audited estimate of the amount that can be sustainably drawn down each year from the Fund in perpetuity. That amount is currently around US$500 million, but will fall inexorably each year as government draws down on the principal of the Fund.

The government's expansionary spending program is driven by an ambition to overhaul the nation's public infrastructure in order to crowd-in private sector investment and boost long-term growth prospects. While this represents a viable economic strategy in principal, it is dependent on the quality of the investments being made, and that public investment is indeed the binding constraint to private sector development. There are indications of limited capacity to implement the program, with execution rates for the infrastructure budget low and increasingly high prices demanded for construction works. A combination of marginal investments and high costs also raise important questions of the quality and prioritization of the investment program. One 30km stretch of road currently under construction in an underpopulated, rural area of the country costs an average of US$10 million per kilometer (compared to a norm of US$1–2m).

Timor-Leste's only significant non-oil export product is coffee. Export values and volumes fell from US$18.8 million (34m kg) in 2012 to US$13.8 million (10.2m kg) in 2014 with production recovering in 2015 to US$15.2 million (19.2m kg). Overall, the current account surplus has declined along with falling oil exports, from 44 percent of GDP in 2013 to 13 percent in 2015.

Outlook

In 2016 and 2017, domestic growth is expected to continue in a similar range as the last two years, with growth forecast at 5.0 and 5.5 percent, respectively. While strong government spending, especially on infrastructure investment, will continue to stimulate growth, foreign direct investment is expected to increase as well. The Government recently signed the concession agreement for its first public-private partnership which will see a major international operator invest US$150 million for the construction of a new container port near the capital city. Construction has also begun on a Heineken factory, and other potential investors are showing interest in some sectors.

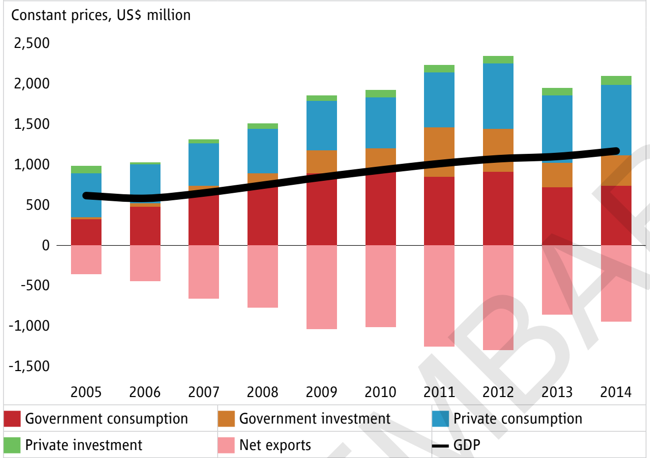
Development of the domestic economy will be essential. With no new oil fields under development and current wells depleting rapidly, Timor-Leste is expected to be a post-oil country in as little as five year's time. Oil production, exports and gross value added from the offshore oil sector will decline rapidly each year for the next few years.

The Government recently submitted a supplementary budget for the current fiscal year to appropriate additional expenditure financed by excess drawdowns from the Petroleum Fund. As a result the budget deficit is expected to widen considerably in 2016 to more than 20 percent of GDP. In 2017 the budget deficit is forecast to widen even further as revenues from the oil sector decline.

Risks and Challenges

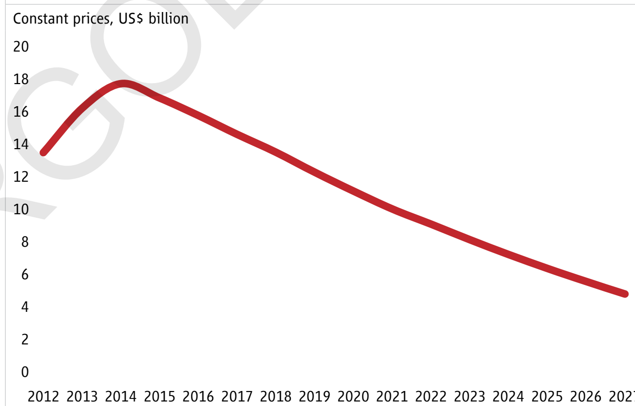
The government has focused a considerable amount of their resources and focused their political agenda on supporting improvements in physical infrastructure nationwide. Achieving the best results in terms of long-lasting economic and social impacts will require an effective management of the public investment program to ensure that projects are prioritized that have a high return and support steady and rapid progress along a viable path of economic development. This task requires careful planning, backed up by solid analysis, including of complementary investments in skill development and technology adoption required to ensure that infrastructure investments pay-offs are high. Introducing quality and productivity enhancing technologies in coffee production, for example, can potentially benefit a large number of small farmers. Existing financial assets should also be used as effectively as possible. The investment strategy of the Petroleum Fund should be in line with the Government's use of the fund. A recent shift to invest more heavily in higher-risk equities is seemingly at odds with the Government's strategy of drawing down on the Fund's principal in the short-term. Securing a return, even a modest one, is a priority. Financial reports show the Petroleum Fund made a net loss on its assets in 2015. While Timor-Leste faces a daunting infrastructure gap, there are a variety of other constraints that would also need to be addressed to support private-sector-led, inclusive growth. Timor-Leste still ranks as having one of the least conducive regulatory environments for business in the world. A lack of functioning state systems of identification, registration, and dispute resolution over land title make it extremely difficult to secure a claim over land, and it is difficult to see how businesses could commit to investments in this context. The lack of laws governing the enforcement of commercial and credit contracts also make doing business much more difficult. While Timor-Leste has much to offer, concerted effort is needed to address these critical constraints before it can realistically expect to attract large-scale foreign investment and spur domestic enterprise.

Figure 1. Gross domestic product, expenditure components



Sources: Government of Timor-Leste and World Bank staff estimates.

Figure 2. Projected petroleum fund balance



Sources: Government of Timor-Leste and World Bank staff estimates.

TIMOR-LESTE Selected Indicators	*2013*	*2014*	*2015e*	*2016f*	*2017f*	*2018f*
Real GDP growth, at constant market prices	2.8	5.9	4.3	5.0	5.5	6.0
Exports, goods and services, US$ million[a]	87.9	89.3	91.6	100.0	113.0	128.0
Imports, goods and services, US$ million	1,139	1,286	1,198	1,297	1,605	1,668
Consumer Price Inflation (annual average % change)	9.5	0.7	0.6	0.5	3.0	4.0
Current Account Balance (% of GDP)	43.6	26.2	13.3	2.0	-11.9	-12.2
Fiscal Balance (% of GDP)[b]	41.7	21.8	-8.7	-23.7	-29.5	-27.7

Sources: National authorities and World Bank staff estimates.
Note: f = forecast. a) exports exclude offshore petroleum shipments; b) overall fiscal balance as a proportion of total GDP, including petroleum sector.