Among young women, the MEASURE DHS (Demographic and Health Surveys) project has documented a drop in age at first marriage and age at first birth, as compared to previous generations. In addition, some of the most serious health problems mainly concern youth. Cases of trauma following road accidents represent 25 percent of hospital bed occupancy, and about half of these are youth under 25. Youth are easily drawn into gang violence, as witnessed by the growth of martial arts groups; fights between such groups have resulted in destruction of property and several deaths since 2000.

### **Gender**

Timor-Leste is determined to overcome the numerous social and demographic obstacles to the promotion of equality and gender balance. Timor-Leste has one of the highest maternal mortality rates in the region, estimated at 420 deaths per 100,000 live births in 1999. Only 45 percent of women are literate, compared to 54 percent of men. Although enrolment rates are equal for boys and girls in primary and lower secondary school, a gender gap emerges in higher secondary and tertiary education. The incidence of domestic violence and sexual assault is high in Timor-Leste. Cases of gender-based violence are being brought to court and have been successfully prosecuted, which represents a significant improvement over the Indonesian era when such cases did not even reach the courts. However, victims face significant challenges in the court system, as witnessed by the large backlog and long processing time of cases brought by women.

Under the new Government the office for the Promotion of Equality has been upgraded as Secretary of State reporting directly to the Prime Minister. Some of the ministers occupying prominent positions in the Government are women (e.g. Minister of Finance; Minister of Justice and Minister of Social Solidarity) and 28% of the Members of Parliament are women, a significantly higher share than in many OECD countries. Still, women in Timor-Leste suffer significant discrimination in many respects. They have higher drop out rates at school, are more illiterate than boys. Women also suffer discrimination at work: they are less likely to work in the formal labour force and they are paid significantly less than men.

Strong cultural biases are an obstacle to women assuming leadership roles and participating in decision making at community and family levels.

### **II.3. The recipient country's development strategy**

Pending the formulation of the Strategic Plan for Economic Development, Timor-Leste's National Development Plan (NDP) and the Stability Programme (SP) developed in 2001 still remain as the Government's vision for national development and represent the country's poverty reduction strategy.<sup>5</sup> Vision 2020, a document formulated alongside the NDP sets out the vision for 20 years for the country.

The development of an effective administrative and governance structure to serve the needs and interests of the people is one of the most critical national priorities. The 4<sup>th</sup> Constitutional Government includes in its organic law a State Secretary for Administrative Reforms. Given the existing environment the medium-term priority programmes will have to be the establishment and strengthening of the organs of state and of public administration, laying the foundations of good governance, creating the avenues for popular and community participation, developing the legal and regulatory framework, building the human resources capacity for policy formulation and execution as well as service delivery, strengthening oversight institutions and fostering relations with the press and civil society.

Because poor people in TL are engaged primarily in agriculture (including fisheries and forestry), improving productivity in this sector is also a high priority. Proposed initiatives include rehabilitation and construction of irrigation systems and their improved operation, introduction of water harvesting techniques, wider distribution of improved seeds of cereal crops, fruits and vegetables, improved livestock health, improved management of fishing, and sustainable management of forests and other natural resources. These initiatives will be undertaken with the participation of the communities that depend on them. Improvements in marketing and infrastructure are also planned.

A critical requirement for poverty reduction is to strongly enhance opportunities in the formal private sector, where growth and employment can be achieved in manufacturing, construction, trade, transport, tourism, and many domestic services. Priority policies and legislation are being formulated to improve the private sector and the ability of TL to sustain both domestic and foreign investment. Poverty reduction cannot occur without the provision of infrastructure that includes an effective network of roads and bridges, efficient seaports and airports, reliable electric power, a telecommunications system, and postal services. Agricultural and business developments are crucially dependent on this infrastructure, and trade, tourism, and foreign investment cannot be encouraged without it.

Currently, standards of education in TL are among some of the lowest in the world. Consequently, the new Government focuses on capacity building for reconstructing and developing the education system – through prioritising strategies for teacher training, increasing primary school enrolment, improving retention rates, modernising the curriculum, and enhancing community involvement in the management of schools. In addition, one of the most difficult tasks for schools in the years ahead will be to extend both on the use of Portuguese language and the standardisation of Tetum for use in schools.

Health priorities are also among the most crucial sector that will require utmost attention. Standards of health in TL are poor, and existing health provision is weak. The focus necessarily will be on the provision and delivery of services to meet basic needs. Existing

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<sup>5</sup> The IV Constitutional Government has recently presented its programme. Priorities for the short, medium and longer term have been set out although their order of importance is not yet reflected in a 5 years investment plan. Emphasis shall be on economic growth, security sector reform, institution building, supporting the return of displaced people, providing youth employment, vocational training, community development programmes, agriculture, infrastructure, health and solidarity with vulnerable groups. This may transform in new Sector Investment Programmes, however, at the time of concluding this CSP there was no further evidence available. Previous sector plans to implement the National Development Policy focussed on basic services, production sectors, infrastructure and governance.

policies focus on ongoing, long-term programmes in child, maternal and reproductive health. They also focus on current needs to build capacity for the provision of support services and management systems for the delivery of these programmes. The recently developed Health Sector Strategic Plan 2008-2012 is a milestone for the implementation of the health policy.

To build capacity to meet all these needs during the coming years is a huge task. Capacity building will be based extensively on government partnerships with civil society organisations, the church, non-government organisations (NGOs), the private sector, traditional institutions, informal networks, and mutual-help groups, particularly at the village level. However, capacity building at the government level will be crucial. The vast majority of current civil servants are neither adequately experienced, nor trained for the roles they will have to undertake.

#### **II.4. Analysis of the viability of current policies and the medium-term challenges**

The National Development Plan (NDP), the Stability Programme (SP) and the road map for its implementation have been considered by the Boards of the World Bank and the International Monetary Fund (IMF) as a poverty reduction strategy. The Joint Staff Advisory Note (JSAN) commended the comprehensiveness of Timor-Leste's planning instruments, but noted that the NDP poverty reduction goals and targets are over-ambitious. While applauding the genuine efforts to link planning and budgeting, the JSAN suggested that planning and budgeting be linked to monitoring outcomes, and that the Sector Working Groups<sup>6</sup> fully develop their monitoring function. It recommended bringing about improved service delivery through institutional capacity building and partnerships. It highlighted weaknesses in governance as an emerging issue and suggested an early focus on the justice sector and customs administration. It stressed the need for the early enactment of measures to improve the legislative and regulatory environment for businesses.

Some important achievements have been made since the adoption of the NDP and the SP. These include the preparation and promulgation of key legislation for improved governance, e.g. a legal framework for petroleum production, taxation, and revenue management that is considered international best-practice and is consistent with the principles endorsed by the Extractive Industries Transparency Initiative; steps to enhance service delivery in the health and education sectors; the maintenance of a relatively sound core financial management system.

But a good deal remains to be done. Far too many people remain in poverty or are vulnerable to poverty and food security.

As international experience indicates that economic growth is the single most important factor that influences poverty reduction outcomes, GoTL plans in the year ahead to launch a major step-up in public spending that, in combination with rising levels of private investment, should lift non-oil GDP economic growth to 7-8% a year from 2010, a rate required to ensure a sustained decline in the incidence of poverty in the country.

While the political vision and strategy of the new Government has clearly highlighted the focal areas for development it will now be important to see how this translates in the envisaged Strategic Plan for Economic Development.

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<sup>6</sup> Joint donor-government sector working groups (SWG) were established under the previous administration for health care, agriculture and basic infrastructure, education and training. As these groups were based on previous sector plans to implement the National Development Policy it would be essential that revision/amendment of the sector plans would be undertaken as a priority in order to have effective continuation of Government-donor coordination (as successfully executed under the Ministry of Agriculture).

## CHAPTER III: OVERVIEW OF PAST AND PRESENT EC COOPERATION, COMPLEMENTARITY AND CONSISTENCY

### III.1 Overview of past and present EC Cooperation

#### ALA Geographical Budget Line, ECHO, EC Thematic Budget Lines (food security and health)

After the emergency phase between 1999 and 2002, EC support has focussed on rural development and health, with capacity building, democracy and good governance as the main cross-cutting issues.

The EC approved contributions to Timor-Leste, since September 1999, amount to € 206.5 million which can be summarised as follows:

- **Humanitarian assistance**, emergency, relief and rehabilitation, food security (including contributions to multi-donor Trust Funds and UN agencies) (€145 million)
- **Rural development** including support for rural infrastructure, private sector employment generation (€34.5 million)
- **Support to the health sector** (€24.5 million)
- **Capacity building** to the line Ministries as well as for education, the judiciary and tourism sectors, and women's leadership, support to elections (€2.5 million)

Cfr Annex 7: detailed breakdown of the above.

Cfr Annex 8: detailed information on ECHO's current programme.

The Commission's approach up to now has been a good example of linking relief, rehabilitation and development. After the initial emergency phase (1999-2002) and with the definition of the 2002-2005 CSP, food security, rural development and health have been the backbone of the EC support while capacity building, gender and good governance have been the main crosscutting issues.

#### Rapid Reaction Mechanism (RRM):

As a reaction to the political and humanitarian crisis of April/May 2006, the Commission adopted on 31 August 2006 measures under the RRM aimed at contributing to post-crisis stabilisation totalling € 4 million. The support package addresses some of the underlying causes and destabilising factors of the crisis and comprises two components:

- a) Support to the national dialogue at all levels of society, with high-level outside facilitation through the Club of Madrid and technical support to the national dialogue process, including local consultation and civic education;
- b) Short-term rural employment schemes ("cash for work" programme), esp. for the urban youth, aiming at reducing tensions among unemployed youngsters, who became a major factor of insecurity during the crisis.

#### EDF funds:

Timor-Leste ratified the ACP-EC Cotonou Partnership Agreement on 19 December 2005. The 9<sup>th</sup> EDF CSP-NIP, which was signed on 9 June 2006, provides an amount of €18 million for the two remaining years (2006-2007) to cover the country's transition from the Asia-Latin America budget line (ALA) to the cooperation assistance under the 10<sup>th</sup> EDF.

### **III. 1.1 Focal sectors**

The areas of concentration of the ALA CSP-NIP (2002-2005) were food security, rural development and health.

The 9<sup>th</sup> EDF CSP-NIP (2006-2007) areas of concentration were rural development and institutional capacity building with an allocation of respectively € 12 and 6 million. However, in view of the crucial importance of institutional capacity building and the improvement of public financial management systems, it was agreed with the NAO to revise the allocation and allow a transfer of € 2 million to institutional capacity building, thus reducing the amount available for rural development to € 10 million. The allocation of € 8 million to institutional capacity building has been directed to three projects:

- Reinforcing NAO capacities to perform and fulfil its responsibilities as set in the Cotonou agreement and reinforcing the capacity of the Ministry of Development on trade aspects and developing a trade policy (€ 3 million);
- Support to improve systems/processes and strengthen institutions in the field of election (€ 1.5 million as contribution to a UNDP-managed multi-donor project);
- Institutional capacity-building and improvement of management systems in Public Financial Management (€ 3.5 million as contribution to the World Bank administered Planning and Financial Management Capacity Building Programme (PFMCBP, multi-donor trust fund).

The rural development programme (RDP III) shall build on the experience of previously financed support schemes and complements the EC's ongoing Rural Development Programmes (RDP I in 2003 and RDP II in 2006) under ALA as well as the nutrition and food security programmes. Its overall objective is to contribute to poverty alleviation and socio-economic development in particular in the poorer areas of Timor-Leste. Target groups shall be the underprivileged rural poor, including women, youth and otherwise impoverished people. The programme will focus on sustainable agriculture production, diversification and rural infrastructure rehabilitation. It also stresses the need to continue institutional capacity building to the Ministry of Agriculture and Fisheries (MAF) and other key line ministries. RDP III received a favourable opinion at the EDF Committee of 24/10/07 and the related Financing Agreement was signed on 24 November 2007.

#### **Lessons learnt from past EC cooperation in focal sectors**

Lessons learnt have been sourced mainly from the evaluation of the Trust Fund for East Timor (TFET) (2004), mid-term evaluation of RDP I, from implementation reports and EAMRs. After the initial relief phase, the main areas of EC cooperation have been rural development, health and capacity building.

The Commission has followed a clear-cut strategy of financing the Trust Funds established to assist the UN missions and the multi-donor Trust Fund managed by the World Bank (TFET). This has facilitated both implementation and coordination, and avoided fragmentation of aid whilst providing support for a new and weak administration. Programming jointly with other donors also ensures complementarity of aid.

An interim evaluation of TFET took place mid-2004 and concluded that "most of the infrastructure rehabilitation needs identified by the Joint Assessment Mission and the joint donor sector missions had been completed. Basic levels of services in health and education had also been restored. It is (though) a relative success because the mechanism did not significantly improve the country's low institutional capacity and failed to develop Timorese ownership of the reconstruction programme".

A major lesson learnt after the crisis in 2006 is that while state building initiatives are crucial, delivery of services to the citizens should not be disregarded. The EC cash for work programme as well as the Skill and Vocational training financed by the RRM have demonstrated the possibility of creating employment while implementing quick impact initiatives.

The following are common **lessons learned** from previous ALA funded programmes:

1) The need for a **comprehensive approach in rural development**: Farming is the sole source of income for about 80% of rural households, and will remain the main source of employment and income for the majority of the population for the foreseeable future. Past programmes demonstrate that upland and dryland areas which produce the bulk of food supplies these areas have responded well to investments aimed at improving food security and increasing productivity in the Eastern rural part of the country, provided that the necessary plans and resources are deployed. The previously-supported pilot project could now be extended to other part of Timor-Leste and other poor upland and dryland areas. A project which started recently is targeting 2 districts in the Western Region. It is now important to tackle impediments to a further increase in productivity through training, use of new technologies, improvements in water infrastructure as well as in rural roads in order to transport the goods produced to the markets. Also the capacity of community based organisations and water user organisations need to be improved.

2) Support to the **health sector**:

**Support to policy development from the start.** Policy planning and infrastructure rehabilitation went hand in hand in EC's support to the health sector in order to ensure a coherent development of a potentially long-lasting, sustainable health system. As a major result a health sector strategic plan, a medium-term expenditure framework and a long-term human resources plan were developed. Hospital construction is going ahead in the 4 sites and slight delays are observed in Dili, Maliana and Maubisse, while Oecussi is ahead of time. The construction of 3 hospitals (Oecussi, Maliana and Maubisse) is scheduled to end in 2007 while the rehabilitation of the Dili hospital should end in 2008.

Whilst spending has accelerated due to the hospital construction, the health activities indicate uneven results in terms of vaccination and health care coverage. District planning has to be strengthened and be more focused, while the work force analysis needs to be updated in the face of the substantial support of Cuban doctors operating at sub-district levels. The 400 Timorese medical students in Cuba and their future placement in sub-districts will further change the situation, as well as the current tasks of the nurses. At the same time risks and assumptions need to further be taken into consideration due to the increasing private health services and the possibility that trained doctors may opt for the private sectors.

3) **The need for continued institutional capacity building** to the Ministry of Agriculture and Fisheries (MAF) and other key line ministries such as the Ministry of Finance, Ministry of Economy and Development, Ministry of Tourism, Commerce and Industry. The EC has provided capacity building either for operations aimed at facilitating investments or special capacity building programmes aimed at providing assistance for specific gaps (like budget execution) in the frame of their focal areas of rural development and health. Capacity building did not address the wider scope of governance, accountability and supporting check and balance institutions. Training and capacity building will remain important for Timor-Leste with huge training needs of Timorese civil servants (including language, skills training and specialised training abroad). Since institutional capacity building requires a good deal of coordination and long-term planning, it is best provided in close coordination with other donors.



### III.1.2 Projects and programmes outside focal sectors

The 9<sup>th</sup> EDF CSP-NIP did not foresee any provision for projects outside the two focal areas. In the ALA CSP-NIP (2002-2005) the non focal areas were capacity building, gender and good governance.

Common **lessons learned** from previous EC supported programmes outside focal sectors:

**1) Gender.** There are still many barriers to local rural women participating in secondary and informal education, and in benefiting from rural development programme activities. These barriers include social taboos, the low status of rural women and their domestic and reproductive work loads. Agricultural extension workers must include women who speak the local dialects.

**2) Governance, Democracy/ and conflict prevention.** Equal opportunities to voting access and the general concepts of the importance of participation and representation are key areas to achieve empowerment of minority groups, women and the disadvantaged. Recent recommendations by the EU Election Observation mission of the 2007 elections have pointed out the need for supporting a national civil register system which will be very important for the electorate registration. Support to electoral complaint institutions is another key area for the establishment of accountable elected institutions, and very much linked to the promotion of the rule of law, and long term stability. The country's ability to manage public finance efficiently, transparently and to deliver basic services to the poorer areas will be crucial to long term stability.

### III.1.3 Utilisation of Envelope B

There was no B-Envelope allocated to Timor-Leste under the 9<sup>th</sup> EDF.

Emergency humanitarian needs of the country were taken care of by ECHO. Its objective has been to act in the short-term to contain and reduce the prevalence of acute malnutrition.

ECHO has been involved in fighting malnutrition since October 2003, when it restarted its programmes in Timor-Leste in response to a Government's appeal for international aid launched after some severe food shortages in 2003. ECHO's response was channelled through several decisions including food aid, nutrition and agricultural rehabilitation, targeted supplementary and therapeutic feeding. Projects in 2005 were targeted to more than 100,000 people. During the mid-2006 crisis, some of these programmes were reoriented to directly benefit the IDPs.

Actually, ECHO is still addressing the emergency humanitarian needs of the Internally Displaced Persons (IDPs). In 2007, due to still large numbers of IDPs and the volatile security situation ECHO has been supporting the country with € 3 million (€ 1 million for food distribution; € 0.5 million for food production in rural areas; € 1.5 million for 3 projects to NGOs and IOM for water and sanitation and for reintegration of displaced into their communities).

Projects in support of the IDPs target the needs of the population in food aid, nutrition and hygiene education, small-scale food security projects, as well as water and sanitation infrastructure. As the ongoing crisis is expected to have an adverse effect on malnutrition and food security, further short-term interventions may prove necessary to cope with the most immediate acute needs. A recent WFP assessment of the nutrition situation in Dili concluded that 25,000 people are at risk to lives and need immediate assistance. A total of 11% of children under 5 years suffer from acute or moderate malnutrition.

However, short-term impact humanitarian actions need to be complemented by longer term (development) efforts addressing the underlying causes of malnutrition to have a sustainable impact. Once the longer-term food security and rural development projects start producing results, ECHO plans to discontinue provision of humanitarian aid in the sectors of nutrition and food security.

### **III.2 Information on the programmes of the Member States and other donors (complementarity)**

In addition to the multilateral agencies, there are 19 main bilateral donors in Timor-Leste, though not all are physically present. The EC is the fourth largest donor after Portugal, Australia and Japan<sup>7</sup>, while the EC and the Member States combined represent about half of the overall contributions made so far to Timor-Leste. Portugal is particularly active in the education sector (together with Australia and Japan) and on governance and the justice sector. Ireland and Sweden are present in the governance sector. UK is together with Ireland and Sweden providing commodity assistance. Germany provides assistance to rural development in the frame of the EC rural development programme II.

Division of labour is well reflected with EC being the major donor in rural development and together with Australia and United States a major donor in health. Donor coordination is particularly relevant in institutional capacity building and, to that respect the EC has set some clear priorities for this support without overlapping with other donors.

Since December 1999, there have been six-monthly and, since 2004, yearly donor coordination meetings, during which bi- and multilateral donors and NGO's meet and discuss in order to enhance coordination according to GoTL priorities and avoid overlapping or conflicting activities in the sectors or regions.

In order to ensure the effectiveness and the impact of EC development assistance, it will be necessary to continue the already close co-ordination with other donors, in particular with EU Member States, with other major donors such as Australia, USA, Japan, UN agencies, WB and IMF. Coordination has been increased among the EU Member States still present in Timor-Leste (Portugal, Ireland, Spain, France and Germany through GTZ) through the sharing and discussion of cooperation priorities, the sharing of cooperation data, presentation of identified priorities during EC financed missions and workshops, preparation of the human rights fact sheet, preparation of a strategy for supporting human rights defenders etc.).

Complementarity among Member States and the EC has been achieved mainly in the common participation and financing of TFET, managed overall by the World Bank. Coordination has been particularly active in the preparation of the Stability Programme, the Sector Programmes and Sector Working Groups which were recently established by GoTL. The joint participation in the Consolidation Support Programme, although the EC is only observer, helped to prepare a shared monitoring tool and to prepare for the EC sector support. This close coordination among donors has assisted GoTL in preparing its sector programmes.

There is need for further coordination with other donors in areas of EC concern which can not be tackled by this strategy (such as areas of energy policy and statistics).

It is now confirmed that TL is eligible for the US Millennium Challenge Account (MCA). Components and amounts have not yet been decided.

Cfr Annex 9: Donor matrix

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<sup>7</sup> The last available donor matrix from beginning of 2006 attached in Annex 9 presents EC still as third largest donor.

### **III.3 Other EC policies**

This CSP is fully compatible with other EC policies. As far as trade policies are concerned this relates to the effective participation of Timor-Leste in international trade fora and agreements, in particular WTO, the promotion of the trade dimension in the national development plan and capacity-building for the line ministry responsible for trade. Timor Leste has applied for membership in the *Integrated Framework process*, which suggests the will to integrate trade policy into its national development plans and to improve the trade governance structure. A diagnostic phase was planned to start in October 2007.

As far as agricultural and fisheries is concerned, the rural development programme should ensure that activities are fully compatible with EC policy, and attention will also be paid to current guidelines on transport and energy, which will also be addressed in the context of rural development.

Wherever relevant EC policies/guidelines concerning cross-cutting issues such as human rights and democratisation, gender, conflict prevention/security and the environment have been taken into consideration, and efforts have been made to create synergies between the national development plan, the proposed strategy, and the programmes of other donors.

In line with the EU commitments on policy coherence for development some of the non direct aid policies are of particular relevance to developing countries and may need certain adjustment measures.

Agriculture remains a priority of the development agenda of the country. Within the framework of the EU Common Agricultural Policy the EU has committed itself to substantial reductions of trade distortion. At this juncture trade of Timor-Leste with the EU is at a very small level (some coffee) and should not be negatively affected. Timor-Leste as an LDC will also benefit from "Everything but arms" conditions. Potential agricultural exporters may need at some time in the future assistance in meeting the high sanitary and phyto-sanitary standards of EU markets in order to get improved market access to European markets.

The country will have to actively use research and technological developments of the past in order to make informed planning and decision making at different levels. Enhancing science and technological capabilities (S&T) have to be pursued wherever possible within the planned programme.

The need for stable, secure and sustainable energy supply has to be addressed through the development of a national energy policy with support of policy and planning capacity in the relevant Ministry. In that respect, the EC will promote the formulation of a national energy policy at the donor coordination forums in the country.

Economic planning through improved statistics is another area of importance for EC. Within the PALOP programme statistical support has been rendered in the past. The new PALOP/Timor-Leste programme on governance initiatives could take up a statistical support programme as a contribution to economic governance.

### **III.4 Description of the political dialogue with the partner country**

The Commission has noted with satisfaction that Timor-Leste shares EU vision on the importance of good governance which includes the sound and transparent use of public finances, the commitment to improve the delivery of quality public services including in the judicial area and to guarantee equitable access to social services for the poorest parts of the population. In this context, the Commission can only but commend the government's decision to set up a state-of-the-art Petroleum Fund under Parliamentary scrutiny to manage and distribute in a sustainable fashion the present and future oil and gas resources that Timor-Leste expects.

The EC support to the national dialogue during the crisis and the support to the elections including the EU Election Observation Mission have been a qualified assistance in this dialogue.

The Cotonou Agreement, which Timor-Leste ratified in December 2005, foresees in its article 8 also political cooperation through a regular and structured political dialogue. Due to the limited presence in the country with only an antenna office there is at present no regular and structured political dialogue. With the envisaged opening of a fully fledged Delegation political dialogue should become a regular feature. The country is invited to take advantage of such an opportunity to discuss ways in which the EC can support the country's democratic transition from a post-conflict situation to sustainable development in the framework of a strengthened EC-Pacific Islands strategic partnership.

Some discussions already took place concerning the accession to possible additional resources from the "incentive tranche" of the 10<sup>th</sup> EDF based on commitments to reforms or governance criteria.

### **III.5 Description of the state of the partnership with the recipient country and progress towards harmonisation**

Since the restoration of independence, Timor-Leste's development cooperation is characterised by a strong partnership with donors. GoTL has taken firm leadership over the coordination of development activities and chaired the Timor-Leste and Development Partners Meeting (TLDPM) with the assistance of the World Bank. This close coordination with donors has greatly assisted GoTL in preparing its Sector Programmes.

The participation of the EC, even though only as observer, in the Consolidation Support Programme (CSP), a budget support operation of several development partners (including some EC Member States) coordinated by the World Bank and one of the main instruments of monitoring and policy dialogue between GoTL and its development partners, helped to prepare for the EC sector support. EC will be co-funding the World Bank funded Public Finance Management Programme which could further improve the basis for sector or budget support operations in the country. Under UNDP guidance the EC like many other donors was involved in the election observation of the presidential and general elections in 2007.

Cfr Annex 12: Harmonisation road map

Continued emphasis on donor coordination will be crucial as the Whole-of-Government approach had deepened upon active engagement on the part of a broad set of development partners who together support the government in implementing its (own) policies.

## **CHAPTER IV: EC RESPONSE STRATEGY**

### **THE STRATEGIC CHOICES FOR EC COOPERATION**

The EC response strategy is derived from the economic, social and political analysis of the local context, the government strategy and activities of other development co-operation partners, taking into account the views expressed by civil society groups. See Annex 15 "CSP Drafting Process".

The response strategy supports GoTL's National Development Plan. It has been derived from Sector Investment Programmes in agriculture and health which have come under revision following the establishment of a new Government. The government aims at a new Strategic Plan for Economic Development. The sectors of concentration under the EC response strategy

have been selected and maintained with the new Government's consent following the approval of the political programme 2007-2012 in the national parliament. The choice of three focal sectors is justified by the amount of the CSP, the needs of the country and the presently low absorption capacity. The strategy takes also account of the exceptional situation of the country, where any assistance measure is difficult to implement and doomed to failure without improving GoTL's own capacity to manage its country in the future and creating an enabling environment through institutional capacity building. A total of € 63 million are available for this strategy for the period 2008-2013.

It also takes account of some of the underlying causes which contributed to the crisis in Timor-Leste as mentioned in the analysis of the political and institutional situation of the country. These are amongst others the failure of previous Governments to engage with the people, unhealed wounds of the past, demand for justice and poverty. A further analysis of the root causes of instability and follow-up activities as well as recommendations and follow-up activities how to use petroleum wealth for a sustained pro-poor development are essential and part of the EDF or any other instrument could be used for this.

### **FOCAL AREAS**

Assuming that the present crisis subsides significantly by early 2008, the main areas of concentration for the 10<sup>th</sup> EDF shall be:

- **sustainable rural development** conceived as a programme-based approach supporting the implementation of the Ministry of Agriculture and Fisheries (MAF) "Policy and Strategic Framework" programme as well as the programme of the Ministry of Infrastructures;
- **health** in order to support the huge needs of the health sector as outlined in the recently developed Health Sector Strategic Plan (HSSP) 2008-2012;
- **institutional capacity building** within the Executive, particularly the State Administration and in the institutions which are responsible for checks and balances such as the Parliament and the Judiciary.

**A. Sustainable Rural Development:** Agriculture and livestock make up 80% of all self-employment and account for one fifth of non-oil GDP. 30% of households rely on subsistence agriculture alone and are facing food insecurity every year. While the MAF ranks food security as the country's first priority, food production is the only sector of the economy outside the petroleum sector which can bring economic growth and therefore contribute to sustainable poverty reduction and unemployment reduction. Any significant improvements in food security will only come from increased efforts in upland and dry land areas, which produce the bulk of food supplies, but remain the poorest in the country.

The challenges the country faces in the rural sector are inextricably linked and it is therefore critical to adopt a broad-based cross-sectoral approach including various ministries beside MAF with the Ministry of Infrastructures for rural roads, Ministry of Natural Resources for water resources and electricity and Ministry of Economy and Development for support to the private sector.

The Government took steps to improve inter-sectoral planning and coordination and recently a State Secretary for Rural Development has been established within the Ministry of Economy and Development.

To improve agricultural production through services delivery in rural areas, one will have to support the MAF decentralisation process and to address unemployment and acute problems of low rural productivity in a more sustainable way. This will serve at the same time both food security and economic growth purposes.

The sustainable rural development component of the 2008-13 NIP will build on the experience of former EC programmes in the same sector and will complement the Commission's ongoing Rural Development Programmes as well as the Nutrition and Food Security programmes. Besides agriculture related activities geared towards increasing production, the programme will contribute to the creation of an enabling environment which will increase productivity and economic growth as it will improve access and rural roads, supply small scale hydro-electric plants and solar panels and implement rural water supply schemes.

**B. Health:** EC has supported the health sector in policy planning and in infrastructure rehabilitation. The Health Sector Strategic Plan (HSSP) and related Medium Term Expenditure Framework (MTEF) developed in the ongoing EC funded Health Sector Investment Programme (SIHSIP) has been disseminated to partners in September 2007. These documents will be agreed upon by the Ministry's Council of Coordination and will contain well defined mechanisms for donor coordination. The needs of the health sector as outlined under the HSSP are huge and the health indicators of the population are still alarming (maternal mortality, child mortality). Decentralisation of health services is hampered by efficient service delivery (lack of medical and administrative staff). EC support (whether project support or budget support) would support the delivery of health services throughout the country at the district level and below. High priority target groups would be women and children. The EC support under the 10<sup>th</sup> EDF should be seen in the context of longer term development needs over a period of 10-15 years.

**C. Institutional capacity building** (cfr also to Annex 10): Institutional capacity-building was selected in order to further enhance the administrative capacity of the government as supported under the country strategy for the 9<sup>th</sup> EDF. Fostering sustainable growth and poverty reduction will depend on strengthening capacity in key areas, such as state administration and justice. Though the Government has made great strides, institutional capacity remains weak. The vast majority of current civil servants are neither adequately experienced, nor trained for the roles they will have to undertake. Low levels of education and professional experience have led to a shortage of technical expertise. The scarcity of skills in accounting, auditing, economics, and legal drafting has been reflected in the Government's difficulties recruiting qualified personnel across sectors. In addition, the administration is still highly centralised, which inhibits the development of capacity and responsibility and reduces government effectiveness.

In October 2006 GoTL under the aegis of the Ministry of State Administration launched a wide-ranging reform policy on decentralisation and local government. GoTL has vowed to provide the municipalities with sufficient human resources and fiscal revenues to enable them to effectively contribute to the realisation of the country's development objectives. Although the election process during 2007 left the decentralisation programme on a slower pace the new Government is continuing the programme through a revision of policies and their implications in terms of human resources needs.

The judiciary is almost fully dependent on the international community for lawyers and training. It is still incomplete – some courts, such as the Supreme Court or the High Administrative, Tax and Audit Court, have not yet been established – and is to be regarded as the weakest branch of TL's governance architecture. Various efforts have been made to improve the judicial sector, including the appointment of international judicial officers, setting-up a Judicial Training Centre for training and evaluation of court actors. But much remains to be done to translate the governance architecture set out in the Constitution into a well-functioning and fully autonomous judicial system.

Strengthening the functioning of the National Parliament is a task which the international donor community has largely neglected until now. Even though constitutionally the Parliament has a pre-eminent position in the national system of governance, in practice its role and influence is limited due to a number of constraints.

Further support for NAO's office which started under the 9<sup>th</sup> EDF shall be funded in order to further strengthen the capacity of the Ministry to deal with EDF projects and help increase the absorption capacity of the country.

Communication within institutions, across them and interaction with the wider population remains very weak. The crisis has demonstrated that in the absence of information, the population tends to react and act according to underground and parallel rumours as during the resistance period. Institutional capacity building should therefore include support to communication services.

The present strategy proposes to address these capacity development needs, either in the context of sector programmes through selected ministries (MAF and MoH in the context of related EC programmes) or through specific capacity building programmes/projects for the benefit of other ministries (e.g. State Administration, Justice) and other pillars of the state such as the Parliament and the Judiciary.

## **SUPPORTING STRATEGIES (NON-FOCAL SECTORS)**

### **Support for Non State Actors (NSA)**

The possibilities for GoTL to adopt participatory approaches are limited. Civil society is only emerging and in a process of development. Civil Society Organisations (CSOs) are rather fragmented and suffer from the same challenges of infrastructure, communications and language barriers as all other sectors. The crisis has also shown the vulnerability of some of them to partisanship.

EC support will focus on capacity building for the Network of Community Based Organisations (CBOs) with a view to enabling them to improve their code of conduct, their organisational and managerial set up as well as on strengthening the institutional capacity of relevant CSOs with a view to enabling them to engage in a meaningful policy dialogue with both the State and elected bodies for enhanced democratic governance. Criteria for a representative participation in the network will be applied.

Support to NSAs engaged in service delivery could also be envisaged. Gender equality, HIV Aids awareness and environmental awareness issues will be taken into account.

Support to the private sector may be given for capacity building of private sector associations in order to support emerging businesses.

### **Technical Cooperation Facility**

The TCF is an essential instrument for the support to the Government and the EC Delegation in preparing the financing agreements and for wider programmatic issues, including evaluation. Capacity building on trade, which started under the 9<sup>th</sup> EDF, should continue to be supported in order to enhance the export potential of the country and in view of a possible integration into the Pacific EPA. Assistance with statistical reporting in close cooperation with the National Statistics Directorate (Direcção Nacional de Estatística) and the relevant sectoral Ministries may also be supported.

### **PALOP/Timor-Leste Governance based Initiatives:**

In continuation of past EC PALOP cooperation, activities in support for the area of governance will be considered. The five PALOP countries and Timor-Leste have a strong shared identity based on history, culture, language, heritage (including similar systems of public administration, justice, public finance management, inter-linked labour markets and social services) and have interest to enhance collaboration and exchange on their own contexts, specificities and experiences in these fields.

Against this background and with the experience gained from past interventions and the analysis of capacity and common needs, support in form of common projects will be considered in particular in the areas of political (democratic and rule of law), economic and social governance as well as government effectiveness.

Special emphasis will be placed on joint capacity building actions as enabling factor for facilitating successful implementation of national development and poverty reduction strategies, including through effective delivery of public services, particularly to the benefit of the poorer strata of the population. In these areas, the PALOP countries and Timor-Leste will continue to benefit from sharing experience and knowledge, as well as developing jointly replies to commonly identified needs.

### **CROSS CUTTING ISSUES**

Cross-cutting issues, notably gender equality, the promotion of human rights, children's rights and the rights of indigenous people, environmental sustainability and combating HIV/AIDS, require special attention and will be mainstreamed in each focal sector.

There is a need to integrate a gender perspective into the government's food security policies to ensure that the needs of malnourished women and children are equally addressed. Women and children will be high priority target groups in the health sector support programme.

Environmental degradation is a significant problem in the countryside because of the wide spread of "slash and burn" farming technique. The rapidly growing and dispersing population puts tremendous pressure on agricultural land, much of which is situated on steep slopes and this trend is exacerbated by accelerated deforestation following the substitution of kerosene by firewood. The sustainable rural development programme geared towards improving agricultural productivity will promote environmentally sound techniques.

The prevalence of HIV/AIDS is presently very low but the population is dangerously unaware of the risks. Four out of five women have never heard of the disease with a ratio only slightly lower for men. Raising the awareness of people concerning HIV/AIDS could be done through appropriate health education and agricultural extension activities.

### **RISKS OF THE RESPONSE STRATEGY**

Sustainable rural development: It will imply inter-sector planning and coordination as many factors constraining agricultural productivity and related downstream activities such as marketing and processing fall outside the mandate of the Ministry of Agriculture and Fisheries. Much remains to be done to develop effective supra-ministerial and donor coordination of sectors in rural development. It includes transport, water, energy, credit, education, private sector involvement and health.

The development of the agricultural sector hinges critically on policies that allow wages and prices to remain flexible and to adjust to economic conditions. This is particularly important for agricultural exports. Wages are relatively high compared to other countries in the region particularly given low labour productivity. This limits the competitiveness of domestic



products on both national and export markets and tends to discourage large-scale labour-intensive foreign investment.

Health: Within the health policy framework, care is needed to ensure that inadequate expansion in facilities and services level does not undermine the sustainability of the health system. A significant issue of funding recurrent costs is emerging. In trying to overcome the problem, both the Ministry and donors will have to cooperate: there is a need for the Ministry to cut costs through improvements in efficiency and to seek retaining the involvement of donors for a longer period in funding some aspects of the operational costs of the publicly funded health system.

Institutional capacity building: Donor support in the field ought to be better coordinated than in the past, both in terms of programmes and approaches. The pre-Independence experience has shown that the heavy reliance on expatriate advisors to provide one-to-one training and skills transfer has had significant limitations both in terms of coverage of the civil service and cost-effectiveness. It is the reason why since the restoration of Independence, the government has placed increasing emphasis on a two-track approach to capacity building that focuses on both individuals and institutions. Building the skills of a limited number of individuals is not sufficient to meet the capacity building needs of the public service as a whole.

Another element of key importance for the effective implementation of the 10<sup>th</sup> EDF will be that adequate capacity will be in place in the NAO's office. It remains to be seen how the recently started Institutional Capacity Building Programme will influence the work in the Ministry of Finance and how it will be integrated in the Ministry. At present the NAO's office has only a very limited number of key support staff. For the smooth and timely implementation of the 10<sup>th</sup> EDF, the GoTL would need to adequately address these issues.

Finally, the smooth and successful implementation of this programme needs a fully functional Delegation. The Delegation is about to be opened but it needs to be fully operational in 2008 to allow a proper assistance in the timely implementation of the projects.

## V. ANNEXES

### V.1 POLITICAL TRANSITION IN TIMOR-LESTE

Occupying the mountainous eastern half of the island of Timor, Timor-Leste was a Portuguese colony for 400 years. Following a brief civil war, the country unilaterally declared its independence on November 28, 1975. Within days it was invaded and illegally occupied by neighbouring Indonesia. For 24 years the population of Timor-Leste maintained a staunch resistance against the invasion, characterised by near universal popular support and effective coordination between the armed wing of the resistance, Falintil,<sup>1</sup> an elaborate and active network of civilian supporters, “clandestinos”, and representatives in the diaspora. One-third of the population is estimated to have died as a result of the occupation. Following the fall of President Suharto in 1998, Indonesia offered to hold a referendum allowing the territory a choice between autonomous status or an independent state. An overwhelming majority of Timorese voted for independence. Tragically, the referendum was accompanied by a well-planned campaign of violence led by armed militia. The violence left over 1,000 people dead, the majority of the population displaced, and most of the private and public physical infrastructure in ruins.

Following the intervention of a multi-lateral peacekeeping force, the United Nations Transitional Administration in East Timor (UNTAET) was established with supreme executive, judicial, and legislative authority. At its height, UNTAET included almost 9,000 uniformed and civilian personnel. To ensure Timorese participation early on, the National Council, a quasi parliamentary body representing different segments of Timorese society, was created in 2000, as well as the first transitional Government consisting of four Timorese and four international cabinet members. In 2001, elections were held for a Constituent Assembly. The elections were won by Fretilin,<sup>2</sup> which gained 55 of the 88 seats in the Assembly, short of an absolute majority, and all in all 11 parties won representation. A second transitional Government was formed, now composed entirely of Timorese. Following the adoption of the Constitution, presidential elections were held in April 2002 and won by independence leader and Falintil Commander Jose Alexandre (Xanana) Gusmao. The Democratic Republic of Timor-Leste fully restored its independence on May 20, 2002. The Constituent Assembly became the National Parliament, and the current Government, formed by Fretilin, was sworn in under the leadership of Prime Minister Mari Bim Amude Alkatiri. A 900-person United Nations Mission of Support in East Timor (UNMISSET) was created, focused primarily on peace-keeping, training and support to the Timor-Leste police force, and the deployment of advisers to Government and other State institutions. On May 20, 2005 UNMISSET was succeeded by the United Nations Office in Timor-Leste (UNOTIL), now reduced to about 120 civilian and police advisers.

Since the restoration of independence, Timor-Leste has relatively maintained peace and political stability, and established security. Despite differences in opinion and

style, the President, Government, and security forces have consistently worked together toward these goals.

The country's stability has been seriously disrupted once, by riots in Dili in December 2002 following the shooting and killing of two demonstrating students by police.

Stability was tested again during a three-week demonstration organised by church leaders in April/May 2005, yet the demonstration remained largely peaceful and showed the police forces capable of restraint and professionalism. Elections for village councils have been conducted in January 2005.

For the 3<sup>rd</sup> time, unrest in Timor-Leste started again in February 2006, when hundreds of soldiers left their barracks and went on strike. Originating mostly from the western part of the country, the soldiers complained of regional discrimination in the attribution of promotion, which allegedly benefited soldiers originating from the East. At the end of April 2006, demonstrations by former soldiers ended in rioting, with several injuries and deaths, as well as property damage. The security conditions deteriorated significantly in some parts of the country, including the capital, and, at the request of the Government, Australia, Malaysia, New Zealand and Portugal sent on 26 May troops to help restore order.

On 26 June 2006, Prime Minister Mari Alkatiri resigned from office and Jose Ramos-Horta, former minister of Foreign Affairs was appointed as a new PM by the President on 10 July 2006. Both the President and the new PM committed themselves to achieving reconciliation without sacrificing accountability for crimes committed during the past months.

During the months of April to June 2007 presidential and general elections were held. International observer missions – one of the largest missions was provided by the EU – were by and large satisfied with the elections. The EU election observation mission declared them as credible and genuine.

The Presidential elections were convincingly won by Ramos-Horta who was sworn in as new president of the country.

In the parliamentary elections seven out of 14 parties/coalitions gained seats (65 in total) and none of them won the absolute majority. President Horta nominated Xanana Gusmao as Prime Minister (PM) and asked him to form a coalition. The strongest party Fretilin (21 seats) declared the process of forming the government unconstitutional. As the strongest party they felt they had the right to form the Government. The decision to appoint Gusmao as PM led to several security incidents. The announcement of the new Government triggered public disturbances with violent demonstrations mainly in the Eastern districts (Baucau and Viqueque).

In September 2007 the Government presented a 5 year programme with priorities in economic growth; reform of state management; human resources development; solidarity, health and social protection; infrastructure; strengthening democracy; defence and foreign policy.

Recognising the fragility of political unity and the necessity of healing past divisions, the leadership and communities have taken important steps to foster dialogue and reconciliation. The Commission on Reception, Truth, and Reconciliation has used customary mechanisms to bring about community re-integration of perpetrators of low-level violence during the 1999 events. Since 2006, a Commission for Truth and Friendship (CTF) co-chaired by Indonesia and Timor-Leste has had several hearings and its report is expected by January 2008. The National Dialogue, initiated by the President, has involved a series of local and national level public meetings on the role of the UN in an independent Timor-Leste, local government, justice, and veterans. The leadership has also taken important steps to recognise and honour veterans of the resistance as called for in the Constitution. Acknowledging the potentially destabilising effect of disillusionment among veterans and the broad community demand for their recognition, the President appointed three commissions to register veterans of the armed and civilian resistance. On the basis of the work of the commissions, Parliament has recently approved a veteran's law that will establish recognition measures.

Civil society and media play a constructive and increasingly important role. Much like political leaders and Government, civil society has had to make the difficult transition from resistance against the Indonesian occupation to effective participation in nation building. A number of non-governmental organisations (NGOs) undertake useful monitoring, advocacy, education, and advisory services in the areas of human rights (Associação HAK), justice (Judicial System Monitoring Programme), gender awareness (Fokupers, Rede Feto), the environment (Haburas), and international assistance (Lao Hamutuk). As 98 percent of Timor-Leste's population is Catholic, the Church is very influential and plays an active role in conflict mitigation and service provision. The print media in Timor-Leste have grown from non-existent under Indonesian times to several daily and weekly newspapers, but only a small proportion of the population has access to them. National and community radio, on the other hand, reaches a wide audience and provides a popular forum for interactive debate.

Poor outreach on the part of Government may contribute to Timor-Leste's vulnerability. Effective communication and genuine participation are critical to shoring up popular support for the national development process, and for avoiding conflict. Many of the positive and necessary development outputs of the last three years, such as policies, laws, and the completion of institutions, are largely invisible to the electorate. At the same time, service delivery results are mixed. Expectations of prosperity following the restoration of independence are high, but the Government neither has the resources nor the intention to re-establish the paternalistic State maintained by the Indonesian occupation. Yet the Government is hesitant to collaborate with civil society and maintains a "statist" style. It has not yet succeeded in engaging constructive critics or in maintaining an effective dialogue with communities. While both Portuguese and Tetun are national languages, critical documents are often only published in Portuguese, which only a small fraction of the population understands. Government is increasingly recognising the importance of

consultation and information dissemination and has, for example, established a public information office and recently undertaken extensive public consultations on the petroleum revenue savings policy and the associated Petroleum Fund.

Despite considerable progress, the current stability in Timor-Leste is fragile, and the country remains vulnerable to conflict. While limited in number, the hard-core militia remaining in West Timor poses a real, if small, risk of externally generated conflict. Since 2002, there have been several incursions by militia in which Timorese villagers have been killed. More significant than external factors are internal fault lines contributing to the risk of renewed violence, including declining income, increasing poverty, high unemployment, and emerging corruption. Rapidly expanding youth cohorts and high youth unemployment have fuelled an expansion in martial arts groups. There are a number of relatively small, but vocal groups who reject the legitimacy of the Government and some former members of the resistance continue to feel disenfranchised. While steady improvements have been made, the security forces still lack professionalism and experience. There have also been several serious altercations between the forces themselves, causing significant public concern. While no one of these factors is likely to ignite serious conflict, their combined effect remains unpredictable.

## V.2 DEVELOPMENT OF TRADE IN TIMOR-LESTE

The following are some of the constraints to trade that have been identified:

- Terms of trade are affected negatively as flexible management of monetary and interest policy is not possible (USD currency)
- High factor costs of production as expensive e.g. local skilled labour, high energy, water and transport cost
- Poor rural market facilities and poor rural access roads limit domestic trade, and lack of microfinance has led to a cash based economy.
- Enterprises are predominantly micro and small and medium sized enterprises (SMEs), most work under donor funded government contracts
- The domestic market is negligible in terms of volume and purchasing power.
- The concentration of businesses around Dili reduces opportunity for rural employment
- A complicated business registration procedure and corporate taxation system further reduce investor interest
- Poor port and road infrastructure increases the cost of production
- Lack of skills in terms of craftsmanship and management, and in agricultural production (quality cannot be guaranteed) and difficulties with complying with international standards.

The following facilities could be of particular interest to Timor-Leste in boosting trade and investment:

- € 110 million programme (under 9<sup>th</sup> EDF) to promote foreign direct investments and entrepreneurship (PROINVEST, managed by the Centre For Development of Enterprise (CDE), including support for:
  - o Investment and technology flows to enterprises
  - o Intermediary organisations and professional associations
  - o The development of enterprise partnerships
- € 20 million Enabling Environment Facility (9<sup>th</sup> EDF)
- € 30 million FISH 2 to assist in meeting sanitary standards and development in the fisheries sector (9<sup>th</sup> EDF)
- € 30 million Food and feed programme to meet sanitary and phytosanitary standards (SPS) (9<sup>th</sup> EDF)
- € 2.2 billion "Investment Facility" managed by the EIB which facilitates loans, equity and guarantees for investment projects
- € 50 million programme under Trade.com. Main components:
  - (i) Facility to reinforce local analytical and research capacity for trade policy formulation including stakeholder participation;
  - (ii) Facility to provide immediate assistance for ongoing negotiations through the recruitment of a pool of more than 55 ACP trade experts and training for negotiators;

(ii) Facility to promote catalytic pilot initiatives for institutional reinforcement in the area of trade support services, which can then be developed through other financing mechanisms, with special attention to ensuring an enabling regulatory environment to overcome Technical barriers to Trade and Sanitary, Phytosanitary and Biotechnology barriers to trade.

- In addition, there is a commodities programme for € 45 million under the 9<sup>th</sup> EDF

### V.3 TIMOR LESTE AT A GLANCE

Land area	Population	Population density
15,000 sq Km (= half Belgium)	926,000 (2004 Census data)	61.7 per sq km
<b>Population of main town Dili:</b>		
60,000 (1998); rising to 140,000 approx. (Sept 2001); 167,000 (2004 Census data)		
<b>Annual population growth rate (%)</b>		
1975-2002: 0.3	2002-2015: 2.8	

#### Political situation

Timor-Leste was a colonial territory and overseas province of Portugal until 1975. It was occupied by Indonesia December 1975 until September 1999. On 30 August 1999 in a UN-managed referendum, 78.5% of participants voted against the offered status of autonomy within Indonesia, and thus for independence. In September 1999 Indonesian integrationists and militia responded to this result with an outburst of indiscriminate violence, killing over 1000 persons, causing the forced displacement of more than 250,000 others and leaving three-quarters of all public infrastructure, private housing, telecommunications and valuable public archives destroyed. The Australian-led UN INTERFET peace-keeping forces (admitted by Indonesia) re-established peace. In October 1999 the UN Security Council established UN Transitional Administration for East Timor (UNTAET) until the Parliamentary and Presidential elections and the restoration of independence on 20 May 2002. Three successive UN Peace keeping missions have provided, with gradually decreasing human and financial resources, support to security, the justice systems and to other state building activities. The present UN mission (UNOTIL) is carried out under the jurisdiction of the UN Political Affairs Department and will end in May 2006. The present Government is made up of 17 Ministers, 14 vice Ministers and 10 State Secretaries. Village elections were held by the Government in 2004/05, while both National Parliamentary and Presidential Elections are due in 2007.

Timor-Leste has made some impressive achievements. It has succeeded in adopting the most urgent legislation, it has gradually established most of the institutions foreseen in the Constitution and has established a clear orientation toward sustainable development through a National Development Plan (NDP), a Stability Programme (SP) and 17 Sector Investment Programmes (SIPs).

The country has benefited from the support of donors who have provided financial contributions amounting to up to 40% of recurrent expenditure and more than 100 million USD per year for investment programmes and projects.

Successful negotiations with Australia on sharing mineral resources in the Timor Sea mineral resources have also raised the perspectives of increased local revenues and future self-reliance. However, population growth is one of the world's highest and is offsetting the non-oil GDP growth. Formidable problems still exist. The downsized and weak public sector is called to promote the production of non oil revenues and to provide adequate services to the population.

Farmers are expected to diversify and improve their production without any subsidy and very often without the support of agriculture extension. Likewise, the private sector is expected to solve the huge unemployment problem, while local capital is not available and the business environment is not yet attractive to foreign investment except for oil-gas and telecommunications.



## Selection social and economic indicators

Indicator	2000	2001	2002	2003	2004	2005	2006
Gross Domestic Product (US\$ millions)	316	368	343	336	339	350	356
Real annual GDP growth (%)	15.4	16.6	-6.7	-6.2	1.8	1.8	-1.5
GDP per capita (US\$)					366	365	375
Inflation % (US\$ based CPI for Dili)	3.0	-0.3	9.5	4.2	1.8	0.9	5.7
Unemployment rate (%)		6.2			8.5	5.0	
Exports growth rates (%) <sup>(1)</sup>			50.0	16.7	14.3		
Imports growth rates (%) <sup>(2)</sup>			2.6	-12.0	-9.3		
Non-petroleum exports (USD millions)					8.1	9.0	
Current account balance				-85	103	292	411
Trade deficit (USD million)				186	154	127	133
Fiscal balance <sup>a</sup> (% GDP) <sup>(3)(4)</sup>	-52	-53	-48	-33	29	32	37
Land Area	15,000 sq. km (= half Belgium)						
Population Timor-Leste 000s	779.567 <sup>b</sup>	787.338 <sup>e</sup>			924.000		
Population Dili District 000s		120.474 <sup>c</sup>			167.777		
Adult Literacy Rate (% age 15 and above)				58.6			
Primary school enrolment %		75					
Secondary school enrolment %	20						
Life Expectancy at Birth – Female/Male (years)	57		49.3	55.2		55.2	
Life Expectancy at Birth – Female (years)			50.2	56.6		56.6	
Life Expectancy at Birth – Male (years)			48.5	54.5		54.5	
Underweight children for age (% under age 5)			43.0	45.8			
Under 5 mortality rate (per 1,000 live births)	102		126		130		
Maternal mortality rate (per 100,000 live births)	660						
Immunisation rate (%) <sup>(5)</sup> – Measles			47	60	55	55	48
Immunisation rate (%) <sup>(5)</sup> – DPT				70			
Births supervised by trained personnel (%)	20		24		18		
Households with access to safe water (%) rural/urban average						58	

Sources: Economic indicators: International Development Association, *Country Assistance Strategy for the Democratic Republic of Timor-Leste for the period FY06-FY08*, July 26, 2005.

Socials indicators: UNDP, *Human Development Report 2005*, 2005.

Others: <sup>a</sup>IMF, Democratic Republic of Timor-Leste: Selected issues and Statistical Appendix, May 31, 2005.

<sup>b</sup>UN Common Country Assessment, *Building Blocks for a Nation*, November 2000.

<sup>c</sup>ETTA, IMF, WB, UNDP, *Success Survey in Timor Loro Sa'e*, August 2001

Article IV mission of IMF, 2007

Notes: <sup>(1)</sup> Merchandise exports nominal growth rate. Excludes oil/gas revenues.

<sup>(2)</sup> Merchandise imports nominal growth rate.

<sup>(3)</sup> Fiscal year basis (July-June); for example, 2000 refers to FY2000/01.

<sup>(4)</sup> Includes fiscal and quasi-fiscal expenditure programmes undertaken by bilateral donors and international financial institutions, outside the central government budget. The sharp revenue decline in FY 2005/06 reflects the adoption of the new savings and petroleum fund policy according to which only the sustainable income from the oil wealth is transferred to the budget.

<sup>(5)</sup> % of children ages 12-23 months.

#### V.4 SELECTED SOCIAL INDICATORS

Indicator					Estimate	
	1990-93	1996	2001-02	2003	2004	2005
Total population	750	840			924	1000
Annual population growth (% change)	3.5	2.4			4.7	
Total fertility rate	5.7	5.1	7.8		8.3	
Maternal mortality rate (per 100, 000 live births)	800	850			660	
Life Expectancy at Birth (years)	52	53		55.2	58	
Female	53.7	55		56.6	61	
Male	50.7	52		54.5	55	
Adult Literacy Rate (% age 10 and above)	35.6	40.4	58			
Primary school enrolment %	83		75		75	
Secondary school enrolment %			20		38	
% Urban population with access to safe water	68		73		73	
% Rural population with access to safe water	26		50		43	
% Urban population with access to sanitation	49		65			
Underweight children for age (% under age 5)			43		42	
Under 5 mortality rate (per 1,000 live births)	250		126		130 (3)	
Immunisation rate (%) <sup>(a)</sup> – Measles			47 <sup>(1)</sup>	60 <sup>(1)</sup>	55(2)	55 (2)
Immunisation rate (%) <sup>(a)</sup> – DPT				70 <sup>(1)</sup>		
Births supervised by trained personnel (%)	20		24			

Source: UNDP, *Human Development Report 2005*, 2005 and UNDP Country Strategy, Sept. 2005

<sup>(1)</sup> International Development Association, *Country Assistance Strategy for the Democratic Republic of Timor-Leste for the period FY06-FY08*, July 26, 2005.

<sup>(2)</sup> World Development Indicators database, November 2006

<sup>(3)</sup> Health Sector Strategic Plan 2008-2012, Ministry of Health Timor-Leste

Note: <sup>(a)</sup> % of children ages 12-23 months.

## WELL-BEING INDICATORS BY REGION

	Timor-Leste	Urban	Rural East	Rural Center	Rural West	Lowland	Highland
Poverty Head Count (2001)	40	14-40	32	49	47		
Earth Floor (2003)	70	40	77	76	85		
TV and/or Radio (2003)	40	84	25	28	24		
Car and/or Motorcycle (2003)	6	17	3	2	2		
Infant Mortality Rate (1994-2003)	82	72	77	90	88	77	106
Under 5 Mortality Rate (1994-2003)	107	86	103	117	122	102	130
Births Attended by Skilled Staff (2003)	18	40	14	11	11	20	9
Child Malnutrition (2003)	46	42	44	45	57	46	48
Treatment Sought for Sick Child (2003)	24	28	26	22	18	25	19
Net Primary Enrollment (2003)	75	85	74	69	75		
Literacy Women (2003)	45	63	49	36	35	48	35
Literacy Men (2003)	54	68	59	44	50	58	46
Fluent in Portuguese (2003)	2						
Fluent in Indonesia (2003)	30						
Fluent in Tetun (2003)	79						
Piped Water (2003)	39	50	12	50	38		
Access to Electricity (2003)	26	73	19	11	3		
Firewood as Fuel (2003)	98	93	100	100	100		
Months with Insufficient Rice/Corn (2001)	3.6	2.7	4.2	3.8	3.9		

*Source: Timor-Leste Living Standards Measurement Survey for 2001 data; Demographic and Health Survey for 2003 data.*

*Note: All data are in percentages except "Months with Insufficient Rice/Corn."*

## **V.5 ENVIRONMENT PROFILE**

### **1. STATE OF THE ENVIRONMENT**

The area of Timor-Leste is approx. 14,874 km<sup>2</sup> (half Belgium) with a total length of approx. 265 km, and a maximum width of 97 km. Timor-Leste includes the eastern end of the island of Timor, the enclave of Oecusse (2,500 km<sup>2</sup>), and the islands of Atauro (144 km<sup>2</sup>) and Jaco (8 km<sup>2</sup>).

The Timor Island is the easternmost of the Lesser Sunda Islands. To the north lies the Banda Sea, and to the south, the Timor Sea. The distance to Australia in the southeast is only approx. 500 km.

Geologically, Timor is part of the Australian continental plate, and the bedrock is mainly sedimentary calcareous rock. This differs from most of the other islands of Indonesia, which are volcanic in origin. This means the island has relatively unproductive, low fertility, fragile soils. In most areas, this low fertility is compounded by the rapid decomposition of organic matter due to the tropical climate. The soils tend to be relatively thin, and with low water holding capacity. The topography of the island has a profound effect on the vegetation and contributes to high levels of erosion. Almost half the land has a slope of 40 percent or more shallow soils and susceptible to erosion. Several mineral deposits have been recorded. The most important at present may be the mineral oil, which is found both on land and in the Timor Sea. The rainfall pattern – particularly in the north with long dry periods followed by intensive, short rainfalls – is also conducive to erosion. Deforestation and over-grazing is thought to have further increased the susceptibility to erosion in many areas.

#### **Particular issues for Timor-Leste**

Timor-Leste's economy is heavily dependent on its natural resources. Land, water, forests and coastal zones provide a livelihood, or are the major source of income, for at least three-quarters of the population. They are the basis for social and economic security and growth. Mineral and petroleum deposits are expected to provide a significant source of income and foreign revenue for many years to come. Finally, many of Timor-Leste's resources – for example, its pristine coastal ecosystems, its stands of sandalwood and its remaining primary forests – are a world heritage in need of protection.

These resources can certainly be exploited to a far greater extent – if well managed. However, as with other countries throughout the region, some of Timor-Leste's natural resources have been degraded through over-harvesting during the periods of colonisation and occupation. Forests have suffered in particular. These threats are currently on the increase. Natural resource degradation – for example, of water and of productive land – is already limiting economic opportunities in many areas. It is also leading to significant direct economic costs, for example, by damaging infrastructure, increasing floods and contributing to health problems. Finally, there are localised threats to Timor-Leste's air, coasts and remaining biodiversity.

**Situation of Lands** There is no comprehensive, up-to-date information available on land use and land cover in Timor-Leste.

### **Forests**

Forests have always been important to the economy of Timor-Leste. Very valuable sandalwood has been harvested for centuries and, at other times, honey, beeswax and other timbers such as teak. There is no up-to-date and comprehensive information of the forests of the country. Maps for forest cover produced by the Australian Government funded ALGIS project continue to rely on information collected during the Indonesian period for the 1993 inventory. While accurate data are not available, it is generally believed that the forests have been severely over harvested and degraded in recent times. It is likely that not all the open and poor quality forests now to be seen have actually been badly degraded, especially in steep land. Skeletal soils and poor moisture relations have produced extensive areas of natural savannah formations.

Fuel wood collection, land-clearance, high levels of shifting cultivation and over-grazing are thought to be the source of the problem. Within Timor-Leste there is a strong demand for fuel wood for household. Anecdotal evidence suggests that small industries also use large amounts of fuel wood. Reliance on fuel wood, especially in urban areas, has increased substantially.

### **Water**

Generally speaking, areas north of the central Mountain range are in a rain shadow, with a short rainy season that begins around November and extends to March-April, usually accompanied by a westerly monsoon. Total annual rainfall ranges from under 1,000 mm to 1,500 mm in the drier coastal areas. The rainy season is short and intensive. Dili, for example, may receive up to 30 percent of its annual rainfall (900 mm) in one day. The steep slopes and geological conditions mean that many northern areas are unable to store water effectively. Given the long dry season, many northern areas, particularly in the uplands, traditionally experience seasonal water shortages. This is a limiting factor in agricultural production and a source of food insecurity and poverty.

As in many other countries water is used for many purposes often in conflict one with the other. Timor-Leste is no exception and there is not yet an integrated management of the water resources.

### **Fisheries**

Timor-Leste is surrounded by sea on three sides, has a coastline of about 700 km and a potential exclusive economic ocean zone of approximately 75,000 km<sup>2</sup>, although the precise boundaries of this zone have not yet been determined. Fisheries resources may be considered in four zones or styles of fishing operation. These zones are not exclusive as there is some overlapping of resource use. The offshore zone supports a level of industrial fishing using large vessels (length 15 m or more) operating over an extended period of time. The near shore zone, 1-12 km from the coast, has been exploited by motorised (outboard motors) vessels with a capacity to hold catches suitable for local markets. The inshore zone is dominated by smaller boats operating close to shore with the catch either being sold or used for family consumption. Finally, subsistence fishery is

focused on the utilisation of the reef flats or beach areas, but sometimes from small vessels off the beach or reefs. The present state of the fisheries resources is unknown.

### **Biodiversity**

Little is known of Timor-Leste's genetic biodiversity, although the probability that Timor Island is the centre of origin of the sandalwood tree indicates that the island's sandalwood, at least, may contain valuable genetic characteristics. General observations indicate that the status of much of Timor-Leste's biodiversity is better than many places in the region. The most likely exception is the forest biodiversity, which has suffered due to the high levels of primary forest loss. The biodiversity of Timor-Leste is poorly documented and poorly studied. The country is known to have good quality, rare and possibly unique terrestrial, lake and marine ecosystems which originate from the unique geological and meteorological conditions. Many important terrestrial animals are found, including deer, cuscus, wild pigs, monkeys, crocodiles, snakes and lizards. A recent survey tentatively identified eight ecosystem and species diversity.

### **Solid Waste and Sewerage**

Solid waste, mostly associated with increased consumption, is a major concern in urban areas, particularly in Dili. The consumption patterns of the large international community based in Dili in recent time are believed to have influenced both the scale and nature of the solid waste. The size of this community has been steadily declining along with some reduction of solid waste disposal. Solid waste contains a mixture of organic, non degradable and hazardous waste, each posing specific threats, and each requiring specific management or treatment. In Dili, waste is collected by the formal system and taken to the Tibar landfill site.

### **Economic Impact of Resources degradation**

Environmental degradation is a major concern because of its impacts on economic growth and poverty. There is not sufficient information available to determine the costs of these impacts in Timor-Leste and their ultimate impact on GDP. The following are believed to be among the more important costs:

- Land degradation leads to losses of agricultural production, to damaged waterways, and to increased costs of water treatment and water supply systems.
- Water pollution leads to health costs and to reductions in productivity in the fishery, agriculture and tourism sectors.
- Air pollution leads to health costs and associated economic losses.
- Biodiversity loss leads to short-term losses in the health and food sector, and possibly huge long-term losses covering many sectors.
- Floods, landslides and fires cause severe economic damage, and are in part a result of environmental degradation.
- Climate change may have significant implications on economic development in Timor-Leste.

The further development of the country's natural resources will depend primarily on private sector initiatives and investment. The opportunities can be available for diverse groups, including: local communities and farmers; small and medium-sized, locally

owned businesses; and international investors, including large multinationals, especially in oil and gas. The key role for the Government is to create, as soon as possible, the enabling conditions for this investment and to manage and regulate the activities of the private sector in a way that protects the environment, the resource base and the heritage of the country.

The Government is well aware of the potential trade-offs in this sector. Short- and medium-term social and economic gains can be made at the expense of medium and long-term environmental degradation, thereby limiting social and economic possibilities in future years. The Government further recognises that in the past years of colonisation and occupation, this trade-off was badly managed and, as a result, the natural resource base of the country has been depleted; the degradation is now imposing substantial additional costs on the country, contributing to widespread poverty and food insecurity. Finally, the Government is aware of the equity issues involved - growth and prosperity for one section of the community should not come at the expense of decreased environmental security and poverty for other sections of the community.

## **2. ENVIRONMENT POLICY, LEGISLATIVE POLICY AND INSTITUTIONAL FRAMEWORK**

In the short time since Independence, the Government of Timor-Leste has made progress on the overall strategies to manage natural resources and the environment. For the petroleum and minerals sectors, the Government has created a strong governing framework and has promoted private sector investment laws. In agriculture, forestry and fisheries, these approaches are complemented by efforts to develop joint and community management mechanisms in rural and isolated areas. The Government has also made a start in establishing a strong regulatory and management framework for environmental protection. Until now, efforts have focused on developing laws and policies, establishing and strengthening institutions, training and capacity building. Some efforts have been undertaken to develop information databases and to develop a cross-sectoral mechanism for management of natural resources.

### **Petroleum and Mineral Sector**

The strategy of the Government is to manage minerals, energy and extractive activities in a consistent, fair, environmentally sustainable, transparent and timely fashion as mandated in the National Development Plan. The guiding principles to this are sustainability, efficiency of resource use and equity. The Government has set out its strategy for achieving these objectives in the NDP and in its Strategic Plan. The approach, for both minerals and petroleum, is to create as quickly as possible an enabling environment that will encourage the domestic and foreign private sector to invest. With the successful creation of this environment, the role of the Government will be limited to oversight and regulation and to continued investment promotion. In formulating its strategy for offshore development of resources, the Government decided to proceed immediately to invite investors to bid on exploration and revenue sharing contracts based on existing information. Partnerships have been established with international private companies to initiate the exploration and exploitation of these resources. In the JPDA,



contractual arrangements have been established with Conoco-Phillips (operator for the *Bayu-Undan* field) and with Woodside (operator for the Greater Sunrise field). As a result of the off-shore programme, the petroleum sector is expected to be the main source of revenues for Timor-Leste within the next years. Just taking the interest of the petroleum fund would generate annual revenues of about 200 million US\$. In addition to these revenues, careful management and development of this sector can bring other benefits, including job creation, skills development, institution building and foreign direct investment.

In the case of the on-shore and near-shore resources, the Government has decided to adopt a phased approach, first investing in more sophisticated seismic/exploration information, the results of which, have been shared with potential private investors launching a tender for the resource exploration and extraction.

The National Environmental Legislation enhanced so far are:

- Law on the Petroleum Fund
- Law on Petroleum Taxation
- Petroleum Act;
- The tender protocol for off shore resources

### **Energy**

At the present time, Timor-Leste is almost totally dependent on imported petroleum products and domestically produced firewood to meet its energy requirements. Petroleum products are the single largest import of the country. According to the trade data released by the National Statistics Directorate, Timor-Leste imports about \$36.8 million of petroleum-related products per year – equal to a quarter of all merchandise imports. Informal estimates indicate that the power sector now consumes the equivalent of 450 barrels of oil a day, while the transport sector uses the equivalent of 600 barrels a day. The commercial development of domestic petroleum sources could therefore have a significant economic impact that, among other things, could result in a substantially lower merchandise trade deficit, which was almost \$140 million last year.

At present there is no National Energy Policy for Timor-Leste. It is essential for the country to have an energy policy that provides the basic Road Map for movement towards the objective of stable and secure sources of energy.

### **Environmental Protection and Management**

As recognised in the National Development Plan, “real lasting poverty reduction is only possible if the environment is able to provide the service people depend on, and if natural resources are used in a manner that does not undermine long-term development”. Accordingly, the Government’s main goals for protecting and managing the environment are:

- Manage extractive activities in an environmentally appropriate fashion.
- Protect and enhance the natural environment.
- Raise community awareness about the importance of protecting the environment.
- Integrate environmental considerations into policies, programmes and plans.
- Ensure accountability to the government and the community for environmental aspects of the extractive industries.

As the earlier discussion indicates, the main environmental issues are water pollution, land degradation and biodiversity loss, together with a growing threat to the marine and coastal ecosystems. An upturn in economic activity and increase in private investment has the potential to exacerbate these threats. For example, there are some 600 investment projects waiting to start up after the new Investment Law is promulgated. An important challenge for the Government is to build capacities for quick approval of these proposed investments, while at the same time ensuring that they are consistent with the environmental laws and regulations and that they do not have adverse social and economic impact.

In the first country report on the Timor-Leste's Millennium Development Goals in 2004 three indicators have been identified as being especially relevant for the sustainable development of the natural resources of Timor-Leste and sound management of the environment. These are:

- Energy use per unit of GDP
- Carbon dioxide emissions per capita
- Population using solid fuels

No specific targets have been set for these indicators as yet. A start is being made in developing capacities for periodic monitoring of these aspects of environmental management.

Firewood is the major source of fuel for about 80 percent of the households. This compares with an average of 75 percent of households in all developing countries that use solid fuels. Approximately 1.6 million cubic meters (JAICA-Report) of fuel wood is consumed each year in Timor-Leste. With the elimination of fuel subsidies the use of firewood is growing. No reliable data is available on commercial energy use in Timor-Leste. Commercial energy consumption for Timor-Leste may range between 300 and 400 kg of oil equivalent per \$1,000 of GDP, which is similar to many other developing countries.

There is a direct relation between the amount of energy use and the CO<sub>2</sub> emissions. As carbon dioxide (CO<sub>2</sub>) is mainly generated from the burning of the fossil fuels, this includes also fire wood.

Existing Governance Framework To date, the main focus of the Ministry of Natural and Mineral Resources and the Secretary of State for Environment have been on establishing the framework for effective environmental governance, on developing capacity at the national level, and on pollution or the 'brown side' of environmental management. The following laws have been approved.

- Law on Fishery and Aquaculture (Decreto-Lei n° 6/2004)
- Law on Water Distribution (Decreto-Lei n° 4/2004)
- Quarantine Law (Decreto-Lei n° 21/2003)

Timor-Leste is also a party to the UN Convention on Desertification and Land Degradation (UNCCD). However it has not yet decided on the other conventions making it eligible to the Global Fund for Environment.

The Institution responsible for coordinating environmental issues is the State Secretariat for the Coordination of the Environment, the Arrangement of the Territory and the Physical Development. However the Secretary of State refers directly to the Prime Minister who is also Minister for the Natural and Mineral Resources and for the Energy's Policy. However a number of Ministries (Agriculture, Development, Public Works, Transport and Communication, Planning and Finance, Health and Education) are also concerned at different levels with environment.

### **3. SUPPORT TO THE SECTOR**

The support to the environment is provided by different donors through the different Ministries concerned with the sector. It is provided through the recurrent budget and through investment projects. From Fiscal Year 1999/00 through FY2003/04, the total support amounted to US \$ 10 millions. Donors accounted for about 90% of both modalities. The petroleum sub-sector accounted for almost two third of the total spending. This was due to the large support of Norway, USA, China and which included capacity building for the Timor Sea development programme and the launch of onshore and near shore survey by Petro-China.

For the next 4 years, the Government is proposing a significant increase in spending on natural resources and the environment. Most of these outlays are aimed at laying the foundations for an increase in private investment in resource related industries by improving the enabling conditions for this investment, improving the understanding of the resource base of the country and its prudent management, and strengthening the legal, regulatory and environmental management capacities of the Government. The proposed level of expenditures is \$21 million during FY2004/05 through FY2008/09, some \$7 million of which is related to donor programmes ongoing and under preparation and currently planned budget allocations.

Disbursements from proposed new projects and programmes amount to \$13 million over the same period, along with a small amount of additional budget counterpart funding for the environment programme. About 36.3% are allocated to the development of on shore and off shore Petroleum sub-sector; 15% for mineral resources; 7.3% for renewable energy; 23.6% for the completion of on-going legal and regulatory framework for environment, improvement of environmental management and awareness campaign; 17.8% for integrated resource management.

### **4. CONCLUSIONS AND RECOMMENDATIONS**

Despite the ongoing efforts, many weaknesses still remain across the natural resources sectors. Some of the more notable ones include the overall absence of reliable, comprehensive up-to-date information, the lack of technical and management capacity, and difficulties in empowering local communities and in implementing participatory approaches. Lack of funds, working laws and equipment exacerbate these weaknesses.

The Sector Investment Programme for the Natural Resources and Environment has prioritised and sequenced measures that, if implemented in the mid term, will establish a strong governance framework for the natural resources sector. These programmes will

facilitate and promote private sector and community development, whilst at the same time assuring the long-term protection of Timor-Leste's land, forests, waters, air, urban areas and biodiversity. Some of the Government proposed investments are relatively high cost. Many are not, and will have high social returns for small investments (as for example the proposal to support the technical and coordination activities of the newly created, high-level, inter-sectoral resource management working group). This can help Timor-Leste avoid the costly sector-specific approaches that have led to many problems in other countries in the Region.

There has also been progress, albeit uneven, in developing the policy framework required to pursue the objectives. In almost all areas of natural resource and environmental management, agency staff must work closely with officials in other agencies, with local communities, with the private sector, the media and other members of civil society. Much work remains to be done in building the skills of staff in these important areas. A particular concern is building capacities at the district and local level to ensure that there are effective mechanisms for collaboration with local communities in the management of local resources and the environment. The EC, through the Trust Fund and through other single donor agreement with the WB, has been supporting the development of strategies and legislation mainly related to the Agriculture sector and to water and sanitation. Technical assistance and capacity building has been provided to the Ministries responsible for Rural development, Health and to the Timor Sea Office responsible for Petroleum. The last generation of EC support includes the development of forestry inventory, reforestation and agribusiness development.

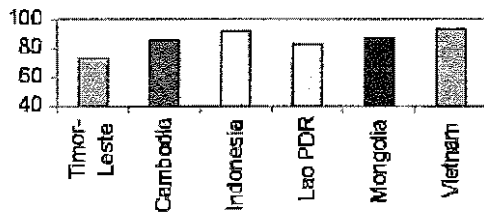
## **V.6 PROGRESS TOWARDS MDGs**

The Government of Timor-Leste's National Human Development Report assesses poverty against the MDGs as follows:

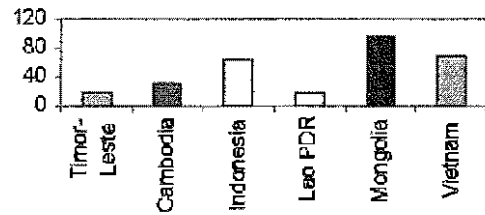
- i) 4% per annum economic growth is the minimum requirement to achieve targets on eradicating extreme poverty, and stronger policies on food security and more support for mothers are required to achieve targets for maternal and child health.
- ii) Significant additional investment will be needed to meet the 2015 requirement of 100% primary school enrolment.
- iii) Gender equity targets in primary and junior secondary school enrolments are likely to be achieved, but not for senior secondary school.
- iv) To reduce child mortality to 96 per 1000 by 2015 is realistic.
- v) HIV prevalence is low in Timor-Leste, whereas malaria, dengue and other diseases remain prevalent, and will need investment.
- vi) Measures are not in place to reverse environmental degradation: the Government must contribute more to achieve water supply and sanitation targets.

## TIMOR-LESTE AND REGIONAL PROGRESS TOWARD MDGS

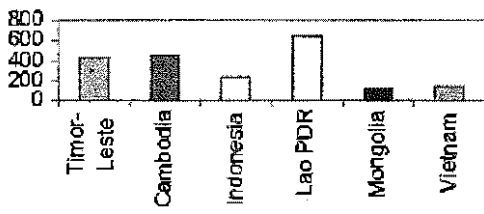
Net Primary School Enrolment 2001



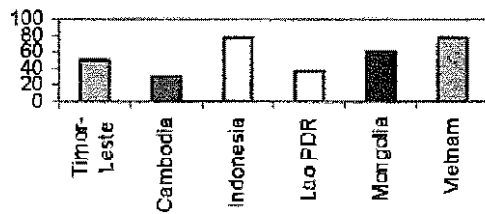
Births Attended by Skilled Staff 2001



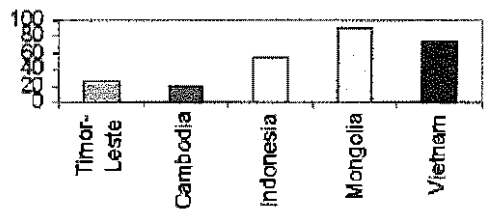
Maternal Mortality 2001



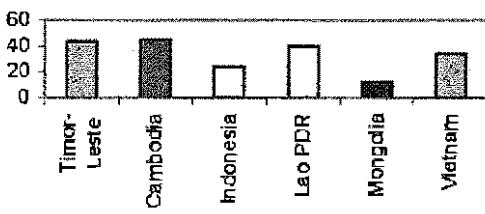
Improved Water Source 2001



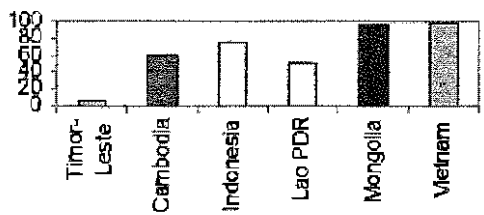
Access to Electricity 2001



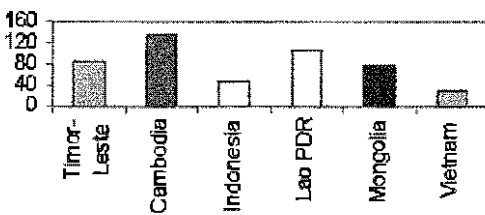
Child Malnutrition 2001



Measles Vaccination 2001



Under 5 Mortality 2001



## **V.7 SUMMARY OF EC CO-OPERATION**

### ***Relief and rehabilitation (€85.5 million)***

- €55.4 contribution to the multi-donor Trust Fund for East Timor (TFET)
- €30.1 million contributions to :
  - UNTAET Trust Fund which supported the UN missions (2000)
  - Food aid through the World Food Programme in 1999-2000.
  - Repatriation and re-integration of East Timorese refugees wishing to return from West Timor implemented through UNHCR. €1.7 million of this grant has gone to the Special Fund to pay the pension and separation indemnities of former East Timorese employees of the Indonesian government and € 317,000 to the Commission for Reception, Truth and Reconciliation.

### ***Humanitarian Assistance and Food security (€56.5 million)***

The EC Humanitarian Aid Office (ECHO) has provided **€44 million** of humanitarian assistance through NGOs and UN Agencies for the following:

- medical assistance, including mental health and training for health workers
- water and sanitation projects, a large portion of which was for the rehabilitation of school water and sanitation systems
- shelter and non-food items
- food and logistics
- protection and transport of refugees and displaced persons
- disaster preparedness (DIPECHO)
- nutritional support and combating the consequences of 2002-2003 drought

Further support:

- Food security (€6 million)
- Support for NGOs (€6.5 million)

### ***Rural development (€34.5 million)***

The EC allocated €25.5 million for 2003 to support the Government of Timor-Leste in attaining its overall objectives of poverty reduction and promotion of economic growth. The programme addresses priorities for the development of the rural areas' agriculture; off farm employment-generation; women's empowerment; rural infrastructure. The programme started in March 2004.

In 2005, the EC committed €9 million to the EC-Timor-Leste Rural Development Programme 2005. The overall objective of the programme is to attain food security and sustainable livelihoods for poor rural communities in Timor-Leste, and particularly in the poorest districts located in the border area of Timor-Leste and Indonesia (Bobonaro and Covalima).

### ***Health sector (€24.5 million)***

- Support for the health referral system, training and drugs, approved in 2002
- Support the Implementation of the Health Sector Investment Programme, 2004.

### ***Capacity building, including election support (€2.5 million)***

Several actions have been financed in support of capacity building of different institutions and NGOs, such as:

- Support for civic education and electoral observation for the Constituent Assembly and the Presidential elections (via UNDP)
- contribution to the “200 Development Posts” as part of the capacity-building programme managed by the UNDP, approved in 2002
- Support for the Justice sector through the NGO “Lawyers Without Borders”
- Support of the promotion of Children’s Rights through CARE
- Support to the Teachers Training Colleges through Caritas Sweden
- Support of women’s development through NGOs Horizon/Timor Aid
- Support of regional information systems for East Timor
- Support for a Trade Needs Assessment



## V.8 TIMOR-LESTE HUMANITARIAN PROFILE

### 1. Humanitarian Situation

#### *Internally Displaced People (IDPs)*

The main humanitarian issue the country is now facing is the estimated 100,000 people that have been displaced for more than a year now. In May 2006, camps of Internally Displaced People (IDPs) sprung up quite anarchically around churches, convents, UN / military / NGOs compounds, or by the airport. A large number of IDPs also moved from Dili to the districts, mostly to stay with host families. This large displacement, which still directly affects more than 10% of the Timor-Leste total population, was triggered by the violent events of the first half of 2006 that unfolded into a full-scale civil and security crisis.

In 2007, the IDP situation in Timor-Leste remains volatile and the people react very quickly to any event that they feel could threaten their security. The real number of IDPs still present in the camps is probably overestimated. (By end of September 2007, approximately 30 000 people are living in camps in Dili and 70 000 in the rural district, mainly with host families). Many people seem to go to work or back home normally during the day and only spend the night in the camps, where they feel more secure and where free food distribution are available.

Insecurity and unresolved land and property issues prevent return; in the absence of any mechanism for compensation and property restitution, the displacement crisis is likely to persist.

#### *Malnutrition / Food Security*

A severe and recurrent humanitarian problem faced by the population of Timor-Leste is the high prevalence of global acute malnutrition across the country, which remains close to the emergency threshold (15%) as a national average.

Global acute malnutrition is caused by several factors, the most important of which is the structural food shortages that affect two thirds of the rural population, and which are particularly acute in November/December and February/March. In fact, Timor-Leste is a food-deficit country affected each year by localized droughts and floods, which systematically result in crop damage. Coping mechanisms of the rural population, that is the largest and poorest population in the country, remain insufficient. Another main reason for the high malnutrition rates is poor water and sanitation conditions (half of the population does not have access to a safe water supply), which directly results in diarrhoea and other water-borne diseases: Finally, other underlying causes of

malnutrition are insufficient crop diversification, poor nutritional practices and deficient health services.

The current security situation and the displacement of populations are severely hampering economic activities, which will further worsen overall poverty and the level of malnutrition. In the districts, IDPs staying with host families are additional mouths to be fed and are putting a heavy strain on their hosts' coping mechanisms, leading many hosting rural households to consume their seed stocks or sell their livestock. This burden is exacerbated by the simultaneous disappearance of the flow of money previously earned in Dili by the IDPs and sent back to their families in the districts. In that regard, WFP, in coordination with several key stakeholders, completed a comprehensive Emergency Food Security Assessment throughout all of Timor-Leste in the summer of 2006 to look at the impact the crisis is having on the food security situation of the population as a whole (IDPs, hosts and general community members). The assessment confirmed that the impact IDPs have had on host families outside of Dili is of real concern, particularly given the persistence of pre-crisis vulnerabilities. The impact of the crisis has led many families to already feel lean season effects in September 2006, and has placed normally food secure households into food insecure situations.

## **2. The Commission's Humanitarian Aid Department response and targeting**

### ***IDPs***

Following the outburst of violence that led to the displacement of some 150,000 people at the peak of the crisis in May/June 2006, a EUR 3 million Emergency Decision was adopted by the Commission's Humanitarian Aid Department (DG ECHO) on 28 June 2006, covering the following emergency needs: food, emergency shelter, protection, non-food-items, water and sanitation, and health. These programmes, which benefited more than 100,000 IDPs, were implemented by the World Food Program (WFP), the United Nations High Commissioner for Refugees (UNHCR), WorldVision Germany and Plan International UK.

As some 100,000 people were remaining displaced across the country early 2007, DG ECHO adopted a EUR 1.5 million ad-hoc Decision on 21 February 2007, to provide assistance to the people of Timor-Leste directly affected by the crisis, and in particular the IDPs, focusing its intervention on the sectors of water and sanitation, camp management, health, logistics, shelter, support to return and reintegration. These programmes are being implemented by IOM, Triangle Génération Humanitaire and Plan International-UK.

### ***Malnutrition / Food Security***

DG ECHO's objective in Timor-Leste has been to act in the short-term to contain and reduce the prevalence of acute malnutrition. In parallel, other Commission's programmes are being put in place on the mid and long term in order to address the root causes of malnutrition in a sustainable way.

DG ECHO has been involved in fighting malnutrition since October 2003, when it restarted its programmes in Timor-Leste in response to a Government's appeal for international aid launched after some severe food shortages in 2003. DG ECHO's response was channelled through a EUR 2 million Emergency Decision which included the following components: food aid, nutrition and agricultural rehabilitation.

The emergency response was followed in 2004 by a targeted supplementary and therapeutic feeding project implemented by CARE Austria in the western districts of the country (Bobonaro, Liquiça and Cova-Lima).

In the second half of 2005, a new EUR 2.5 million Decision was adopted to extend the nutritional intervention to the central districts of the country. Five projects started on the last quarter of 2005, targeting more than 100,000 people, with the three main components: providing supplementary feeding for acutely malnourished children under five years old and to pregnant and lactating mothers, improving safe water supply in rural areas and enhancing livelihoods in sucos affected by acute malnutrition. During the mid-2006 turmoil, some of these programmes were reoriented to directly benefit the IDPs.

While therapeutic followed by supplementary feeding programmes have had an impact on severe acute malnutrition rates, acute malnutrition remains high in the country. The ongoing crisis is also having a negative impact on an already fragile food security. While the long term development programmes that are being started by the Commission are addressing the structural causes of this nutrition / food security situation, a short-term intervention was considered necessary to cope with the most immediate acute needs of the population. Therefore, Timor-Leste was included as a beneficiary country for EUR 1.5 million under the ECHO 24-month € 135 million Global Food Aid Decision starting January 1<sup>st</sup>, 2007, decision which was approved on March 21st, 2007. The main activities are food distribution to IDPs and the most vulnerable households affected by the crisis, and food security. DG ECHO-funded blanket distributions of food are planned to phase out in the last months of 2007, leaving the way to targeted distributions focusing on vulnerable households.

DG ECHO's humanitarian assistance to Timor-Leste in 2007 is therefore totalling EUR 3 million.

The amount of DG ECHO's assistance to the country in 2008 is expected to be EUR 2 million, through one ad hoc multi-sectoral financial decision.

### **Disaster Risk Reduction (DIPECHO)**

DG ECHO has also been implementing its Disaster Risk Reduction Programme (DRR) in Timor-Leste since 2004. Projects aim at reinforcing the local coping capacities of vulnerable communities, raising their awareness together with local/district/provincial and national authorities on recurrent natural hazards, implementing small-scale mitigation activities, as well as establishing localised early warning systems (EWS) on droughts and floodings.

Recurrent natural hazards are identified together with the various stakeholders in the framework of National Consultative Meetings. Priority hazards in the targeted geographical areas (Oecusse, Covalima, Liquiça, Bobonaro, Lautem and South-west

coastal areas) are largely hydro-meteorological, predominantly droughts and slow-onset floods.

Under the fourth DIPECHO Action Plan for South East Asia (2004-2006) EUR 479,431 were spent on DRR activities through two partner organisations in Lautem and Liquica districts. The recently launched fifth Action Plan (2006-2008) foresees EUR 188,475 for one partner in Lautem district to enhance the capacities and strategies of the communities at risk in the Raumoco watershed to cope with flooding and drought.

As DIPECHO activities are normally part of partners' longer term strategies and initiatives in the country, they create synergies with longer term instruments (like food security) and also contribute to the mainstreaming of disaster risk reduction in a sustainable manner.

### **3. Linking relief, rehabilitation and development (LRRD)**

Solving the ongoing civil crisis and the chronic food insecurity requires both short and long term interventions. DG ECHO funds humanitarian actions that have a quick impact and address the humanitarian needs of IDPs whether they are in camps or with host families, as well as the most vulnerable households directly affected by the crisis. However, a sustainable solution to the crisis will be found only when its structural causes will have been addressed. Therefore, DG ECHO will keep closely coordinating its humanitarian actions in favour of IDPs and other populations affected by the ongoing crisis with the other Commission's interventions.

In the food aid and food security sectors, ongoing humanitarian actions targeted at the Timorese population affected by the crisis need to be complemented by longer term efforts addressing the underlying causes of malnutrition to have a sustainable impact. DG ECHO plans to discontinue provision of humanitarian aid in these sectors once the situation stabilizes and the longer-term food security and rural development projects funded by the Commission start producing results.

## V.9 DONOR MATRIX

(in thousand € contributions since Independence)

Donor	Main bilateral donors (ongoing assistance)								
	EC	Finland	Germany	Ireland	Italy	Portugal	Spain	UK	Sweden
Budget policy						5070			
Industry, mining and construction						3309			
Energy									
Transport			9585			4183			
Education						31545	1833	3619	5051
Health	24500		1653	151	216	381	625	101	
Water			4520	108		1236		24	168
Child protection									
Women in development				201					
Environment/rural development	34500								25
Poverty monitoring									
Agriculture and fisheries			3700	110		2167	1230		
Private sector and NGOs		813				2985			
Culture, youth, communication			409	52		3194			
Government and civil society	2500	6374	7946	7778	538	168845		4585	7327
Emergency and relief	85500	1510	516	1170		2221		10275	
Commodity assistance		5605		8725	175			30730	4507
Administrative costs		745				4437		34	
Bank and financial services				129		818			18
Social services and infrastructure			614	1046		7910			14
Food security	56500		6159				381		
Business and trade				6		691			
Tourism						182	317		
Multisectoral						111976			
<b>Total</b>	<b>203500</b>	<b>15047</b>	<b>34692</b>	<b>19576</b>	<b>929</b>	<b>351150</b>	<b>4386</b>	<b>49368</b>	<b>17110</b>

**Sectoral breakdown (2006)**

Donor	Main bilateral donors (ongoing assistance)						Multilateral		
	Australia	Brazil	Japan	New Zealand	Norway	USA	World Bank	Total	EU%
Budget policy									
Industry, mining and construction			690		3714	1505			
Energy			17193		8852	3618	25		
Transport	552		36951		410	117			
Education	15036	1195	11370	1164	778	1447			
Health	11255		4728		1505	10342			
Water	19950		31326		343	648			
Child protection									
Women in development			9		146	17			
Environment/rural development	168		1020		170	139			
Poverty monitoring					12				
Agriculture and fisheries	12348	292	15014			18761			
Private sector and NGOs	365					4024			
Culture, youth, communication	4001		195			7439			
Government and civil society	108421		3493	2803	10301	30216			
Emergency and relief	8270		1656		423	117	4318		
Commodity assistance	48741		36874	1166	11621	14307	16304		
Administrative costs	1316				29				
Bank and financial services	635		3			852			
Social services and infrastructure		1758	196		1117	1001	1395		
Food security	122					589			
Business and trade			27		42	2801			
Tourism	196		36			64			
Multisectoral	182		85		1712				
<b>Total</b>	<b>231557</b>	<b>3245</b>	<b>160866</b>	<b>5133</b>	<b>41285</b>	<b>94745</b>	<b>22042</b>	<b>1254631</b>	<b>55.5</b>

## V.10 CAPACITY BUILDING

Fostering sustainable growth and poverty reduction through successful implementation of the NDP and SIPs will depend on strengthening capacity in key areas, such as public financial management and justice. Though the Government has made great strides, institutional capacity remains weak in Timor-Leste. Low levels of education and professional experience have led to a shortage of technical expertise. The scarcity of skills in accounting, auditing, economics, and legal drafting has been reflected in the Government's difficulties recruiting qualified personnel across sectors. For staff already in the civil service, there is a lack of familiarity with new and changing systems and processes. Well performing sectors have benefited from strong national leadership with a clear vision. Early on, these agencies adopted sound policies and strategies and developed institutional and legal frameworks, allowing them to function within a clear structure in pursuit of well defined goals.

Though many early capacity building efforts focused on getting critical systems up and running quickly, they have left behind a legacy of heavy reliance on international advisers who have often focused on in-line tasks rather than skills transfer. This situation gained a note of urgency as the United Nations Mission in East Timor was scaled back considerably in May 2005. Since then, the Government has worked with the smaller United Nations Office in Timor-Leste (UNOTIL) to ensure a smooth handover of functions, especially in the areas of justice and public financial management. Timor-Leste is now moving beyond the transitional substitution of international for local expertise and focusing on a more integrated approach to institution building. Under the leadership of the CDCU, the Government has adopted a capacity building strategy that relies on three inter-related pillars: skills and knowledge, systems and process, and attitudes and behaviours.

Based on this integrated framework, and with the expectation of a further reduction in international advisers following the downgrade and eventual withdrawal of UNOTIL, the Government requested that development partners support a programme of capacity building in planning and financial management. In response, the PFMCBP aims to sustainably strengthen planning, budgeting, public expenditure management, and revenue administration for growth and poverty reduction. The programme will focus on providing international staff where necessary, recruiting national staff as needed, and developing the *skills and knowledge* of national staff so that they are able to perform their jobs efficiently and effectively. In addition, the PFMCBP aims to improve the *systems and processes* governing the flow of work within MoPF and between MoPF and line ministries, districts, and the private sector. The programme will work to strengthen *attitudes and behaviours*, such as managing change, building professional integrity, encouraging communication and cooperation, and developing a strong work ethic. Finally, the PFMCBP will address important cross-cutting aspects of capacity building, including leadership and management, delegation of authority, transparency and accountability, and training in basic skills that are needed across the civil service. PFMCBP activities were elaborated in a participatory and demand-driven manner and

will be implemented as part of a multi-donor programme closely tied to the CSP. The World Bank's contribution to the programme was approved by the Bank's Executive Board in March 2006, and with support from development partners, implementation has started in 2007.

International support has also been critical to the functioning of the justice sector. The Justice Sector Programme (JSP), supported by the UNDP, has continued to prepare national professionals at the Judicial Training Center (JTC). A first group of candidate judges, prosecutors, and defenders is expected to complete theoretical training (including human rights and gender issues) by the end of May 2006. Of the 40 participants who initiated the programme, 27 continue. Based on evaluation results, probationary judges, prosecutors and defenders will be appointed in mid-2006 to work with the international court actors for a one-year period. Official appointment of national judges, prosecutors and defenders is scheduled for mid-2007 on completion of the probationary phase. A second group of 15 candidates has started JTC training. In advance of UNOTIL's closure in May 2006, the JSP has taken on the responsibility of funding the international posts of seven judges, four prosecutors, four defenders and two court clerks to sustain operation of the courts until national professionals complete their training. Out of a budget of USD 10.3 million over three years, USD 3 million has been committed to date. It is expected that a similar amount will soon be secured, which should allow for the continuation of the project.

With substantial international support the *Parliamentary and Presidential elections* were successfully carried out in 2007. Recommendations on how to improve on the electoral process will have to be implemented in the light of the coming local elections in 2008. Recommendations include the finalisation of the legal framework and capacity building of the election administration, (independence and impartiality of election bodies; division of tasks, communication, voter/civic education, improve on safeguard, fairness of election campaigning, capacity building of election administration.



## **V.11 CSP DRAFTING PROCESS**

In the drafting process of the 10<sup>th</sup> EDF CSP-NIP and as evidenced in the attached list, a broad consultation took place among key ministries and representatives of main donors, of still present in the country MS and of a sample of Non State Actors.

### **Meeting with key ministries**

- 1 - D. Minister of Planning and Finances and D. NAO
- 2 - Minister of Labour and Community Reinsertion in charge of the Simu Malu (Mutual Acceptance) programme for the IDPs
- 3 - Minister of Agriculture, Permanent Secretary and key directors
- 4 - Minister of State Administration in charge of Public Sector management
- 5 - Minister of Health
- 6 - Minister of Development in charge of Trade and Private Sector support
- 7 - Minister of Justice
- 8 - Minister of Public Works
- 9 - Chief of staff of the Office of the President

### **Meeting with donor's representatives**

- 1 - World Bank acting country Director
- 2 - AUSAID Resident representative
- 3 - USAID Resident representative and 2 programme managers
- 4 - UNDP Resident representative and D. SRSG, and 2 assistants
- 5 - JICA Resident representative
- 6 - ADB Resident representative
- 7 - UNDP project Officer (Strengthening parliamentary democracy in TL)

### **Meeting with Member States**

Ireland and Portugal representatives (only 2 MS countries are still represented in TL)

### **Meeting with Non State Actors**

Representatives of 11 NSAs (see list attached)

**Consultation with NSAs for the Preparation of the 10<sup>th</sup> EDF CSP 2008-2013  
Meeting, 20 September 2006 at EC Office**

**List of Participants**

<b>No</b>	<b>Name</b>	<b>Organisation/Title</b>	<b>Contact No</b>	<b>Email</b>
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## V.12 HARMONISATION ROAD MAP

Timor-Leste has a National Development Programme and a series of Sector Investment Programmes which operate as a framework for international assistance.

Following the crisis of 2006 a reflection of how to more effectively use the own and foreign resources and review new priorities emerging from the crisis has started which should lead to a shared commitment and coordinated efforts under a **common platform for recovery** called a "COMPACT" between Timor-Leste and the international community under the leadership of the Timorese authorities. This should entail a reorientation of the existing National Development Plan and the external financing framework required to address the crisis and to ensure that donor resources are complemented by and coordinated with the Government's own budget resources. The new Government also intends to revise the sector investment plans in order to set their new priorities.

A multi-sectoral forum to bring together all actors involved in the compact is required. A definition of priorities, activities and the role of different partners (as to defining their priorities of funding in the country) should allow for a clear identification of any gap in the political, security and development assistance needed for sustainable peace building and development.

Areas of special focus will include national reconciliation and social trauma, public safety and security sector reform, humanitarian assistance, justice, and the rule of law, and communication with civil society, youth employment, and human resource development.

Compact consultation meetings were held with the civil society, political parties, and the private sector.

The compact will be further defined in a series of workshops and identify key benchmarks for the Compact priority areas and ways for their implementation. The COMPACT is expected to be launched later in 2007.

### **V.13 TL AND ITS ADHESION TO INTERNATIONAL CONVENTIONS**

The setting of the “ Rights, Equality and Justice” sector stems from the Constitution and the vision articulated in the National Development Plan that “communities will live in safety, with no discrimination “ and that “the State will be based on the rule of law”.

Since the ratification of the Constitution, progress has been made in establishing many of related institutions, namely the Ministry of Justice, the Judiciary (Courts), the Public Prosecutors Office, the Office of the Provedor and the Offices of the Human Rights Adviser to the PM and the Office of the Promotion of Equality.

Moreover, the government has made additional steps in pursuit of above vision and the National Parliament has ratified in December 2002 not less than 7 conventions and 4 protocols including:

- The Convention on the Rights of Children
- The International Covenant on Civil and Political Rights
- The International Covenant on Economic, Social and Cultural Rights
- The International Covenant on All Forms of Racial Discrimination
- The Convention on the Elimination of all form of Discrimination against Women
- The Convention against Torture and Other Cruel Treatments
- The Convention on Migrant Workers.

Human and institutional capacity constrains prevent TL to report on a regular basis on the implementation of related conventions.

## V.14 LIST OF ACRONYMS

Acronym	Description
ACP	Africa, Caribbean, Pacific
AFTA	ASEAN Free Trade Agreement
ALA	Asia-Latin America Budget Line
APEC	Asia Pacific Economic Corporation
ARF	ASEAN Regional Forum
AUSAid	Australian Cooperation
CEDAW	Convention on Elimination of All forms of Discrimination against Women
CTF	Commission of Truth and Friendship
CSP	Country Strategy Paper
EC	European Commission
EU	European Union
EDF	Economic Development Fund
EPA	Economic Partnership Agreement
GoTL	Government of Timor-Leste
HSSP	Health Sector Strategic Plan
IDPs	Internally Displaced Persons
ILO	International Labour Organisation
ISF	International Security Forces
JPDA	Joint Petroleum Development Area
JSAN	Joint Staff Advisory Note
MAF	Ministry of Agriculture and Fisheries
MDGs	Millennium Development Goals
MTEF	Medium Term Expenditure Framework
NSA	Non-state actor
NDP	National Development Programme
NGOs	Non Government Organisations
NAO	National Authorising Officer
NIP	National Indicative Programme
HDI	Human Development Index
HRD	Human Resource Development
GDI	Gender Development Index
GDP	Gross Domestic Product
MTEP	Medium-term expenditure plan
NAO	National Authorising Officer/EDF
NGO	Non-Governmental Organisations
NSA	Non State Actors
PALOP	African countries having Portuguese as official language (países africanos de lingua oficial portuguesa)
PIF	Pacific Islands Forum
RDP	Rural Development Programme
SIP	Sector Investment Programme
STIs	Sexually Transmitted Infections
SWAp	Sector Wide Approach
SWG	Sector Working Group
TCF	Technical Cooperation Facility
TFET	Trust Fund for East Timor
TL	Timor-Leste
UN	United Nations
UNDP	United Nations Development Programme
UNTAET	United Nations Transitional Administration in East Timor
UNMIT	United Nations Integrated Mission in Timor-Leste
WTO	World Trade Organisation

## PART 2: INDICATIVE PROGRAMME

### 1.1 Introduction

On the basis of the cooperation strategy presented in Part One and in accordance with Article 4 of Annex IV to the Cotonou Agreement, the Indicative Programme has been drawn up as a set of tables showing the intervention framework for each sector, the financial programming timetable and a detailed chronogram of activities for all listed programmes over a rolling three-year period.

Amounts mentioned in this chapter indicate the overall breakdown of funds between the focal sector(s), macro-economic support and other programmes. The breakdown may be adjusted in the light of the operational, mid-term, final or ad hoc reviews. However, for any adjustment resulting in a substantial change to the structure of the response strategy, a formal decision in the form of an addendum to the strategy document will be required.

### 1.2 Financial instruments

The implementation of the EC's cooperation strategy with Timor-Leste will be financed from several financial instruments. The following is an indication of their mobilisation as currently envisaged.

#### 1.2.1 10<sup>th</sup> EDF, A envelope, € 63 million:

This amount shall serve to cover long-term programmable development operations within the framework of the Support Strategy. It is tentatively to be divided among focal and non-focal areas as follows:

<i>Focal sector 1:</i>	<b>Sustainable rural development</b>	[€ 35] million [55%] of total
<i>Focal sector 2:</i>	<b>Health</b>	[€ 8] million [13%] of total
<i>Focal sector 3:</i>	<b>Institutional capacity building</b>	[€ 13] million [21%] of total
<i>Non focal sectors:</i>	<b>Support for Non State Actors (NSA),</b>	[€ 4] million,
	<b>Technical Cooperation Facility,</b>	[€ 3] million, [11%] of total,

In line with the Commission decision C(2007)3617 of 1.8.2007 on the EDF10 aid allocation criteria, this amount will be increased by an incentive tranche once the Government will submit commitments on Governance and by an additional amount for functional cooperation in the field of governance in the PALOP context.

#### 1.2.2 10<sup>th</sup> EDF, B envelope, € 1.1 million:

This envelope will cover unforeseen needs such as emergency assistance where such assistance cannot be financed from the EU budget, contributions to internationally agreed debt relief initiatives and support to mitigate adverse effects of instability in export earnings.

In accordance with Article 3(5) of Annex IV to the Cotonou Agreement, this amount may, if necessary, be increased in the light of the operational or ad hoc reviews.

### **1.2.3 Investment Facility:**

In addition to the financial instruments mentioned above, of which the A envelope is the main programmable basis for the NIP, the 10th EDF also includes an Investment Facility, which is an instrument managed by the European Investment Bank. The Investment Facility is not part of the NIP.

Some specific activities may be supported by the Centre for the Development of Enterprise (CDE) and the Centre for the Development of Agriculture (CTA).

### **1.2.4 10th EDF regional indicative programme:**

This allocation will cover long term programmable development operations under the regional strategy for the Pacific. The allocation is not part of the Indicative Programme but may have repercussions at national level depending on the participation of Timor-Leste in the programmes proposed under the regional framework.

### **1.2.5 Other financial instruments**

Specific activities may be supported by external actions funded by the general budget of the European Community carried out under the financial framework for 2007-2013 subject to special procedure and availability of funds, and out of the own resources of the EIB. Actions funded by the general budget include, among others, programmes funded under the Development Cooperation Instrument such as the thematic programmes "investing in people", "non-state actors in development", "migration and asylum", "environment and sustainable management of natural resources, including energy" and "food security", as well as actions funded from other instruments such as the stability instrument, the instrument for the promotion of human rights and democracy or the instrument for humanitarian and emergency assistance.

### **1.2.6 Monitoring and evaluation**

Monitoring of results and evaluations of impact of individual activities (programmes, projects, sectors) under this CSP will be undertaken in line with the Technical and Administrative Provisions that are attached to each individual Financial Agreement prepared to implement this CSP.

The results and impact of the Community's cooperation with Timor-Leste implemented through the NIP and through other external actions funded by the general budget of the European Community, will be assessed by means of an independent external evaluation. This country-level evaluation may be undertaken jointly with EU Member States and possibly also with other donor agencies.

## **1.3 Focal sectors**

### **Focal sector 1: Sustainable rural development**

#### **Context/Strategy:**

Agriculture and livestock make up 80% of all self-employment and account for one fifth of non-oil GDP. 30% of households rely on subsistence agriculture alone and are facing food

insecurity every year. While the Ministry of Agriculture ranks food security as the country's first priority, food production is the only sector of the economy outside the petroleum sector which can bring economic growth and therefore contribute to sustainable poverty reduction and unemployment reduction. Any significant improvements in food security will only come from increased efforts in upland and dry land areas, which produce the bulk of food supplies, but remain the poorest in the country.

It will be critical to adopt a broad-based cross-sectoral approach including various ministries beside the Ministry of Agriculture and Fisheries (MAF). Cross-sectoral programmes include among other rural roads (Ministry of Infrastructures), water resources and electricity (Ministry of Natural Resources), support to the private sector (Ministry of Economy and Development) and environment (Secretary of State for Environment and Reforestation in the Ministry of Economy and Development). To improve agricultural production through services delivery in rural areas, one will have to support the MAF decentralization process and to address unemployment and acute problems of low rural productivity in a more sustainable way. This will serve at the same time both food security and economic growth purposes.

There are still many barriers to local rural women participating in secondary and informal education, and in benefiting from rural development programme activities. These barriers include social taboos, the low status of rural women and their domestic and reproductive work loads. Agricultural extension workers must include women who speak the local dialects.

The country will need to develop private sector and labour-intensive activities, particularly in rural areas where 86% of the poor live, targeting both internal (food) and external markets (niche products) and focusing on processing and value added activities. Several causes of low productivity find their origin in poor degraded soils in hilly areas and lack of water, and are therefore typically on-farm problems. They can only be addressed if improved farming practices are available for dissemination and if a delivery mechanism (extension service) exists. Private initiative is considered as the main source of sustainable future employment but business faces in TL formidable obstacles. Incomplete regulatory framework, unclear and cumbersome administrative procedures, high cost for labour and electricity (where available), poorly developed infrastructure and growing corruption pose significant challenges to business development.

The sustainable rural development component will build on the experience of former EC programmes in the same sector and will complement the Commission's ongoing Rural Development Programmes under the ALA budget line (RDP I and II), the 9<sup>th</sup> EDF CSP/NIP (RDP III) as well as the Nutrition and Food Security programmes. Besides agriculture related activities geared towards increasing production, the program will contribute to the creation of an enabling environment which will increase productivity and economic growth as it will improve access and rural roads, supply small scale hydro-electric plants and solar panels and implement rural water supply schemes. Specifically the 9<sup>th</sup> EDF survey of rural roads, which is complementary to the ADB survey of national roads will provide priorities for rural network development and maintenance systems. This survey will be carried out in the context of the soon to be started Rural Development Programme III. The development of a trade policy under the 9<sup>th</sup> EDF could also provide inputs for the development of norms and standards to be applied for possible exports.

Specific objectives:

The following specific objectives will be pursued: Improved food security and livelihoods of the rural population



### Possible activities:

The main actions proposed are:

- Agricultural production and extension activities , including training and sensitization in sustainable techniques for conserving natural resources, and possibly deforestation and integrated water resources management
- Development of links between producers and traders and appropriate financial institutions
- Development of rural roads and rural infrastructure notably in the fields of sustainable energy and water supply
- Strengthening the extension and support services of MAF to improve service delivery.
- Capacity development in MAF and possibly other Ministries involved in the programme
- Skills enhancement on central and local level (provision of on-the-job trainings)

These activities are indicative and will be agreed during the formulation phase of the project.

### Expected results:

The expected results are: Improved policy and planning capacity in Ministry of Agriculture and possibly other Ministries involved in the programme, improved farming systems including agro-forestry, improved service delivery, improved agricultural diversification, agro-industry and agri-business developed, improved livestock production, improved job creation/local labour markets, improved access to rural roads, improved sustainable and affordable access to energy services taking into account energy efficient objectives, and improved water supply. GoTL decentralisation policy will be supported in this sector.

### Funding and implementation arrangements:

As an indicative amount, € 35 million will be set aside for this focal sector.

The support to this focal sector is conceived as a programme based approach supporting the implementation of the “Policy and Strategic Framework” Programme of the Ministry of Agriculture and the strategy of the Ministry of Infrastructures. It will also aim at supporting the Ministries in implementing their increased domestic budget.

The main sectoral policy measures to be taken by GoTL as a contribution to the implementation of the response strategy in this field: The MAF is busy drafting various policies related to seeds, fertilisers and pesticides. Other policies will soon be dealt with: livestock, land use, extension and forestry.

Cross-cutting issues, notably gender equality, the promotion of human rights, children’s rights and the rights of indigenous people, environmental sustainability and combating HIV/AIDS, will be essential aspects to be taken into account throughout the programme. The main commitments by GoTL to ensure mainstreaming of the crosscutting issues are dealt with in the CSP.

Decent work and internationally agreed core labour standards will be respected throughout the NIP. The Ministry for labour and employment issues will be closely involved.

In view of the fact that part of the proposed actions will affect and impact different natural resources, a multi sectoral approach will be necessary. In order to avoid potential negative impacts a Strategic Environmental Assessment will be carried out. This study will take into consideration biodiversity and water resources as well as climate change variability.

## **Focal sector 2: Health**

### Context/Strategy:

The Ministry of Health with the assistance of the ongoing EC health sector programme, has elaborated a draft National Health Sector Strategic Plan (HSSP) and a Medium Term Expenditure Framework (MTEF). These documents will be agreed upon by the Ministry's Council of Coordination and will contain well defined mechanisms for donors' coordination. Any future sector support program would support the delivery of health services throughout the country at the district level and below. High priority target groups would be women and children. The duration of such a needed support is estimated at a minimum of 5 to a more realistically 10-15 years period.

### Specific objective:

Contribute to the sustainable improvement of the health status of the Timorese population.

### Possible activities:

Strengthening of preventive and primary health care

Improvement of primary health care activities on district level (target according to health sector plan: 60% of recurrent expenditures devoted to district level)

Training of medical and administrative staff

Training of population in health related decision making

These activities are indicative and will be agreed during the formulation phase of the project.

### Expected results:

The expected results are: improved availability, accessibility and affordability of health services to all people in TL; improved participation by the communities and other stakeholders in health related decision making. The GoTL decentralisation process is particularly supported in this sector.

### Funding and implementation arrangements:

As an indicative amount, approximately € 8 million will be set aside for this field depending on the financial gap identified in the MTEF which is being elaborated in the framework of the ongoing EC funded Support to the Implementation of the Health Sector Investment Program (SIHSIP).

The implementation modality – project support, co-financing or sector budget support – will be decided in light of coordination with other donors and assessment of needs and management capacities.

The main sectoral policy measures to be taken by the GoTL as a contribution to the implementation of the response strategy in this field will be available in the forthcoming Health Sector Strategic Plan (HSSP). Related measures, quantification, timetable, result and impact indicators will also be available in the HSSP.

Cross-cutting issues, notably gender equality, children's rights (women and children as a high priority target group), and combating HIV/AIDS, will be essential aspects to be taken into account throughout the programme. The main commitments by GoTL to ensure mainstreaming of the crosscutting issues are dealt with in the CSP.

Decent work and internationally agreed core labour standards will be respected throughout the NIP. The Ministry for labour and employment issues will be closely involved.

The proposed programme will be screened to determine whether an environmental impact assessment is needed or not. In any case, environmental considerations will be mainstreamed from the early stages of identification and formulation in order to ensure sustainable development.

### **Focal sector 3: Institutional capacity building:**

#### Context/Strategy:

Timor-Leste is now moving beyond the transitional substitution of international for local expertise and giving the preference to a more integrated approach to institution building.

The support to the sector shall assist in strengthening capacity in key areas, such as state administration and judiciary.

Strengthening the functioning of the National Parliament is a task which the international donor community has largely neglected until now. Even though constitutionally the Parliament has a pre-eminent position in the national system of governance, in practice its role and influence is limited due to a number of constraints ranging from insufficient office facilities and translation and interpretation services to poor in-house law-making capacity.

In October 2006 GoTL under the Ministry of State Administration launched a reform policy on decentralization and local government. This process will be supported through reinforcement of capacity at decentralised level. This component is cross cutting and needs to be addressed in the other two focal sectors as well.

#### Specific objective:

Contribute to the development of institutional, organisational and human capacities of the pillars of the State

#### Possible activities:

The main actions proposed are:

- Judiciary: building the capacities of personnel (training of judges and lawyers) and institutions (reinforcement of tribunals and various courts);
- State Administration: actions to improve the capacities and performance of the civil service; actions to make systems and processes more effective, including through support for decentralization processes (in coordination with activities in other two focal sectors);
- National Parliament: actions to develop its institutional capacities to enable it to fulfil its formal mandate under the Constitution (strengthening in-house support systems and processes);
- Support to communication with the aim of fostering understanding and information within institutions and with the population. This will be done through national and community radio as well as other available media;
- Support to NAO's office as a measure to effectively implement the EC programme in all sectors.

These activities are indicative and will be agreed during the formulation phase of the project.

#### Expected results:

The expected results are: Improved institutional, organisational and human capacities of the Judiciary, State Administration and the National Parliament enabling them to ensure transparent and timely access to justice for all citizens, to ensure full service delivery and adherence to a clearly articulated set of principles for good governance as well as continuous oversight of government activities and expenditures and the initiation and the drafting of laws.

#### Funding for analysis of the root causes of instability

As Timor-Leste is a country in a post-conflict situation the support to the different sectors shall take account of the underlying causes which contributed to the conflict. As mentioned in the Country Strategy Paper lack of communication between political leaders and people, demand for justice and increased poverty are among the factors that need to be addressed. A further analysis of the root causes of instability and recommendations how to use the resources of the country for a sustained pro-poor development is essential as well as possible follow-up measures of any already existing analysis. Part of the EDF or any other instrument shall be used for this.

#### Funding and implementation arrangements:

As an indicative amount, approximately € 13 million will be set aside for this area.

The implementation modality – project support or co-financing of multi-donor programmes – will be decided in light of coordination with other donors and assessment of needs and management capacities.

The proposed programme will be screened to determine whether an environmental impact assessment is needed or not. In any case, environmental considerations will be mainstreamed from the early stages of identification and formulation in order to ensure sustainable development.

### **1.4 General budget support**

The indicative programme does not provide for general budget support. However, in the light of changing needs, it may be decided to reallocate funds from other implementation modalities in the NIP to this type of support. Such a decision can be taken in the form of a specific agreement between the Chief Authorising Officer and the National Authorising Officer or within the context of an operational, mid-term, final or ad hoc review. Depending on the design of the health sector support being carried out by the WB and Ausaid, the EC may decide to provide sector support directly through the Ministry of Health.

### **1.5 Other programmes**

An indicative amount of € 7 million is set aside for support outside the three focal areas. The following actions are foreseen:

- Support for Non-State Actors (NSA):

The following categories of NSA will be eligible for EC support:

- Network of Community Based Organisations (CBOs): capacity building to improve their own organisational and managerial set up and their competency/efficiency in delivering required support services to their members. Criteria for representative network participation to be observed.

- Civil society organisations (CSOs) that set up themselves independently to improve the conditions of the society as a whole or of certain groupings within the society: strengthening the institutional capacity of CSOs to engage in meaningful policy dialogue with both the State and elected bodies for enhanced democratic governance.
- Support to Non-State Actors in service delivery (also private sector associations to increase their institutional and managerial capacity to support private businesses).

In this context HIV/Aids awareness, gender or environmental initiatives of NGOs can be supported.

- **Technical Cooperation Facility:** This facility shall be used to identify new projects and to allow for seminars and workshops with a particular importance for technical assistance for trade policy issues or SPS measures. This may also include assistance to the National Statistics Directorate (Direcção Nacional de Estatística) and the relevant sectoral ministries.

- PALOP/Timor-Leste Governance based Initiatives:

Activities in support for the area of governance will be considered, in particular in the areas of political (democratic and rule of law), economic and social governance as well as government effectiveness. Special emphasis will be placed on joint capacity building actions as enabling factor for facilitating successful implementation of national development and poverty reduction strategies, including through effective delivery of public services, particularly to the benefit of the poorer strata of the population. In these areas, the PALOP countries and Timor-Leste will continue to benefit from sharing experience and knowledge, as well as developing jointly replies to commonly identified needs.

The general orientations and modalities of this cooperation are established in a separate Memorandum of Understanding signed between the PALOP, Timor-Leste and the European Commission.

The National Authorising Officer contributing to a project co-financed by the other countries participating in this cooperation, delegates his functions for the implementation of this project to the National Authorising Officer "Chef de File" within the limits necessary for that purpose.

Assistance with statistical reporting in the relevant authorities (Statistics Directorate and line ministries) in cooperation with the other PALOP countries could be a possible support area.

## **1.6 Intervention Framework**

Indicators are covered in the log-frame. However, whilst national economic indicators will be available, those relating to poverty levels, especially in rural areas, will require specific surveys to reveal progress. Certain social indicators including MDG targets are also likely to be unavailable, although in the education and health sectors more data should be available as a result of improved data collection systems being implemented. Environmental indicators are likely to be largely qualitative.

### Intervention Framework and Performance Indicators

	<b>Intervention Logic</b>	<b>Objectively Verifiable Indicators</b>	<b>Sources of Verification</b>	<b>Assumptions</b>
<b>Overall Objectives</b>	To contribute to poverty alleviation and socio-economic development in particular in the poorer areas of the country	<ul style="list-style-type: none"> <li>• MDG indicators</li> <li>• Household consumption and income</li> </ul>	<ul style="list-style-type: none"> <li>• GoTL statistics;</li> <li>• Donors reports</li> </ul>	The new Government will be committed to political and macroeconomic stability; No major environmental disasters
<b>Programme Purpose</b>	To assist GoTL in the following: <ol style="list-style-type: none"> <li>1) Improving agricultural policy, production and services</li> <li>2) Improving health services in the country</li> <li>3) Improving institutional capacity in justice and parliament and enhance the efficient delivery of services</li> </ol>	<ul style="list-style-type: none"> <li>• Provision of wide range of services</li> <li>• Per capita income in rural areas</li> <li>• Health status of population</li> <li>• Municipal administration equipped with resources to properly carry out their tasks</li> </ul>	<ul style="list-style-type: none"> <li>• Baseline data</li> <li>• Rural household surveys</li> <li>• Programme reports</li> </ul>	Continued priority will be given by the Government to agriculture and rural development and health  Governments at all levels will be willing to enhance a conducive environment for service delivery  Political situation remains stable

	<b>Intervention Logic</b>	<b>Objectively Verifiable Indicators</b>	<b>Sources of Verification</b>	<b>Assumptions</b>
	<p><b><u>Focal sector</u></b>  <b><u>No.1:</u></b>  <b><u>Rural</u></b>  <b><u>Development</u></b>            To achieve sustained poverty reduction and food security as a result of positive contribution to rural livelihoods and rural socio-economic development and improved services</p>	<p>New production techniques            Establishment of links between producers and traders under inclusion of financial services            Access to village based infrastructure</p>		

<b>Results</b>				
1	Improved policy and planning capacity in Ministry of Agriculture and Fisheries (MAF) and Ministry of Infrastructure and any other involved in programme	<p>1.1 A MAF policy planning document is provided with policies related to seeds, fertilisers, pesticides            1.2 Other policies to be dealt with: livestock, land use, extension services and forestry            1.3 Decentralisation aspects in policy planning            1.4 Decision processes for implementation of rural roads component (Ministry of Infrastructures)</p>	<p>MAF policy document             Policy and Planning documents of other Ministries involved</p>	
2	Improved agriculture techniques,	2.1 Quality of agricultural production , including development of suitable cash crops	MAF statistics;	

	diversification and output for consumption and sale for rural communities in the target areas.	2.2 New crops 2.3 No. of commodity processing units 2.4 No. of storage places	Donor reports; EC reporting and ad hoc evaluations	
3	Increased earnings for rural communities in the targeted areas due to improved access to markets (rural roads and to private sector (e.g. microcredit institutions))	3.1 Rural roads provide accessibility to services and access to markets 3.2 Links between farmers and markets	MAF statistics Donor reports EC reporting and ad hoc evaluations	Farmers assume ownership of the programme, no major climatic disasters  Sufficient linkages of supply and demand side
4	Extended and/or improved access to clean water, sanitation, and energy sources in targeted rural areas.	4.1 Village infrastructure and services (no of kilometres of road, no of hydroelectric plants, new water supply schemes)	MAF/ Ministry of Infrastructures statistics Donor reports  EC reporting and ad hoc evaluations	Adequate maintenance by GoTL of rural infrastructure  Adequate maintenance and management of community facilities
	<b><u>Focal sector</u></b> <b><u>No.2:Health</u></b>  Contribute to the sustainable improvement of the health status of the Timorese population	Health indicators for maternal and child mortality	Government Annual action plans and statistics from major ministries and donors (e.g. World Bank, IMF)	



			EC-TL Joint Annual Reports	
<b>Results</b>				
5	Improved availability, accessibility and affordability of health services (also in relation to decentralisation)	5.1 New hospitals and health units 5.2 Availability of drugs and vaccines 5.3 Medical staff (doctors and nurses)	Ministry of Health (MoH) reports; statistics; Donor reports	
6	Improved participation of communities and other stakeholders in health related decision-making (as part of decentralisation)	6.1 Role and responsibility for communities in health care 6.2 No. of trained persons to work in community mobilisation around campaigns	Document to formalise roles and responsibilities; Training plans, MoH reports	
	<b><u>Focal sector No. 3: Capacity building</u></b> To assist the state of Timor-Leste in building up its capacity in Parliament, justice and state administration (municipalities level)	<ul style="list-style-type: none"> <li>• System of checks and balances and timely approval process of budget</li> <li>• More efficient functioning of justice</li> <li>• Municipal administration equipped with resources to properly carry out their tasks</li> </ul>	Government Annual action plans and statistics from major ministries and donors (e.g. World Bank, IMF)  EC-TL Joint Annual	Internal stability is maintained International cooperation is not reduced in the short term No natural disasters occur The Government is able to recruit and maintain managerial staff for vacant posts

			Reports	
Results				
7	Functioning of judiciary strengthened	7.1 Increase of no of staff in judiciary in defined periods  7.2 Percentage of reduction of backlog of unresolved cases	Plans and actual staffing figures in Ministry of Justice; Reports of Ministry of Justice	
8	Functioning of national parliament strengthened	8.1 Control mechanisms (checks and balances) to control executive  8.2 Time span of approval process of national budget	Reports of Parliament	
9	Improved capacity at decentralised level (support to the decentralisation policy) <i>also to be seen in connection with support to decentralisation in agriculture and health programmes</i>	9.1 Provision of human resources at municipalities level (No. of staff)  9.2 Access of people to full range of services on municipal level (defined percentage of service coverage over period)	Reports of Ministry	

## 1.7 Timetable of indicative commitments and disbursements

### 1.7.1 Indicative timetable of global commitments

	Indicative allocation	2008		2009		2010	
		1	2	1	2	1	2
<b>1<sup>st</sup> FOCAL SECTOR</b>							
- Sustainable rural development	€35,000,000						€35,000,000
<b>2<sup>nd</sup> FOCAL SECTOR</b>							
- Health	€8,000,000				€8,000,000		
<b>3<sup>rd</sup> FOCAL SECTOR</b>							
- Institutional Capacity building incl. Support to Parliament, support to judiciary, support to state administration and support to NAO	€13,000,000				€6,000,000		€7,000,000
<b>NON FOCAL SECTORS</b>							
- Support to Non-state actors,	€4,000,000				€4,000,000		
- Technical Cooperation Facility	€3,000,000						€3,000,000
<b>Total Cumulative Commitments:</b>					€18,000,000		€63,000,000

### 1.7.2 Indicative timetable of disbursements

	Indicative allocation	2008		2009		2010	
		1	2	1	2	1	2
<b>1<sup>st</sup> FOCAL SECTOR</b>							
- Sustainable rural development	€35,000,000						
<b>2<sup>nd</sup> FOCAL SECTOR</b>							
- Health	€8,000,000					€2,000,000	
<b>3<sup>rd</sup> FOCAL SECTOR</b>							
- Institutional Capacity building incl. Support to Parliament, support to judiciary, support to state administration and support to NAO	€13,000,000					€3,000,000	
<b>NON FOCAL SECTORS</b>							
- Support to Non-state actors,	€4,000,000					€1,000,000	
- Technical Cooperation Facility	€3,000,000						
<b>Total Cumulative Commitments:</b>						<b>€6,000,000</b>	

### 1.8 Chronogramme of activities

1 <sup>st</sup> FOCAL AREA	Indicative Allocation	2008				2009				2010-->			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
- Sustainable rural development and capacity building	€35,00 M								FS		AF		FD
2 <sup>nd</sup> FOCAL AREA	€8,00 M	2008				2009				2010-->			
- Health		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
				FS		AF		FD					
3 <sup>rd</sup> FOCAL AREA	€13,00 M	2008				2009				2010 -->			
- Institutional capacity building incl. support to Parliament, support to judiciary, support to state administration and support to NAO (*)		Q1	Q2	Q3	Q4								
				FS		AF 1		FD		AF 2		FD	
								FS					
NON FOCAL AREAS)	€ 4,00 M	2008				2009				2010-->			
Support to Non-State Actors		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
				FS		AF		FD					
Technical Cooperation Facility	€ 3,00 M									FS	AF	FD	

FS: Feasibility Study  
 AF: Action Fiche  
 FD: Financing decision

(\*) This focal area is likely to result in more than one operation. Therefore more than one FD is envisaged.

NB: The adoption of Annual Action Plans (AAP) is needed for the implementation of the indicative programme, once approved by the Commission, the AAP will also serve as financing decision for all the actions contained therein.