

The fiscal policy objectives for 2024 set by the Government in the context of the 2024 Budget are aimed at setting the conditions for the establishment of budgetary balance over the long term: i) mobilising domestic revenues and introducing new tax incentives; ii) making increasing the use of alternative sources of financing such as concessional and commercial loans and treasury bills; iii) focusing government expenditure on quality over quantity through moving from traditional line-item budgeting and improving annual and medium-term program budgeting.

The Petroleum Fund's revenues mainly sustain the current account. That situation reflects the Timorese economy's structural weaknesses, namely the need for more diversification of its productive structure. Hydrocarbon exports represent 99% of goods exports; the remaining 1% is mainly coffee. From the import side, fuel and food represent half of the total imports, so the changes in international prices of those products strongly impact the current account. Another relevant current account inflow is the migrant's remittances, which reached US\$185 million in 2022, or 5.8% of GDP. This contrasts with the payments of US\$363 million to foreign workers in Timor-Leste. Foreign direct investment (FDI) and portfolio investment are the primary capital inflows. However, the capital inflow could be more significant, reflecting a low level of attractiveness of private investment in TL.

The macroeconomic projections made by the IMF show steady economic growth for Timor-Leste over the medium term, but this depends on stabilising the international economy and effectively mobilising the internal growth factors. The government's projections are around 3.5% over the next four years, but the risks of external shocks remain high. The main risks identified by international agencies that follow the economy of Timor-Leste's continuity of global prices of commodities, namely food and energy, significantly impact the population's cost of living. Moreover, a general decline in international financial market shares could reduce the Petroleum Fund's return duration.

The improvement of the medium-term prospects depends very much on resolving the economic and fiscal imbalances, with appropriate policies to ensure fiscal consolidation and the implementation of reforms to promote and stimulate economic growth and diversification. If the Greater Sunrise fields go into operation, an optimistic scenario could be anticipated. The respective exploration model, including the processing of natural gas, still needs to be developed, including a cost-benefit analysis and an agreement among the interested stakeholders needs to be established.

According to the WB, without major revenue reforms, the fiscal deficit is projected to hover at around 50% of GDP in the medium term. The government assumes, however, an optimistic approach regarding the duration of the Petroleum Fund. In the 2023 Budget Report, it is believed that the Petroleum Fund can last longer if some policy measures are taken. The government recognises that decisive policies are needed to tackle the structural imbalances of the public and external accounts. It has expressed the desire to implement these reforms, although they have faced substantial implementation hurdles. Precisely, the Strategic Development Plan 2011-2030, as well as the Major Plan Options that the VIII Government and Parliament have approved, reflect the political and policy commitments by the executive to advance the reforms.

The Strategic Development Plan 2011-2030 envisages the diversification of the economy, led by the private sector while expressing the government's willingness to use its oil financial resources in a balanced and sustainable fiscal framework. This plan has been recently revised, and a new version, the Readjusted Strategic Development Plan (PEDR) 2023-2028, has been approved.

The strategic objectives are in line with the recommendations of international partners and point to i) increased domestic revenue mobilisation, including the adoption of VAT; ii) rationalisation of the public expenditure through the stabilisation, over the medium-long term, of the ratio of public expenditure/non-oil GDP; iii) improvement of the public investment management through better appraisal, selection, and prioritisation of projects; iv) reduction of the Petroleum Fund withdrawals as a mean to secure fiscal sustainability while preserving the Fund's assets; v) structural reforms to improve the business environment, including progress in facilitating the ease of doing business, addressing digital infrastructure and connectivity bottlenecks, increasing financial assets, building human capacity and strengthening the justice sector.