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PROJECT PERFORMANCE ASSESSMENT REPORT

TIMOR LESTE

FIRST TRANSITION SUPPORT PROGRAM (P075796)

SECOND TRANSITION SUPPORT PROGRAM (P082190)

THIRD TRANSITION SUPPORT PROGRAM (P083894)

June 30, 2008

Country Evaluation and Regional Relations
Independent Evaluation Group (World Bank)

Currency Equivalents (annual averages)

Currency Unit = US Dollar

Abbreviations and Acronyms

AAP	Annual Action Plan
BCG	Bocillus Calmett-Guerin
CAS	Country Assistance Strategy
CEM	Country Economic Memorandum
CSP	Consolidation Support Program
ES	Evaluation Summary
ICR	Implementation Completion Report
IEG	Independent Evaluation Group
IMF	International Monetary Fund
JAM	Joint Assessment Mission
LDP	Letter of Development Policy
MFP	Ministry of Finance and Planning
NDP	National Development Plan
PAD	Project Appraisal Document
PAL	Programmatic Adjustment Loan
PEMA	Public Expenditure and Management Accountability
PPAR	Project Performance Assessment Report
PSR	Project Supervision Report
TFET	Trust Fund for East Timor
TSP	Transition Support Program
TSS	Transitional Support Strategy
UN	United Nations

Fiscal Year

Government: July 1– June 30

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Bank Performance: The extent to which services provided by the Bank ensured quality at entry of the operation and supported effective implementation through appropriate supervision (including ensuring adequate transition arrangements for regular operation of supported activities after loan/credit closing, toward the achievement of development outcomes. The rating has two dimensions: quality at entry and quality of supervision. *Possible ratings for Bank Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Borrower Performance: The extent to which the borrower (including the government and implementing agency or agencies) ensured quality of preparation and implementation, and complied with covenants and agreements, toward the achievement of development outcomes. The rating has two dimensions: government performance and implementing agency(ies) performance. *Possible ratings for Borrower Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

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Principal Ratings

	ICR[1/]	*ICR Review*[1/]	*PPAR*
First Transition Support Program (TSP I)*			
Outcome	--	--	Moderately Unsatisfactory
Risk to Development Outcome[2/]	--	--	Significant
Bank Performance	--	--	Moderately Unsatisfactory
Borrower Performance	--	--	Moderately Unsatisfactory
Second Transition Support Program (TSP II)			
Outcome	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Risk to Development Outcome[2/]	Moderate	Significant	Significant
Bank Performance	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Borrower Performance	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Third Transition Support Program (TSP III)			
Outcome	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Risk to Development Outcome[2/]	Low/Negligible	Significant	Significant
Bank Performance	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Borrower Performance	Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory

[1/] The Implementation Completion Report (ICR) is a self-evaluation by the responsible operational division of the Bank. The ICR Review is an intermediate IEGWB product that seeks to independently verify the findings of the ICR.
[2/] This rating was introduced as of July 1, 2006.
* Since this operation was funded from the Post-Conflict Development Grant Facility, only a Grant Completion Report was produced, with no ratings.

Key Staff Responsible

Project	*Task Manager/Leader*	*Division Chief/ Sector Director*	*Country Director*
First Transition Support Program (TSP I)			
Appraisal	Adrian Fozzard	Homi Kharas	Klaus Rohland
Completion	Adrian Fozzard	Homi Kharas	Klaus Rohland
Second Transition Support Program (TSP II)			
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Third Transition Support Program (TSP III)			
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Preface

This is a Project Performance Assessment Report (PPAR) on three operations in Timor-Leste (TL): the First Transition Support Program for FY2003 (TSP I), the Second Transition Support Program for FY2004 (TSP II), and the Third Transition Support Program for FY2005 (TSP III).

The three projects in the Transition Support Program series were chosen for a PPAR following a strong recommendation contained in the two ICR Reviews completed in September 2007 which suggested that a more detailed review with a field visit would distill:

i. Direct lessons learned that could help improve the design and implementation of the follow-on series of related projects in Timor Leste; and
ii. Insights and lessons of experience with wider applicability in designing better projects in other post-conflict countries.

TSP I was supported by a grant of $5.00 million from the Development Grant Facility (DGF). Co-financing by eight bilateral donors (the governments of: Australia, Canada, Finland, Ireland, New Zealand, Norway, the United Kingdom, and the United States of America) totaled about $23 million equivalent, and was channeled through Bank-administered Trust Funds. The Government of Portugal provided its own support of the program directly. TSP I was approved on July 22, 2002.

TSP II was supported by an IDA grant of SDR2.9 million ($4.16 million equivalent). Co-financing by the eight bilateral donors totaling $29 million equivalent was channeled through Bank-administered Trust Funds. An additional $3 million equivalent, also associated with this operation, was provided directly. The IDA grant was approved on July 22, 2003; became effective on October 10, 2003; and closed on October 31, 2004. It was disbursed in one tranche following effectiveness.

TSP III was supported by another IDA grant of SDR 3.4 million ($4.96 million equivalent). Co-financing by bilateral donors totaling $23.2 million equivalent was channeled through Bank-administered Trust Funds. An additional $3 million equivalent, also associated with this operation, was provided directly. The IDA grant was approved on October 28, 2004; became effective on December 8, 2004; and closed on October 31, 2005. It was disbursed in one tranche following effectiveness.

This PPAR is based on a review of relevant World Bank documents, including the Grant Completion Report for the first operation, the Implementation Completion Reports, and ICR reviews for the second and third operations. An Independent Evaluation Group (IEG) mission visited Dili in January 2008 to discuss the projects with Timorese officials, representatives of other donors and the Bank Office in Dili. Bank staff at headquarters were also consulted. Their cooperation and assistance in preparing this report is gratefully acknowledged.

The draft PPAR was sent to the Government of Timor-Leste for comments. No comments were received from the Government.

This report was prepared by Adil Kanaan (Consultant), in collaboration with Dusan Vujovic (Task Manager). Janice Joshi provided administrative support.

Summary

1. This PPAR reviewed a series of three inter-related operations in Timor-Leste over the 2003-2005 period, in support of the country's Transition Support Program (TSP). The first, TSP I (FY2003), was funded by a post-conflict grant from the Development Grant Facility. TSP II (FY2004) and TSP III (FY 2005) were both provided as IDA grants. These operations were part of a much broader international effort involving the United Nations, the IMF, the Asian Development Bank, and a group of about a dozen bilateral donors in support of this new country's initial reconstruction and development efforts. The IDA grants averaged around $5 million each, and their combined amount of about $15 million was part of an overall grant financing package of slightly over $90 million by all the co-financing partners (eight bilateral donors and IDA). The three IDA grants were disbursed in single tranches at effectiveness, following corresponding sets of completed prior actions. No prior conditionality was involved. The main objective of these fast-disbursing funds was to provide urgently needed bridge-financing to the budget until the expected increases revenues from recently discovered and developed oil and gas became available.

2. Timor-Leste gained its independence in May 2002, following about four centuries of colonization by Portugal, and twenty five years of Indonesian occupation. The resistance to the occupation and the events leading to independence witnessed severe destruction of economic structure and extreme violence and dislocation that left the country at a very primitive socio-economic state on the eve of its independence. Planning, policy and implementation capacity was among the poorest in the world.

3. The Government's TSP was based on its National Development Plan (NDP) and a number of related planning, budgeting and monitoring instruments. The main strategic objectives of the NDP, and of IDA's Country Assistance Strategy, were to promote sustainable economic growth and to reduce poverty. To that end, each of the three TSP operations was based on extensive, rather unwieldy, Action Matrices of specific measures in a wide range of policy, institutional, regulatory, and legislative areas. Measures that were not completed, or started, in one operation were taken up in the next operation. The broad components and coverage of all three operations were essentially the same (except for the power sector component which was dropped after the first operation). The three main components that were common to the whole series basically covered: (i) governance; (ii) service delivery, mainly in the health and education sectors, but including veterans' affairs; and (iii) job creation, through the private sector, work programs, and agriculture.

4. Implementation experience and outcomes under the individual operations, and in view of their interconnected nature, of the series as a group, was mixed. Good progress was made in establishing and running the Petroleum Fund, intended to safeguard the bulk of petroleum revenues against abuse and for future generations. In the health sector, the quantitative targets that were set were either met, or exceeded. Electricity metering and added capacity initially reduced the dependence of the power authority on budgetary transfers, but deteriorated following the 2006 political disturbances. In addition, the Government, the donor community, and the involved Bank staff all considered that putting in place the process and culture of planning, budgeting, and monitoring was in

itself a major achievement; as was the excellent donor coordination in which the Bank played a key role.

5. Most of the other areas covered by the Policy Action Matrices associated with the three TSP operations witnessed either partial, or poor, progress. The establishment, staffing, and initial phases of operation of the offices of the Ombudsman and the Inspector General was an achievement; although it is still too early to judge how effective they will be, or whether they deserved the level of priority they were accorded in program design and implementation. Budget execution has emerged as a major area of weakness and concern, in view of the very weak implementation capacity. Progress in the education sector has been modest, at best; and that in the areas of private sector development, the judicial sector, and agriculture disappointing, though partial. In addition, it does not seem like the three TSP operations funded by IDA have had any impact on economic growth or poverty reduction; nor on enhancing political stability.

6. In the ultimate analysis, one should not lose sight of where the country started from at the beginning of this new century. The dire conditions that existed at the time made it very difficult to make significant progress across a broad front. As such, the good progress made in a few key areas, combined with the partial progress made across the wider front, was certainly welcome. However, it must also be noted that a large portion of actions envisaged under the three TSP operations could not be completed by the respective closing dates. In the case of the third TSP, 41 percent of actions have not been completed and another 28 percent of actions were re-scheduled for the subsequent series of Bank operations (CSP). Based on that, this review gives a ranking of *moderately unsatisfactory* to overall outcome, and to Borrower and Bank performance; and assigns a ranking of *significant* to the risk to development outcome, in view of the uncertain political situation and the very limited capacity.

7. The main lessons learned from the experience under the three TSP operations are:

- In instances similar to those faced by Timor-Leste on the eve of its independence, and following a period of protracted conflict and devastation, the Bank should argue more strongly in favor of more focused and simpler program design, with tight priorities, especially for grants disbursed in one tranche for generalized budget support. If the Borrower feels strongly that it needs support for a broad-fronted program involving a large number of time-consuming institutional measures with a high technical assistance content, it would be preferable to provide a specific TA operation with a more appropriate (i.e. longer) implementation horizon.
- In cases like Timor-Leste where there is high political risk, due in large measure to high unemployment among disgruntled youth, efforts should be directed at creating jobs and achieving "quick wins" in poverty-related services, and through work programs; rather than dissipating efforts across a wide range of areas and measures, with little explicit priorities.
- Where capacity limitations are severe and TA is normally required to do the work itself, as well as to train a large number of personnel, it is probably more effective to provide TA which is dedicated entirely to training, in parallel to advisors who

actually do part of the work. Combining both functions in the same individual, though attractive in principle, often leads to situations where the advisors devote hardly any time to training, and therefore, building local capacity suffers.

- Quite often, but particularly in countries with limited qualified personnel, success is highly correlated with working with the more competent and committed counterparts. Therefore, where possible, it would be desirable for the Bank to focus its support around proven achievers, while seeking to develop institutional capacity.
- Despite its costs to the Government and its development partners, which can be high at times, the benefits of active donor coordination are often worthwhile and outweigh its costs, as demonstrated by the experience under the TSP program.

Cheryl W. Gray
Acting Director-General
Evaluation

1. Background and Context

Political Background

1.1 Timor-Leste occupies about 15 thousand square kilometers in the mountainous eastern half of the island of Timor. Originally, its population evolved from waves of migrations that characterized the Australasia region, including Austronesians and proto-Malays. The mountainous topography meant that the various groups could remain separate, and that explains the large linguistic and ethnic diversity in the country today.

1.2 Portugal colonized Timor-Leste in the sixteenth century, and remained there for about four centuries; imparting its language, initial institutional structures, and some cultural traits to the territory. After Portugal started its decolonization process in 1974, Timor-Leste declared its independence on November 28, 1975. Nine days later, it was occupied by Indonesia and incorporated into that country, without the recognition of the United Nations. The occupation faced stiff and popular resistance led by an armed movement, Falintil, and included groups of civilian supporters and representatives of the *diaspora*. The occupation was marked by extreme violence that wiped out about a third of the population.

1.3 Following a UN-sponsored agreement among Portugal, Indonesia and the United States, and a surprising offer by Indonesian President Habibie; a UN-supervised referendum was carried out on August 31, 1999. It offered the population a choice between independence, and an autonomous status within Indonesia. An overwhelming majority voted for independence. However, violent clashes broke out immediately, instigated primarily by the Indonesian military and involving Timorese pro-Indonesia militias. An international peacekeeping force, led by Australia, intervened to help restore order, and subsequently evolved into the United Nations Transitional Administration in East Timor (UNTAET) which ruled from September 1999 to May 20, 2002. On May 20, 2002, Timor Leste became a sovereign nation and inaugurated its first Government and joined the UN on September 27, 2002. But this independence was bought at a very heavy price, following more than 25 years of turbulence: the brutal violence surrounding the 1999 referendum witnessed the death of more than a thousand people, the displacement of the majority of the population, and the destruction of most of the physical infrastructure.

1.4 Compared to the turbulent years of the Indonesian occupation that culminated in the marked violence surrounding the 1999 referendum, the short post-independence period started out with some signs of relative stability, for a new country emerging from serious conflicts. Unfortunately, the risks to this stability has continued to be felt due to several factors: the continued presence of the hard-core pro-Indonesia militia in West Timor, fault lines among the country's internal factions themselves, serious problems within the security forces, and the spread of violence by martial arts youth groups. Although these risks could conceivably be contained by a combination of internal diplomacy, security enforcement, and economic policies; they do represent a source of considerable uncertainty and potential upheaval. Recent examples of continued turbulence and violence included the aftermath of the riots that broke out in Dili in April 2006, which were triggered by the dismissal of soldiers who were accused of desertion;

the violence in conjunction with the presidential elections in 2007; and attempts to assassinate the President and Prime Minister in February 2008. Such incidents themselves, as well as the atmosphere of unresolved tensions and problems that breeds them, can certainly become a major drag on economic development efforts in the immediate future.

Economic Background

1.5 ***Overall Economic Developments.*** Aside from some commercial coffee plantations established by the Portuguese at the end of the nineteenth century; a rather primitive, subsistence, mainly agrarian economy prevailed before and throughout the colonization period. There were modest exports of coffee, sandalwood, wax, and honey. Timor-Leste was the least developed of all of Portugal's colonies. It received meager subsidies from Lisbon, and as late as the 1970s, basic education was still being generalized to cover the whole territory, and the first set of tarmac roads was being built.

1.6 Unfortunately, whatever limited progress had been made close to the end of the twentieth century, was drastically set back during the 1999 violence. According to the June, 2005 Country Assistance Strategy (CAS), "An estimated 70 percent of private homes and public buildings were burned to the ground. Bridges and power lines were demolished, and the telecommunications system was rendered inoperable. Valuable files, including land and property titles, civil registry, and education records were destroyed. Following the 1999 referendum, most Indonesian citizens left the territory, resulting in a severe shortage of qualified and experienced professionals. The country was left with only two power engineers, 20 percent of its secondary school teachers, 23 medical doctors including one surgeon, and not a single qualified pharmacist." **It is very important that this dire state of affairs that existed at the time when the country started its development drive, be frontally kept in mind when evaluating progress to-date, as well as assessing achievements by the Government and its development partners, including the Bank.**

1.7 Evaluating economic performance during the years leading up to, and immediately following, independence is hampered by the absence, or poor quality of data. This has been highlighted by successive IMF Article IV Consultations missions, including that of 2007. With this general caveat in mind, the documents reviewed paint a broad picture of overall macroeconomic performance during the 1999-2003 period, on the eve of the preparation and processing of TSP I, the first of the three operations reviewed in this report (Table 1).

1.8 The output figures confirm that Timor-Leste was among the poorest countries of the world, with a per capita GNP of around $375 in 2003. Real non-oil output declined precipitously in 1999 (by 35 percent) due to the heavy destruction caused by the severe violence that year. It rebounded by a significant 15 percent in each of 2000 and 2001, due primarily to a large influx of expatriates brought in under UN auspices to help with security and economic development. It declined sharply in 2002, and became negative in 200 3, as the presence of the expatriate community dwindled. Such severe fluctuations reflect the extreme thinness and fragility of the country's economic base, and its acute dependence on political stability.

Table 1: Selected Macroeconomic Indicators 1999-2006 ($million current prices)

	1999	2000	2001	2002	2003	2004	2005	2006
Output								
GNI at current prices (in millions of US$)	270	319	373	352	349	507	692	848
Non-oil GDP	270	316	368	343	336	339	350	356
Oil/Gas Income	0	3	5	9	13	168	342	492
Memorandum Items								
Real non-oil GDP Growth (%)	-35	15.4	16.6	-6.7	-6.2	0.3	2.3	-1.6
Inflation (%)	140	3.0	-0.3	9.5	4.2	1.8	0.9	5.7
Public Finance	(In percent of non-oil GDP)							
Revenues		18	16	17	21	23	12	13
Expenditures		69	70	71	70	68	62	71
Recurrent		35	38	54	55	52	47	53
Capital		34	32	18	15	15	15	18
Overall balance		-52	-53	-54	-50	-45	-50	-58
External Sector	(In percent of non-oil GDP)							
Trade balance	-25	-75	-76	-62	-55	-46	-36	-38
Merchandise Export	19	2	1	2	2	2	3	2
Merchandise Import	-44	-77	-77	-63	-58	-48	-39	-40
CAB (excluding international assistance)	-34	-87	-86	-71	-62	-4	55	93
CAB (including international assistance)	2	12	13	-37	-25	30	84	116
Overall balance	0	5	2	6	5	36	97	136

Source: IMF, Article IV Consultation Report: 2004, 2005 and 2006.

1.9 The thinness and fragility are also reflected in the public finances and the balance of payments. Both suffered from significant deficits due to meager levels of public revenues (in the case of the budget) and export earnings (in the case of the external account). Both deficits were essentially financed by grant funding from the donor community.

1.10 ***Poverty.*** A Household Survey, a Village Survey, and a Participatory Poverty Assessment were carried out in 2001. They helped quantify the level and nature of poverty and social services. They also confirmed the general belief that poverty was among the highest in the world, and social services among the lowest. About 40 percent of the population was found to be poor. The incidence of poverty was much worse in rural areas (nearly 46 percent) than in urban locations (about 26 percent). It was worst in the rural west and center of the country. About 85 percent of the poor lived in rural areas.

1.11 Poverty was exacerbated by the 1999 violence and destruction of key assets like dwellings and livestock, particularly in the western border areas. Food security was worsened as a result, leading to malnourishment of about half of the child population. A long history of under-investment in public services had led to very poor social indicators. For example, almost half of the adult population had never attended school, 46 percent could not read, and vaccination rates for *Bacillus Calmette-Guerin* (BCG) were 41 percent in urban centers and only 27 percent in rural areas.

1.12 Despite some recovery in the provision of public services that were noted in the surveys, their coverage and quality remained very poor, and represented a major challenge for the years ahead. The most important improvements since 1999, according to the participants in the surveys, had been in the levels of security and political participation; although subsequent events in 2006 and 2007 may prove this conclusion premature, at least with regard to security.

1.13 ***Oil and Gas.*** Prior to independence, oil and gas fields were discovered offshore between Timor-Leste and Australia, in an area of disputed sovereignty known as the Timor Gap. Commercial exploitation is currently governed by the Timor Sea Treaty between the two countries, which has been in effect since April 2, 2003. Under this treaty, the Timor Gap is divided into three areas: (a) the Joint Petroleum Development Area (JPDA), (b) the area under exclusive Australian jurisdiction, and (c) the area under exclusive Timor-Leste jurisdiction. Also under this treaty, Timor-Leste's revenue share in the JPDA was increased significantly to 90 percent, from 50 percent in the previous treaty.

1.14 Three fields have been discovered so far: EKKN, Bayu-Undan, and Greater Sunrise. EKKN was developed first, with production starting in 1998, and generating modest revenues from royalties and taxes. Bayu-Undan, which is located entirely in the JPDA, is estimated to contain 370 million barrels of condensate and LPG, and 2.7 trillion cubic feet of gas. Greater Sunrise is estimated to contain about 7.6 trillion cubic feet of gas; only 20 percent lies within the JPDA.

1.15 Agreement was reached in May 2003 on a development plan for Bayu-Udan. Under this agreement, it was estimated that Timor-Leste would earn about $3 billion in revenues over 20 years, starting with 2004. This is already proving to be an underestimate, since the price assumption used in the projections has already been significantly superseded by recent increases in the price of petroleum. According to the December 2007 IMF Article IV Consultation report, oil and gas revenues increased from $13 million in 2003, to $168 million in 2004, to an estimated $492 million in 2006; and were projected to reach close to $900 million in 2007. Again, this projection will most likely to be significantly surpassed. These revenues have already dramatically improved the budgetary and balance of payments positions of the country; a major concern now is to ensure that they are used wisely to avoid the Dutch disease.

Transitional Arrangements

1.16 During the 1999 troubles, the international community, led by the UN, intervened to pacify and stabilize the situation. The Indonesian military, and much of the Indonesian civilian population, pulled out. They were replaced by the UNTAET which was established in November of that year. It was endowed with large powers to act as a legal state to facilitate the transition to independence and help create essential national institutions. To that end, it was supported by an international military force and a large influx of civilian expatriates to provide essential services in a wide range of technical areas, in view of the dire shortage of qualified and experienced local staff.

1.17 A Joint Assessment Mission (JAM) that also took place in November 1999 concluded that the situation in Timor-Leste was fundamentally different from the typical situation normally encountered in post-conflict countries. There seemed to be no immediate need for pacification among the different ethnic and religious segments of society. Instead, the situation was more akin to one where "a vicious hurricane destroyed all buildings and most crops and removed all records and institutional memory." Timor-Leste was considered to have been fortunate, since the situation had not broken down into a full-blown domestic conflict requiring commensurately large security operations. Nevertheless, the JAM concluded that the need for reconstruction was enormous because the destruction was pre-meditated, thorough, and massive.

1.18 To finance the required UNTAET operations, trust funds were established and funded by a number of bilateral and multilateral donors. One such fund established on September 30, 1999 was the Trust Fund for East Timor (TFET), administered by the Bank and used to channel grant financing from a number of key bilateral donors in support of the transition.

1.19 Meanwhile on the domestic political front, the situation moved relatively rapidly, in response to increasing pressure by the Timorese, and culminated in the establishment of the Constituent Assembly at the end of August 2001. The elections were reportedly virtually problem-free, a cabinet was subsequently formed, presidential elections held, and independence announced on May 20, 2002.

1.20 Commenting on the adjustment process summarized in the above paragraphs, the March 2002 Country Economic Memorandum (CEM) by the Bank concluded that: "The transition from devastation to an elected Constituent Assembly in two years, without major internal conflict, can be considered exemplary as an exercise in political management. From an economic perspective, however, the difficulties that were apparent during the transition, especially in terms of recruiting Timorese candidates with the technical and administrative skills required to run a government, remain an important hurdle to be overcome by the new nation."

Concluding Remark

1.21 Following four centuries of Portuguese colonization and a quarter century of Indonesian occupation, Timor-Leste suffered from additional devastating violence and destruction in 1999. An economic structure and performance that had been very modest to begin with was drastically set back. With prompt and significant assistance from the international community, the political transition to independence in May 2002 was relatively impressive, although it may still be pre-mature to pronounce a final judgment in this area. By contrast, the economic "transition" is likely to be more prolonged and demanding, in view of the dire initial conditions at independence, particularly the extremely limited number of qualified and experienced personnel. The recent discovery and development of oil and gas is already providing significant increases in revenue that have already eliminated any financing constraint facing economic restructuring and development. While avoiding the Dutch disease has now become a matter of concern, it is nevertheless a welcome concern compared to what the situation might have been without the added oil revenues. The main focus of this report, however, is on evaluating the performance of the three Bank operations designed to support the post-independence economic transition during the 2003-05 period. To that end, we will now turn to reviewing the Bank's assistance strategy in support of the country's vision for the future, starting with its transition efforts.

2. Development Strategy and the Three Transition Support Programs

Timor-Leste's Development Vision and Major Policy Areas

2.1 Following independence, the Government, actively assisted by its development partners, including the Bank; moved promptly to lay down its strategic vision for the future of the country and economy in a widely distributed pamphlet that described its "Vision for the Year 2020". This vision statement consisted of ten points setting out rather general and ambitious goals for the country to strive towards. By its nature, it did not include any discussion of priorities and trade-offs. The desired vision was then elaborated in the National Development Plan (NDP) for the period FY2002-07, again prepared in close collaboration with the Bank and other donors. The NDP was reportedly prepared through a broad, consultative process in the country. It was expected to serve as a strategic reference point for prioritizing and sequencing policy measures and actions that would be included in agency-level Annual Action Plans (AAPs). Monitoring of implementation progress under these plans would be carried out through the instrument of Quarterly Reporting Matrices. In addition, and in an attempt to deal with the adverse economic effects of disturbances in December 2002, a Stability Program was interjected into the FY 2004 planning process, and this program was included in a Road Map that attempted to link the NDP to the AAPs. In other words, a rather elaborate set of instruments and processes were set in place to plan, monitor, and evaluate the performance of economic policy; and to make adjustments along the way, as needed. It is not clear why such a seemingly cumbersome and redundant system was needed for a small country with relatively modest endowments and options, and severe capacity constraints.

2.2 With regard to broad policy orientation, the two over-riding objectives of the NDP and its accompanying instruments were to: (i) promote rapid, equitable and sustainable economic growth, and (ii) reduce poverty. The main policy areas aimed at meeting the growth objective were:

- developing a lean, effective and transparent **public sector**, free of corruption;
- implementing a prudent **fiscal policy** and a set of sound **financial management** practices that would allow a transition to financial independence within three years of independence (end of FY05);
- managing **oil and gas revenues** prudently;
- strengthening **economic management institutions**, notably the Banking and Payments authority;
- developing the **economic infrastructure**, including the transport, power and telecommunications networks; and
- promoting an enabling environment for **private sector development**, including legislative and codification measures, and dealing with the difficult land tenure problem that had been inherited from colonial days and the Indonesian occupation period, and exacerbated by the destruction of land ownership files and information.

2.3 In addition to the presumption that economic growth was seen as a precondition for sustained poverty reduction, the main policy areas aimed at meeting this objective more directly were:

- promoting the **economic participation** of the poor , primarily through developing agricultural opportunities;
- delivering **basic social services**, particularly in education and health, and aiming at achieving some "quick wins";
- improving the **security situation**, including food security and protection against disasters;
- aiming to set up a **social safety net** for the vulnerable; and
- promoting **empowerment** of the citizenry through community participation, local government development, and civic education.

2.4 Actions and specific measures falling under the above broad policy areas were included in Action Matrices agreed between the Government, the Bank, and other donors in the context of the annual Transition Support Programs. These are discussed below under separate headings of the three TSP operations.

World Bank Assistance Strategy for the Transition

2.5 A ***Transitional Support Strategy (TSS)*** was approved by the Bank's Executive Directors in November 2000. It provided the strategic framework for assistance to Timor-Leste during the post-independence period, pending the preparation of a full-fledged CAS, then expected for FY03. The main elements of the TSS were: (i) support for poverty alleviation and reconstruction over the short-term, and (ii) analytical and advisory assistance for post-independence policy and governance issues.

2.6 As of early 2000, the primary vehicle used for channeling Bank financial support directed at poverty alleviation had been the multi-donor, Bank-administered TFET. Specific projects financed by TFET covered a variety of sectors: agriculture, education, health, infrastructure, private sector development, micro-finance and community empowerment; for a total of $160 million. By early 2002, and in view of rising fiscal and balance of payments difficulties, it was deemed appropriate for the Bank and the other donors to provide some of their financial assistance in the form of direct balance of payments and budgetary support, hence the series of TSP operations starting in FY02.

2.7 In the meantime, and in line with the second strategic element of the TSS, the Bank carried out a number of analytical and advisory services. The main ones included: (i) a preliminary Poverty Assessment in February 2002, used in the preparation of the NDP; (ii) a Country Economic Memorandum in March 2002, that covered economic policy and governance issues; (iii) technical support, in conjunction with the UK aid program, for the preparation of the NDP; (iv) a Public Expenditure and Management Accountability (PEMA) note, that provided an assessment of fiduciary risk and was designed to help the Ministry of Finance and Planning (MFP) in strengthening its financial management; and (v) a full-fledged Public Expenditure Review in July 2004 that was used as an input in the design and implementation of subsequent public expenditure programs.

2.8 At the request of the Government, the **Country Assistance Strategy (CAS)** that was being drafted in FY03, was delayed till the end of FY05 to accommodate the completion by the Government of a new set of Sector Investment Programs (SIPs) to be used as additional inputs in the design and implementation of annual budgets. The CAS ended up covering the FY06-08 period and is, therefore, not directly relevant to this review. Nevertheless, it is still instructive to summarize its main points.

2.9 Based on an assessment of results and achievements under the TSS, the main objective of the CAS remained essentially as before: to help create the conditions for sustainable growth and poverty reduction. To that end, the Bank would continue to work closely with the Government and the concerned group of donors within a so-called "whole-of-Government" approach in support of the NDP and the Stability Program. The combined efforts would be underpinned by three strategic pillars: (i) delivering sustainable services; (ii) creating productive employment; and (iii) strengthening governance; with due concern to matters of gender and youth. These areas are very closely related to the main components of the three TSP operations being reviewed in this report, and as such, mean that the strategy and program for the FY06-08 period covered by the CAS is expected to build on achievements in these areas, with the main aim of consolidating gains and moving forward along essentially the same path.

2.10 The CAS was very clearly written and quite comprehensive in its coverage, perhaps to the point of being unnecessarily lengthy (46 pages, and almost 50 pages of annexes). Annex B9 by itself, consists of a 15-page matrix attempting to link NDP goals, to challenges, to CAS outcomes, to milestones, to instruments of Bank support. It is reminiscent of the equally comprehensive, detailed and rather unwieldy Action Matrices of the three TSP operations. As with those matrices, the items under the various headings tended to range from the very general and qualitative to some specific and quantitative.

2.11 Since the Bank, and to varying extents some of the other donors, were very closely involved in assisting the Government in drafting its NDP and many of the related planning, budgeting and monitoring documents and matrices; the Bank's assistance strategy and program are naturally closely aligned with the Government's development strategy and programs. In some cases, this raises questions regarding country ownership and commitment. In Timor-Leste, however, it seems that some key members of the Government had taken a lead role and had been fully committed and engaged. Others, in some line agencies, felt that they simply had to go along.

The Three Transition Support Programs: Overall Justification and Broad Design Features

2.12 The overall justification and broad design features of the three operations are basically identical; as is the general political and economic background, with a few evolving developments, particularly regarding significant increases in oil and gas revenues. Therefore, to avoid repetition, these are presented for the three operations combined, rather than for each operation separately.

2.13 The ultimate goal of the assistance strategies of the Bank and other donors at the turn of the century was to support the Government's efforts to promote sustainable growth and reduce poverty. In the meantime, the immediate, practical imperative following independence was to mobilize and provide bridge grant financing during the FY02-05 period, until sufficient revenues from oil and gas came on stream to finance the budget and the external account. The Government had, in any case, imposed a statutory prohibition on borrowing since it had judged that the prospects for raising loans had been nil and unaffordable. According to an TSP I internal review, during the transition, balance of payments support and bilateral budgetary support will address both external and fiscal gaps, mobilizing donor funds and thus allowing East Timor to sustain a level of imports and public expenditures that would not otherwise be possible. Channeling such funds through the budget was also expected to serve developmental goals by strengthening the Government's capacity to mange future revenue streams.

2.14 Total external grant financing requirements for the three-year period (FY02-05) were estimated at about $91 million, of which the Bank's three operations provided a total close to $15 million, roughly $5 million per operation. The first was in the form of a Post-Conflict Grant from the Development Grant Fund, and the last two in the form of IDA Grants. Co-financing by many bilateral donors (Australia, Canada, Finland, Ireland, New Zealand, Norway, the UK, and the USA) was channeled through Bank-administered trust funds, and additional bilateral and multilateral funding was provided directly (Portugal, Japan, and the Asian Development Bank). The Bank grants were disbursed in single tranches, following effectiveness, on the basis of corresponding sets of prior actions agreed with the Government. Simplified disbursement procedures were used. A separate Action Matrix of policy measures and actions was agreed with the Government for each operation, although the three overlapped with each other, as they evolved. Although the implementation of these matrices was monitored closely by the Government and the donors, they were not used to condition disbursement during implementation. It was presumed that progress, or lack thereof, in the implementation of an Action Matrix would be used in judging whether the Bank and other donors would proceed with follow-up operations.

3. The First Transition Support Program (TSP I) for FY2003

Background

3.1 The general political and economic background for the three operations as a group has already been discussed above. At the turn of the century, Timor-Leste was coming out of four centuries of colonization and twenty five years of occupation. A very poor territory to begin with, the wanton violence and destruction in 1999 led to a sharp decline in output and wiped out large portions of the country's physical infrastructure and civil records. Capacity in both the public and private sectors was extremely weak, poverty was high, and the provision of social services limited. Most Government institutions were embryonic and poorly staffed, particularly after the pull-out of Indonesian civil servants.

3.2 Following the cessation of violence and the establishment of the UNTAET, economic activity and output rebounded. Keeping in mind the generally poor quality of economic data, non-oil GDP was estimated to have grown by 15 percent in 2000, and 17 percent in 2001. Overall output and agricultural production were believed to have regained their pre-1999 levels. In January 2000, UNTAET adopted the US dollar as the sole legal tender, eliminating the need to worry about the conduct of foreign exchange and monetary policies, in view of the extremely limited capacity. Two foreign commercial banks opened delegations in Dili, but commercial credit remained negligible and the modest banking activities limited to the capital. Exports were almost non-existent (a mere $4 million), while imports increased substantially ($237 million) to support public investment in infrastructure and a markedly increased level of private consumption, due mainly to the influx of a large number of expatriates. The resulting balance of payments, as well as the budget, deficits were financed by official grants. The other half was financed by oil and gas revenues. An encouraging shift in the structure of public spending took place between 2001 and 2002 in favor of the social sectors (from 26 to 33 percent), and away from some core government functions.

Objectives and Design

3.3 The overriding goal of TSP I was to support the Government's post-independence efforts to build a new nation, as laid out in the NDP; focusing on the immediate measures in the FY2003 budget (the Timorese fiscal year is July 1 to June 30). Priority was given to the creation and early development of key institutions, a legislative framework, and management systems needed for core government functions, and to promote private initiatives. In line with priority areas identified in the NDP, the four components of TSP I consisted of: (i) planning for poverty reduction, and quick wins in service delivery; (ii) governance and private sector development; (iii) public expenditure policy and management; and (iv) power sector management, in view of the need to reduce this sector's heavy dependence on the budget at the time. Measures and actions included under these components were based on an extensive Action Matrix by the Government, attached to its Letter of Development Policy (LDP). Ten such measures were singled out and highlighted by the Bank and the Government, and constituted a list of prior actions that had been completed before this operation was approved (Annex C).

3.4 ***Planning for poverty reduction and quick wins*** were to be achieved through: (a) updating and making operational the NDP and the Poverty Reduction Strategy; (b) expanding access to primary and junior secondary education, while improving efficiency and quality, and creating incentives for partnerships with communities, NGOs, and the private sector; (c) targeting health care on mothers and children; and (d) defining and locating vulnerable groups, and assisting them through targeted training and finance.

3.5 ***Improved governance and private sector development*** were to be achieved through: (a) implementing an annual legislative program; (b) establishing an independent, competent judiciary; (c) creating an enabling environment for the private sector; (d) safeguarding the rights of citizens; (e) creating an efficient and transparent civil service; (f) providing the enclave of Oecussi with a special status, in view of its particular situation; and (g) decentralizing government.

3.6 ***Improved public expenditure policy and management*** were to be achieved through: (a) strengthening capacity in core financial management; (b) better monitoring and evaluation of economic indicators and statistics; (c) implementing prudent, pro-poor expenditure policies; (d) ensuring the transparency and accountability of public expenditure management to the legislature; (e) improving policy consistency, efficiency and effectiveness of public spending; (f) ensuring compliance with expenditure policy and legislation; and (g) ensuring the proper use of oil and gas revenues to benefit present and future generations.

3.7 ***Improved performance of the power sector*** was to be achieved through: (a) strengthening the management of East Timor Electricity; (b) improving cost recovery; (c) establishing an appropriate institutional structure for an independent power authority; and (d) preparing long-term power development plans.

3.8 Individual actions and measures under the above sub-components were detailed in the comprehensive Action Matrix. Most of those measures were of a qualitative, procedural nature involving the establishment of processes, institutional set-ups, management systems, preparation of plans, publication of documents, adoption of policies, or steps toward the enactment of legislation. Only a handful of measures established quantitative targets. Those primarily concerned the delivery of education and health services. In addition, no priorities that focused on the most important measures were articulated. The ten measures chosen as prior actions seem to have been chosen because they had been completed, and not because they were particularly more important, or more urgent, than many of the others.

Implementation Experience

3.9 The Grant Agreement for TSP I had provided for the preparation by the Ministry of Planning and Finance of quarterly progress reports on the implementation of the Action Matrix. Four reports were produced in a timely manner, and were generally accurate and candid in their assessments. A 13-member Progress Mission by the Bank and four bilateral partners took place in November, 2002, and based its findings on the first quarterly progress report. It concluded that, six months after independence, the systems and structures that had been put in place since 2000 remained fragile. It highlighted a number of implementation issues, including: (a) international personnel filling line functions at the expense of training; (b) financing systems geared to control rather than to facilitate the delivery of services; (c) a weak judiciary; (d) legislation put in place by fiat, and not based on policy and consultation; and (e) cost recovery in the power sector remained elusive, with unreliable supply and compliance by customers.

3.10 During plenary sessions, the Government and the mission collaborated on revising the Action Matrix on the basis of experience to date. Some measures were reformulated to better reflect realities, some new ones were added, and a number were pushed back to TSP II for FY2004. An expanded 15-page Revised Action Matrix was attached to the mission's aide-memoire.

3.11 A main conclusion that one draws from reviewing this aide-memoire, with its comprehensive set of annexes, is that overall progress midway through the implementation of this operation was uneven and generally behind schedule. The delay was primarily due to continued capacity constraints and problems with the delivery of the planned technical assistance. The tone was overly diplomatic and optimistic, often stating intentions and desirable outcomes instead of ascertaining actual progress. It was not until later, during the preparation of TSP II, that Bank staff started emphasizing the "intentionally ambitious" design of all the three TSP operations.

3.12 Since TSP I was funded from the Development Grant Facility, it did not require an Implementation Completion Report (ICR). Instead, a simpler Grant Completion Report (GCR) was prepared in September 2003. It was based in part on the very candid, useful, and well-presented fourth quarter progress report, issued by MOPF in July, 2003. The progress report presented a considerable amount of statistics on implementation progress of the Action Matrix, during each of the four quarters of FY2003. Table 2 gives a summary of some purely statistical findings. A listing of the completed, partially completed, not completed, and rescheduled actions to be included under TSP II is provided in Annex B.

Table 2: TSP I: Implementation Progress by Quarter (FY03)

	Number of Actions			
Quarter	***Completed***	***Partially Completed and ongoing***	***No Progress or not submitted***	***Total***
First				
No. of Actions	25	19	4	48
Percent	52	45	8	100
Second				
No. of Actions	23	19	2	44
Percent	55	45	NA	100
Third				
No. of Actions	22	31	10	63
Percent	49	35	16	100
Fourth				
No. of Actions	18	30 [1/]	2	50
Percent	36	60	4	100
Total				
No. of Actions	88	99	18	187
Percent	43	48	9	100

[1/] Actions rescheduled to next fiscal year, FY04.
Source: MOPF, Fourth Quarter Progress Report; TSP I, July 22, 2003, table 4.

3.13 Strictly in terms of numbers, Table 2 shows that 43 percent of the agreed actions were completed, and only 9 percent were not completed. Almost half (48 percent) were partially completed and ongoing. From the information summarized in Annex B, appreciable progress was made in the implementation of the first and third components (poverty reduction planning, and public expenditure policy and management). For the second and fourth components (governance and private sector development, and the power sector), implementation was quite limited, particularly for the governance and PSD component. This is not surprising since many of the actions included in the first and third components fell primarily within the jurisdiction of MOPF, the direct implementing agency for the operation. Most of those actions were also of a process and planning nature. Exceptions that stood out were the successful meeting of the quantitative targets for increasing the number of mid-wives, the rate of DPT3 coverage, and increases in the number of secondary school students and teachers. By contrast, the governance and PSD components required the passage of legislation (on companies, contracts, bankruptcy, investment, civil service) and setting up an ombudsman's office to deal with corruption.

3.14 According to the Grant Completion Report (which essentially reiterated verbatim the assessment of progress under TSP I found in the PAD for TSP II), in addition to increases in the delivery of educational and health services noted above, a number of other achievements were worth noting. These included: the establishment of two commissions in the President's office to start addressing the sensitive veterans' issues; a land law dealing with publicly owned land was passed; a Judicial Magistrates Code was approved by Parliament; several procedural measures having to do with the public expenditure management framework were implemented; and emergency generators, financed by the Norwegian Government, were installed and improved the reliability of service. Despite these improvements, however, many issues and challenges remained. These included: delays in moving ahead with a number of laws to improve the regulatory framework for private business; delays in the establishment and staffing of the office of the ombudsman; significant delays in the establishment of a regulatory framework for the civil service; and a significant increase the budgetary subsidy for the power sector to 11 percent of total recurrent expenditures.

3.15 On balance, the implementation experience under TSP I was uneven and partial. This was in part due to a very limited implementation capacity and delays in the delivery of much needed technical assistance. It must have also been due to the ambitious number of measures called for in the Actions Matrix, without any apparent priorities. This "intentionally ambitious" design that was carried through into the two follow-up operations was justified by the Bank on the basis of the Government's insistent desire for support from the donors on a broad front, in order to make progress in the implementation of the NDP. However, given the wide experience of the Bank and other donors in the development business and their acute awareness of the extremely limited capacity in the country and the difficulties normally encountered in recruiting timely and appropriate technical assistance, the Bank could have advised more strongly against spreading efforts too thinly and argued for a smaller, but well-targeted, set of actions, with tighter priorities. In fact, it appears that some of the donors, particularly Norway, favored that position. It seems that Bank staff-members argued among themselves about this central point, some favoring a more focused approach and others feeling that the Government argued would definitely have not gone along with anything short of its broad program. This point is addressed further below (paragraph 6.34).

3.16 ***Outcome of TSP I:*** While fully acknowledging the significant progress made in few important areas of the TSP I operation and the impact this have had on the improvement of the dire state of affairs which prevailed in the country following independence, the fact remains that only partial results were achieved in most of the other areas identified under the program. Therefore, the overall outcome of the first TSP operation is considered ***moderately unsatisfactory.***

3.17 ***Risk to Development Outcome.*** At the end of the first TSP operation the country was still at a precarious state of the economic and social affairs, with high level of unemployment among the youth and significant poverty issues. Quite serious political risks; particularly across the deep divide along the domestic political fault-lines, continued to be the cause of serious friction and violence that could potentially spin out of control. Concerns over the unstable political and social situation were further exacerbated by the very low implementation capacity of the government, and the risk of corruption. Therefore, given widespread sources of potential risk and unfinished institutional building agenda, the risks to development outcome of TSP I are considered ***significant.***

3.18 ***Bank Performance.*** Allowing for the realities in the country and the strong client's desire for a broad, all-encompassing approach in the program design, the fact remains that the Bank designed a too complex program for a post-conflict country with severely limited implementation capacity. Greater realism and a more careful risk assessment at entry would have suggested a much more streamlined and focused project design, as a framework to convince other donors who preferred a broad over a narrow approach. Furthermore, changes could have and should have been made during the implementation of the first operation to address clear implementation difficulties and focus on the achievement of priority project objectives. On that basis the performance of the Bank merits a rating of ***moderately unsatisfactory***.

3.19 ***Borrower Performance.*** The Government had a strong interest to obtain Bank and donor support for its entire national development program. Lack of true ownership and commitment, distraction caused by the oversupply of donor resources, and the absence of clear feedback (from the Bank and donors alike), all contributed to procrastination in realizing own capacity constraints and selecting clear priorities. Government limited resources were spread too thinly across too many competing development priorities leading to weak and partial implementation of many actions/components. On that basis the performance of the Borrower merits a rating of ***moderately unsatisfactory***.

4. The Second Transition Support Program (TSP II) for FY2004

Background

4.1 The overall political and economic background and context for this operation did not differ appreciably from the background that had existed prior to TSP I. This was only natural and as would be expected over a one-year period only. In fact, since the Government and the Bank had opted for a series of three separate, but very similar, operations in three successive years; the corresponding documentation by both ended up being very repetitive. Although such redundancy may have been called for by the requirement that many of the documents had to be self-standing, it did represent a substantial drain on resources, particularly for the Government but also for the Bank and other donors.

4.2 On the macroeconomic front, there was a marked drop in economic activity in general, with GDP growth dropping to 3 percent in 2002, and to minus 3 percent in 2003. This was apparently due to the departure of large segments of the expatriate community. Because of changes in the tax regime governing oil and gas production, increases in revenue from this source were back-loaded, and could not be counted upon to counterbalance the drop due to the departure of foreigners. Still, the signing of the Timor Sea Treaty in March 2003 promised significant increases in revenues over the long-run, estimated in 2003 at about $3 billion over the following two decades (quite likely to be an under-estimate in view of recent increases in the price of petroleum). The budget deficit declined by about 20 percent in 2003, but that was due to a drop in expenditures in addition to an increase in revenues. Similarly, the deficit on the current account of the balance of payments dropped by about 13 percent in 2003, but that was entirely due to a drop in imports, while exports remained at their very modest level.

4.3 In 2003, there was no significant private sector investment, with private capital still seeking external outlets. A third commercial bank was still expected to start operations, while the two-bank banking "system" remained essentially involved with transactions rather than providing credit for investment. The poverty situation remained very serious. The political situation also remained fragile and tense, following the violent riots in Dili in December 2002, and attacks on rural communities in early 2003. In other words, despite the early efforts by the Government, with the support of the donor community in the context of the NDP and TSP I, the overall economic and political situation deteriorated in 2003, admittedly due to difficult political and social factors. Nevertheless, this was the situation that prevailed while TSP II was being prepared.

Objectives and Design

4.4 Under the circumstances, the Government, the Bank, and other donors decided to move ahead with TSP II, essentially along the same lines as its predecessor, with the same objective of facilitating the transition of a post-conflict country toward greater economic independence, growth and poverty reduction. The implementation completion report for this third operation seemed to argue that there was a material difference from the first operation. It stated that the TSP I "focused on the creation of the institutions, establishment of the legislative and regulatory framework and strengthening of management systems for core government functions"; and that TSP II, while still covering these areas, would cover the three "thematic" areas of: "(i) Good Governance, including: strengthening State institutions, public sector management and public expenditure management; and strengthening administrative capacity in the justice sector; (ii) Service Delivery for Poverty Reduction, particularly improvements in the efficiency and effectiveness in the health and education sectors; and (iii) Job Creation, especially through private sector development and agriculture." In fact, the broad design of the two operations was very similar, almost identical, except for dropping the fourth component of TSP I that had dealt with the power sector (It is not clear why this was dropped at the time), and focusing specifically on agriculture, in addition to the private sector generally, in TSP II, under the job creation component. The difference was more in semantics than in content, and this was reflected in the fact that several sections of the TSP II appraisal document were basically lifted from that for TSP I. This is not to say that there was anything necessarily wrong, in itself, with staying with the same basic design throughout the series of operations, provided they were judged appropriate for meeting the stated objectives.

4.5 While TSP II was being prepared, the Government was trying to respond to the December 2002 riots by announcing a Stability Program in January 2004, focusing on governance, service delivery for poverty reduction, and job creation. This program was expected to guide the prioritization and sequencing of actions within the FY2004 budgeting process, and to be imbedded in a Road Map which laid out the program for the remaining four years of the Government's mandate. But when stripped of this added, perhaps superfluous nomenclature, the essence of the Government's efforts remained the same; namely, to translate its broad development objectives into an annual budget and a set of specific policies, laws and regulations aimed at achieving those objectives. Again, too much effort seems to have been spent on creating new "instruments" aimed at further articulating intentions and programs, probably at the expense of faster and better implementation.

4.6 The rationale for TSP II remained the same as that for TSP I, namely, to provide grant bridge financing to help Timor-Leste implement its NDP until enough oil and gas revenues come on stream. Channeling the grants through the budget was seen as a means to strengthen capacity to better manage future oil revenues. External financing requirements for FY2004 were estimated at $28 million, of which about $4.16 million (corresponding at the time to SDR 2.9 million) was provided by IDA.

4.7 The three "thematic" components of this operation consisted of a number of sub-components each, as follows:

- ***Good Governance*** included: oversight institutions, local government, public sector management, poverty reduction planning, public expenditure management, and the judiciary.
- ***Service Delivery for Poverty Reduction*** consisted, in particular, of improvements in the efficiency and effectiveness of service delivery in the health and education sectors.

- ***Job Creation*** mainly through private sector development and agriculture.

4.8 Individual measures under each sub-component were agreed with the Government and included in an 11-page Action Matrix, attached to the Government's LDP, dated June 12, 2003. As with TSP I, a number of measures (seven in the case of TSP II) that had already been implemented before the preparation of this operation started, were used as prior actions to justify the release of the single tranche of this IDA grant (Annex D).

Implementation Experience

4.9 As with the experience under TSP I, implementation of the wide range of measures included in the TSP II Actions Matrix was uneven, and mainly partial. Some progress was made regarding some specific actions. For example, in the area of governance, an Organic law for the establishment of the Provedor's Office and a Public Service Statute were passed. However, less than half of the scheduled legislation was passed, the development of a policy and procedures for the legislative process did not start, and the proposed legislation governing private investment fell considerably short of international best practice with regard to the treatment of tax incentives and foreign investors. The development of policy frameworks for education and agriculture lagged and were not completed by the closing of this operation. Of particular concern was the very slow progress made in the important area of capacity building and institutional development. The proposed design of a human resources development strategy for the Ministry of Planning and Finance did not take place and was deferred to TSP III.

4.10 The preceding paragraph gives just a small sample that illustrates the partial and mixed progress in a few areas. Table 2 of the Simplified ICR for TSP II gives a more complete listing of implementation progress across the entire set of measures. This table is reproduced in its entirety as Annex D. A notable success story is the health sector where all the proposed measures were implemented, with some of them exceeding expectations. This has been attributed to the strong and committed professional leadership that the Ministry of Health has enjoyed under the entire TSP series.

4.11 The Simplified ICR for this operation recounted the familiar issues that have stood in the way of better implementation results. These included: severe capacity constraints across the board; shortages, delays in recruitment, and uneven quality of technical support from expatriate experts; management weakness and lack of understanding of key procedures in some line agencies; and an overly ambitious design to begin with. Particularly hit by these deficiencies were such important matters like the rate of budget execution, the very slow development of legislation and the judicial system, and the community-based road maintenance program that was supposed to create jobs and help deal with reducing unemployment and poverty. As had been done previously in the transition from TSP I to TSP II, a number of the measures that were delayed under TSP II were slipped to TSP III. Similarly, some of the measures that were actually completed under the second operation were used as prior actions for approving the third.

4.12 ***Outcome of TSP II:*** In summary, although the second TSP operation contained a range of relevant objectives in the areas of governance, service delivery for poverty reduction and job creation, only a fraction was achieved. As more performance indicators became available with a time lag, this pattern was confirmed in governance (with achievements in oversight institutions and some aspects of public expenditure management, compared to a long list of unresolved issues in improving core government functions, the justice system and general public sector management). Similar situation emerges in the areas of service delivery and job creation where notable achievements were made in health but other aspects of service delivery lag behind due to uneven, and mostly partial and incomplete implementation of actions envisaged under the TSP II. Most importantly, there is insufficient evidence on job creation and poverty reduction. Therefore, the overall outcome of the second TSP operation is considered ***moderately unsatisfactory.***

4.13 ***Risk to Development Outcome.*** Some of the most obvious political and institutional risks have been reduced during the second TSP. The country has moved from a very unstable to unstable situation. High levels of unemployment and significant poverty issues remain. So do political divisions and risks from instability. The project ambitious agenda encompassing a large range of issues and development objectives is constrained by the continued lack of institutional capacity and a chronicle shortage of trained individuals to implement the program and, even more, sustain the achieved results. Therefore, the risks to development outcome achieved under TSP II are considered ***significant.***

4.14 ***Bank Performance.*** The second TSP operation continued to be based on a broad and ambitious program which has been designed without due regard to government true ownership and implementation capacity, and continuing harsh realities in the country. The design of the second operation should have addressed clear implementation difficulties faced in the first TSP and focus on the achievement of fewer priority project objectives. Greater realism and a more careful risk assessment at entry would have resulted in more modest and better targeted actions. Furthermore, if not earlier, changes could have and should have been made during the implementation of the second operation. On that basis the performance of the Bank merits a rating of ***moderately unsatisfactory***.

4.15 ***Borrower Performance.*** The Government developed a much stronger ownership of the TSP II program and took the lead in designing and implementing the reforms supported under the project. However, with limited administrative capacity and lack of adequate expertise in the country, the Government was not able to fully grasp, manage and implement the program of such breadth and complexity. Despite the fact that the Government now fully owned the program, it fell short of addressing the institutional and policy coordination problems intended for a much more sophisticated and significantly more developed economy operating under normal circumstances. This led to weak and partial implementation of many actions/components. On that basis the performance of the Borrower merits a rating of ***moderately unsatisfactory.***

5. The Third Transition Support Program (TSP III) for FY 2005

Background

5.1 Again, the overall background and context on the eve of the preparation of TSP III was quite similar to what had existed for the previous two operations. The overall economic situation remained very fragile. In fact, the program document for TSP III reported that due to the continued departure of international staff, GDP declined by about 2 percent in 2003. Imports by humanitarian and UN agencies declined from 50 percent of the total in 2000, to 10 percent in 2003. Combined with a modest increase in coffee exports, although to a level still about two-thirds of the pre-1999 levels, this led to a decrease in the balance of payments current deficit by about $200 million, to about 60 percent of GDP. With the drop in overall economic activity, private sector wages started to drop in response to the lower demand for labor, but remained higher than in neighboring countries. Inflation was in the 8-10 percent range due in part to a scarcity in agricultural goods caused by a drought. Unemployment was assumed to have remained high; the latest available figures from 2001 had indicated that around one fifth of the working age population was unemployed, but the rate was much higher for youth, standing at around 43 percent for 15-24 year olds. Foreign investors continued to show little interest, except in some natural resources like fisheries and forestry, for which the Government deferred consideration pending further review. In fact, the number of larger tax payers with turnover of above $1 million declined. A third bank started operations in August 2003 and promised to extend some services beyond Dili. Despite some increasing interest in microfinance operations, financial intermediation remained very low by international standards, with the bulk of deposits invested abroad.

5.2 A significant development in February 2004 was the start of production of petroleum liquids at the Bayu-Udan field, followed by the production of dry gas later that year. As a result, the part of the oil and gas revenues that were made available for budget financing were expected to account for an increasing share of the consolidated budget revenue, from about 60 percent in FY03 (they had been about 48 percent in FY01), to about 66 percent in FY05. This was expected to still leave total budget revenues short of consolidated expenditures estimates, requiring external financing through grants; leaving a financing gap of just over $30 million in FY05.

Objectives and Design

5.3 In terms of broad objectives and design, TSP III was, by and large, a continuation and extension of TSP II. It still sought to provide bridge grant financing for the country's development efforts by supporting a wide set of policy and institutional development measures of an Actions Matrix, based on the NDP, and reflected in the annual budget and other related planning instruments. Again, the three main program components consisted of: (a) promoting good governance; (b) improving service delivery for poverty reduction; and (c) job creation. As the TSP series matured, the expectation was that this third operation would seek to introduce three principles into the design: (i) making greater use of quantitative performance indicators, as had been done already in the health sector; (ii) using a three-year medium-term perspective through FY2007, as opposed to the rolling annual programs of the previous two operations; and (iii) mainstreaming gender issues, notably in the policies and programs of the Ministries of Health, of Education, and of Justice; as well as in the National Police.

5.4 As with its predecessors, the complete set of measures under the three program components were captured in an updated Actions Matrix, attached to the Government's Letter of Development Policy. Again, these measures were not policy conditions that governed the disbursement of the IDA grant, but targets for the Government program itself. As with the previous operations, a much smaller subset of actions already completed from the Actions Matrix of TSP II was selected as a set of prior actions for the approval of TSP III (Annex C). As before, progress in the implementation of the TSP III matrix would influence the donors' views regarding forthcoming support. In any case, the list of twelve key outputs consisted primarily of procedural and regulatory measures in the areas of governance, budgeting, and private business development; as well as implementing a pilot grant mechanism in primary schools.

5.5 Despite the intention of the three guiding design principles listed above (greater use of quantitative targets, medium-term perspective, and mainstreaming gender), most of the specific measures in the Actions Matrix itself remained extremely similar to what was included in the corresponding matrices for the two previous operations. They were primarily procedural and related to planning, budgeting, regulations, laws, licensing, reporting and monitoring; with a few concrete deliverables in the health and education sectors. This is not to say that many of them were not needed, nor important. It simply confirmed that the over-riding efforts remained on developing the institutional, policy, and regulatory environment on a broad front, instead of focusing on specific quick-wins and some important tangible results.

Implementation Experience

5.6 As with the two previous operations, TSP III was intensively supervised by the Bank, with active participation by some of the other donors. As part of this effort, a substantial fifteen-member mission led by the Bank; and including participants from ADB, AusAID, Ireland Aid, UKDFID, and USAID; visited Timor-Leste toward the end of the third quarter of FY05 to review implementation progress and recommend adjustment, as necessary. At the same time, the mission appraised the proposed CSP I.

5.7 Strictly in terms of numbers, the mission tabulated a breakdown of all the actions of this operation's Action Matrix into three categories: (a) actions considered completed by end March 2005; (b) actions that remained in progress with one quarter left in the fiscal year; and (c) actions re-scheduled to the proposed CSP I (Table 3). Of a total of 122 actions in all the three components of the program, only 38 (31 percent) had been completed in the first three quarters; another 50 (41 percent) were considered in progress, some of which probably slipped beyond the fiscal year; and 34 (28 percent) were re-scheduled to CSP I. The most delinquent component was *job creation*, with only 14 percent of the programmed actions completed by end March, 2005; followed by *service delivery* with a 32 percent completion rate; and governance performed the best in terms of numbers, with a completion rate of 44 percent. It is interesting to note here that the

Action Matrix grew significantly in size between TSP I when it totaled around 50 actions, to TSP III when it totaled more than 120 actions.

Table 3: TSP III – Implementation Progress by Component

	Number of Actions			
Component	***Completed by March 31, 2005***	***In Progress***	***Re-scheduled to CSP I***	***Total for Component***
Governance	21	15	12	48
Service Delivery	12	19	6	37
Job Creation	5	16	16	37
Total	38 (31%)	50 (41%)	34 (28%)	122 (100%)

Source: TSP III, Supervision Mission.

5.8 The aide-memoire of the Supervision Mission went on to highlight four areas that it considered of critical concern for the coming year: education, petroleum revenue management, public finance management, and private sector development. It concluded that of these areas, the management of petroleum revenues was proceeding well, with implementation perfectly on-track. Performance in the public resource management area was judged to have been mixed, with the development of planning, evaluation and monitoring mechanisms proceeding fairly well, but budget execution falling way short of plans, due to implementation capacity constraints and lack of confidence by the Ministry of Finance regarding the delegation of procurement decision to line agencies. The performance of the education sector, which is very important for the development of the economy, was also judged to have been variable, but mainly disappointing. For example, about 40 percent of the sector's budget had not been spent, while about 25 percent of school-age children were not enrolled in primary schools, and textbooks and trained teachers remained in dire shortage. Finally, with regard to the job creation component, although some notable progress had been made in the critical area of solving the land registration problem and setting up some institutions for promoting investment and exports; serious concerns remained regarding the improvement of the overall business environment. The most serious problems cited by the business community included the familiar litany of: delays in customs procedures and registration of businesses, a heavy tax burden, difficulties in obtaining work permits, and pervasive bureaucratic inertia across all Government institutions, due to excessive paperwork and regulations combined with poorly trained and motivated civil servants.

5.9 A full Implementation Completion Report was produced for TSP III in June 2007. It gave an overall assessment of implementation progress under the three operations, but with an emphasis on the third. The report was quite candid in places, but ultimately gave quite a sympathetic and positive overall evaluation, as the simplified ICR had done for TSP II.

5.10 Nevertheless, two well-argued summary paragraphs from this ICR are worth quoting in total in this review (Box 1); the first summarized the major achievements of the TSP program as a whole, and the second pointed out to some significant shortfalls and weaknesses.

5.11 ***Outcome of TSP III:*** As already detailed in the above paragraphs, the third TSP operation had a number of important achievements. However, almost 70 percent of all actions have not been completed by the closing date, or have been dropped and re-scheduled for a subsequent series of operations. Implementation patterns noted in TSP II continue in this operation in each of the key areas (governance, service delivery for poverty reduction and job creation). Relatively few important and notable achievements in governance and service delivery are followed by a long list of actions under slow implementation or no progress at all due to uneven, partial and incomplete implementation efforts. Therefore, the overall outcome of TSP III is considered ***moderately unsatisfactory.***

5.12 ***Risk to Development Outcome.*** Further progress has been made in reducing political and institutional risks during the last operation in the TSP series. Economic growth has been restored, and modest progress has been made on some important fronts. However, the overall risks caused by the overall volatility of the political situation, limited government capacity (especially relative to the demanding complexity of the TSP III operation) and poor rating of governance (i.e. vulnerabilities to possible corruption problems) suggest continued significant risks to development outcomes. Therefore, the risks to development outcome achieved under TSP III are considered ***significant.***

5.13 ***Bank Performance.*** The third and last operation in TSP series maintained a broad and ambitious program, way too complex for a country with such limited implementation capacity, continuously exposed to harsh realities. The design of TSP III should have addressed implementation difficulties faced by the previous operations, and control of quality at entry should have identified and corrected this glaring discrepancy between the complex and demanding project design and limited implementation capacity, especially after this has been clearly noted in the evaluation summary of the TSP II operation. Lastly, if not earlier, changes could have and should have been made during the implementation of the third operation. On that basis the performance of the Bank merits a rating of ***moderately unsatisfactory***.

5.14 ***Borrower Performance.*** Although the Government has moved to further strengthen its ownership of the TSP program in the third operation, it was not able to close the gap between its intent (nominal political ownership) and still quite limited administrative capacity and expertise in the country. Notable shortfall in addressing the institutional and policy coordination problems, coupled with inability to select clear priorities and strengthen the implementation effort to achieve the majority of development results continued to limit Government's performance under the last operation in the program. On balance this led to weak and partial implementation of many actions/components and Borrower performance rating of ***moderately unsatisfactory***.

Box 1. Summary Assessment of the TSP Series as Presented in the ICR for TSP III

"The Government has consistently praised the contribution of the TSP to Government-owned policy prioritization, capacity building, results orientation, and donor coordination in a post-conflict environment. The TSP has supported strategic annual planning and high level monitoring with a whole-of-government approach. By taking guidance from the NDP, sector strategies and AAPs, the program has cultivated Government ownership. It has promoted capacity building by promoting the Government's own systems and processes for budget preparation and execution, including mid-level managers in program elaboration and monitoring, and providing a forum for discussion of prioritization , implementation, results, and monitoring. The preparation of a time-bound matrix of policy and institutional measures, together with their expected outcomes, has instilled discipline while internal disciplinary mechanisms are still weak and has fostered good planning and enhanced agencies' results orientation. The TSP has strengthened donor coordination by bringing together the majority of Timor-Leste's development partners in the preparation and monitoring of the program, thus serving as an anchor for all donor-financed activities. This coordination mechanism has allowed coverage of all critical issues, drawing upon the comparative advantage of each development partner, and promoting the mainstreaming of cross-cutting issues such as gender.

The program's performance has been less strong in setting up basic institutions and supporting job creation. By the end of the three-year program, Timor-Leste still did not have one qualified national judge and budget execution figures remained low. Performance was particularly weak in the areas of job creation and income generation. The private sector continued to encounter important barriers to its operations, resulting in poor scores in the Doing Business survey and anemic job creation. Short-term Government-supported job creation measures monitored under TSP, such as the emigrant workers and the community roads programs also did not deliver the expected results. Finally, although results were more encouraging in the social sectors, many of these results were in the area of sector planning rather than in final outcomes – especially in the education sector.

6. Overview of the Three Operations as a Group

6.1 As we have seen above, the three annual operations were very similar, and essentially formed a unified series, with the first operation flowing into the second, and the second into the third. Most of the measures included in the Action Matrices that formed the core of the operations' content would arguably take several years to be actually completed in most countries, and especially in a country like Timor-Leste with particularly severe capacity constraints. As such, this review concluded that it would be more meaningful and fair to look at the key areas of achievements of the three operations taken together. In other words, to focus on what did the three-year effort by the Government, closely supported by a significant and well-coordinated level of assistance from a sizeable community of donors and development partners, amount to? What were the main accomplishments, and what were the areas that fell short of expectations? Was the design appropriate to begin with? How did the Bank and the Borrower perform? These are the main questions that this section will attempt to answer.

6.2 Before turning to this evaluation, however, the fact that we have chosen to look at the three operations as a group, begs the question why were they, in fact, three separate operations? Why not a single operation, with three tranches over three years? Certainly, the three separate operations involved considerable redundancy in documentation and processing on the side of both the Government and the various donor bureaucracies. Was this wasteful duplication necessary? Interviews with some of the key persons involved in this aspect of design revealed that this question was simply not addressed explicitly. It seems to have been implicitly presumed that, given the difficult initial environment in the country in 2002 and the considerable capacity constraints, a successive horizon of only one year would be more manageable for both the Government and the donors. Committing to a three-year horizon might have been too much to ask for at that stage. In addition, a three-year operation might have raised the question of applying *a priori* conditionality which would not have been appropriate for a post-conflict, new country using of a grant from the Development Grant Facility, as was the case for the first operation of the series. In retrospect, it seems that despite the cost of the redundancy involved, a series of three annual operations did make sense under the circumstances.

Main Achievements

6.3 ***Bridge Financing and Leveraging IDA Grants.*** As a representative of one of the key donor partners put it, "It is absolutely clear in my mind that the bridge financing provided by the donors through the TSP was essential for the economic survival of this new country in the early days. There was a strong political will from several donors to step in a help out, and the TSP provided the right channel for their funds and efforts. The central role played by the Bank in supporting the Government manage the process was valued by my authorities, and by the other donors, I believe."

6.4 This is probably a fair assessment despite the appreciable increase in oil and gas revenues, starting with FY03, when TSP I was disbursed. The flow of grants from the donors allowed the country to support a rising level of needed expenditures during its early formative years, by eliminating the need to borrow to finance the budget deficits.

During the three years of the TSP series (FY03-05), the amount of annual grant financing that helped finance the budget, about $33 million on average, was close to half the average level of consolidated expenditures. However, now that this country of less than a million people is sitting on about $2 billion in the Petroleum Fund, projected to increase significantly in the coming years, the likelihood that it will continue to receive significant amounts of grant financing into the future will diminish.

6.5 ***Aid Coordination and its Benefits.*** Total donor financial support for the three TSP operations came to about $99 million. Of that, IDA grants were about $14 million (14 percent). Nine bilateral donors provided $76 (77 percent) million equivalent through the IDA-administered trust fund, and another $9 million equivalent (9 percent) was provided directly by other donors, but were associated with the program. Since the Bank played a central role in assisting the Government, with the other donors, in designing and implementing the TSP; it can be argued that the influence of the IDA grants was leveraged by the additional and considerable (more than 6 times) donor co-financing. This is not to say that many of the other donors would not have participated if the Bank were not involved.

6.6 The Government, some of the donors, and the Bank all agree that the TSP process itself was a significant achievement, as summarized in the first paragraph of Box 1 above. The TSP provided a framework that was very much appreciated by the Government to help it plan, monitor the implementation, and adjust its development activities and budgetary outlays. According to a senior Government official who was involved with the process from the beginning, and has since risen to a higher level of authority within the administration, "I saw the main benefit of the entire three-year TSP in the process itself and as an instrument that allowed us to instill a new culture of planning, monitoring, and rationalizing our activities. That, for me, was an end in itself at that stage. Specific results and achievements, though important, were not what I was expecting from the exercise at the beginning. Now, in 2008, we need to start making the program more operational, and target for more concrete results." The TSP framework and process also provided an appreciated vehicle for coordination among the donors, and between the donors and the Government. The costs of this coordination were considered by most to be more than offset by its benefits to all. Finally, the TSP process also helped establish some communication channels between the Government and civil society, through various mechanisms, like leaflets, forums, press conferences, and seminars.

6.7 ***The Petroleum Fund.*** There is general agreement among many Government officials, donor representatives, and Bank and IMF staff that the establishment and functioning of this fund has been a major achievement; a real success story, so far. This review agrees with this assessment.

6.8 In 1999, the IMF and the Bank worked closely with the Government to look into options for safeguarding the expected increases in petroleum revenues, as production increased. The concern was to protect future revenue streams from abuse and the political pressure to spend more liberally. A number of models used by different countries were reviewed and it was decided to use a variant of the Norwegian model. The formula adopted consisted of putting an upper limit on any annual amount that can be transferred from petroleum revenues in a particular year to finance budget expenditures. The remainder would be transferred to the Petroleum Fund (PF) to be invested in appropriate financial instruments, to serve as savings for future generations. Going beyond such a limit would require approval by Parliament. This has not been done so far. The limit was set at 3 percent of the present value of the projected revenue stream (based on various relevant assumptions), starting with the year in question. As of early 2008, the PF stood at around $2 billion; that is, more than $2000 per capita for Timor-Leste.

6.9 Many of the technical and legal measures employed in establishing and operating the fund were included in the Action Matrices of the TSP series, and serve as examples of successful elements of these matrices. The PF assets which are held by the Banking and Payments Authority (the country's "central bank") on behalf of the Ministry of Finance have all been invested in US Treasury bills so far. However, the authorities are currently looking into diversification options, and considering asking the Bank's Treasury Department for assistance in this regard. The support given throughout by the Bank and the IMF to the PF has been greatly appreciated by senior officials interviewed in the course of this review, including former Prime Minister Alkatiri, who has been credited by many observers from within and outside the country, with having been a driving force behind the establishment this fund. A main issue for the future is how to determine any dynamic adjustment of the ceiling placed on transfers to the budget; making sure to carefully balance between the need to fund development expenditures, with the limited absorptive capacity to implement such expenditures efficiently.

6.10 ***The Health Sector.*** There seems to be a general consensus among donors and Government officials that the health sector sub-components of the three TSP operations were well implemented. The credit has been uniformly given to the leadership in the Ministry of Health, primarily in the person of the Minister himself, at the time. All the matrix actions called for were met. In particular, the quantitative target regarding maintaining expenditures on hospitals below 40 percent (to safeguard enough resources for primary health care) was consistently met; and those for DPT3 and measles immunizations, attended deliveries, and outpatient visits, were exceeded. Ironically, the minister concerned who is generally viewed as technically and managerially very competent, felt that the performance indicators chosen were second best; but as good as was available, given difficulties with data collection and analysis. He also felt that due to severe staff constraints, the measures included in the Actions Matrices in all sectors were driven by consultants and donors, with insufficient consultation with Timorese. As such, they lacked full ownership by the civil servants. Many local counterparts, in his view, just went along even when they believed that the pace dictated by the matrices was unrealistically fast. He felt that the senior echelons of the Government at the time, including the then Prime Minister, were keen on having the matrices as instruments of dialogue with the donors (and channels for their funding), but were not themselves involved with the details of the tool itself. This view was shared by other Timorese officials in line agencies, and even some donor representatives and Bank staff interviewed in the course of this review.

6.11 ***Electricity Metering.*** This item is included here under main achievements because it was successful for a short while, until the 2006 riots and disturbances, which may be viewed as an unfortunate "external shock" from the standpoint of the power sector.

6.12 A separate power sector component had been included in TSP I, but was dropped in the subsequent two operations. It was included in the first operation because power subsidies at the time represented a significant drain on the budget. The component introduced measures in the Actions Matrix for that operation designed to help remedy this situation. According to the Grant Completion Report, the implementation of this component did not proceed that well, in general. Many significant challenges were not properly addressed at the time and needed further attention. It is not clear, therefore, why it was not included in the second and third operations.

6.13 Despite this disappointing overall performance, the financial position of the power authority did improve temporarily because of two technical factors: the installation of emergency generators which increased capacity, and therefore, sales; and the installation of pre-paid meters in Dili in 2002. Both were financed by grants by the Norwegian Agency for Development Cooperation (NORAD). These measures proved successful and received praise from the authorities and the donor community. Unfortunately, during the disturbances of 2006, many urban customers by-passed the meters and connected themselves illegally to the network. As a result, collections which had averaged around $6 million annually in 2004 and 2005, dropped by half to around $3 million in 2007. To make matters worse financially, the tariff was reduced by around 25 percent in 2007 to 12 cents per KWH, while production cost was around 37 cents per KWH (not including transmission costs and losses). The power authority is now faced with the challenge of re-installing meters and re-establishing more realistic tariffs. However, as a senior official of the authority stated, "The problem we face now is primarily political, and not technical." This official expressed satisfaction with the quality of the cooperation with the Bank.

6.14 ***Veterans Recognition.*** The Veterans Law was passed in 2006, after closing of TSP III. As of 2006, a total of 75,143 veterans were registered in a veterans database. Though the payment of pensions has been delayed due to pending approval of relevant decree laws, US$10m were included in the 2007 budget for veterans' pensions.

Main Areas of Partial, or Poor Progress

6.15 Among the measures designed to improve governance and combat corruption, the establishment and staffing of the ***Office of the Provedor (Ombudsman)*** was given particular importance by the TSP series. It took the entire three-year period of the series to finally have this office running, but despite this delay, it is a good achievement (an example of how some measures had to be rolled over until they were implemented). By early 2008, a total of 27 cases had been considered; either in response to complaints received, or at the initiative of the Office. Of those, 20 had been investigated, of which 8 had been referred to the Prosecutor General. None had been taken to court, nor led to any disciplinary action as of that date. The cases involved matters like tax evasion, or misuse of funds. A number of cases involved Government officials and were reported to the line ministries involved, but no follow-up action had been taken. The Provedor does not have the authority to prosecute. He can only try to persuade line ministries to take action, or refer criminal cases to the Prosecutor General. Line ministries have up to 60 days to act, and if they do not, the Provedor can report the case to Parliament. If Parliament does not act, the report can be publicized. In addition, when a report is referred to the Prosecutor General the media are invited to attend. The Provedor's Office has also been entrusted with overseeing the functioning of the Petroleum Fund, and has so far been satisfied with its performance.

6.16 During an interview with the Provedor, he highlighted a number of additional handicaps he faces which prevents him from carrying out his responsibilities more effectively. For example, there is no law that protects witnesses, nor to force Government officials to disclose assets. The judicial system is considered weak and subject to corruption itself. The Office has plans to establish an "intelligence group" to gather evidence against suspected individuals, and to devise mechanisms to encourage "whistle blowers", but lacks funding. While the Office was generally content with the support it had received from the Bank, it felt that tying funds originating from the Bank to specific line items in the national budget had proven inflexible at times. The Provedor also felt that, due to cultural proximity, receiving technical assistance from neighboring countries like the Philippines, Malaysia, Hong Kong, or Singapore is likely to be preferable than from further places.

6.17 On balance, despite the initial delay in establishing and staffing the Office, the handicaps it is operating under, and its limited achievements so far; this review agrees with the Bank's operational staff that having a Provedor's Office with competent staff is a desirable achievement whose returns are likely to be forthcoming in due course. This said, it is not clear whether it merited the priority it had received throughout the TSP series, given the relatively petty nature of corruption in the country so far, but with rising oil revenues the challenge of corruption may increase.

6.18 The experience of the ***Office of the Inspector General*** has been quite similar to that of the Provedor's. In fact, there has been some overlap in their functions, but they have tried to coordinate to avoid duplication of efforts.

6.19 This Office was established in 2002 during the UNTAET period, within the Prime Minister's staff, to conduct inspections, audits, and investigations of corruption exclusively within the civil service. In case criminal actions are suspected, the Office recommends to the Prime Minister to refer the case to the Prosecutor General. Alternatively, in some cases, informal contacts are made with the line ministries involved to try to resolve the situation more directly and rapidly.

6.20 As of early 2008, the Office had investigated 87 cases concerning allegations of misconduct. Many of those cases ended up revealing that the causes of the alleged misconduct were actually related to poor systems in place, or shortages of skills; and recommendations were made accordingly to the line agencies concerned. In some of those cases, the agencies acted on the recommendations. In one case that was widely publicized and involved using misuse of Government vehicles, a law was passed prohibiting the use of such vehicles for private purposes. Out of the 87 cases, 11 were of a criminal nature, and their files were forwarded to the Prosecutor General. Some of those were dropped due to insufficient evidence, others investigated, but only one case proceeded to court. The civil servant involved was convicted of receiving a bribe of $3,000. He was simply asked to return it, but ultimately kept his position and suffered no other penalties. The interview with the Inspector General revealed that he had heard of more significant cases of corruption involving larger investors, but had not faced anything of this nature formally. In his view, it has been difficult to measure the extent and level of corruption in the country due to flimsy evidence. As with the Provedor, he believed that the judicial system remained very weak, and that the eleven magistrates lacked the experience needed to deal with corruption, and needed training to upgrade their skills The Office itself still suffered from the lack of an Organic Law, which has not been approved yet. Such a law would formalize its functions and give them more clout. The Inspector General also complained that his Office suffered from a lack of qualified staff and office facilities.

6.21 As with the Provedor's Office, this review concluded that the support given to the Inspector General's Office under the TSP series was worthwhile and, on balance, a modest achievement, despite the very limited results so far. In due course, it could prove to have been a good investment to combat more openly serious cases of civil service misconduct.

6.22 ***Budget execution*** has been very slow and hesitant, despite improvements in budget planning, monitoring and evaluation. This has been attributed to the severe capacity constraints and to the reluctance of the MFP to delegate spending authority to line ministries, or to lower echelons within the Ministry itself. In view of the capacity constraint, perhaps more effort should be directed to improving implementation than to seemingly devise endless and redundant planning and monitoring instruments.

6.23 Government officials and staff of donors, including the Bank, all admit that progress in the development of the ***judicial sector*** has been very limited and disappointing, with the number of competent magistrates still very limited, the backlog of adjudicated cases rising, and the suspicion that this sector itself is handicapped by corruption.

6.24 The ***public works*** program that was designed to bring about immediate employment opportunities to generate income, promote growth, and reduce poverty; produced very limited results. A main reason seems to have been the reluctance of the funding authorities to disburse funds, fearing that they would be misused.

6.25 Despite its importance, particularly for poverty reduction, the performance of the ***education sector*** was partial, and broadly disappointing, especially compared to that of the health sector. It seems that in health, the local capacity constraint was overcome by contracting with a neighboring country to provide trained personnel. Apparently, this was not easy to replicate in education because of the language barrier. Teachers would need to be able to instruct in the main local language, Tetum.

6.26 Progress achieved in ***private sector development*** was mixed. Some legislation that would facilitate business dealings was passed, and some other was still pending, or in progress, as of early 2008. An export promotion agency (TradeInvest Timor-Leste) was established, albeit after the closing of TSP III. Business Development Centers had trained a large number of participants. However, business registration and procedures in general were still cumbersome. More importantly, any administrative or legal achievements that had taken place, had not led to any significant job creation, and the private sector had remained a far cry from serving as an engine of growth. The Emigrant Workers'

Program, designed to encourage employment abroad, had so far led to relatively insignificant number of migrant workers; at most a hundred, or so.

6.27 Most of the other areas of the Action Matrices had also witnessed partial, or limited, progress compared to expectations, as elaborated in the ICR for TSP III, which also assessed achievements of the entire TSP series.

Remarks

6.28 As elaborated earlier in this report, creating the conditions for ***sustainable growth and poverty reduction*** has been the main pillars of the country's NDP and the Bank's CAS from the days immediately after independence. As such, they have also served as the main ultimate objectives of the TSP series.

6.29 National accounts data in Timor-Leste remain rather approximate and, according to the IMF, should be viewed as indicative trend figures rather than robust statistics. With that in mind, the IMF used estimates produced by consultants working with the Ministry of Finance, and reported that non-oil real GDP growth was around 5 percent annually in both 2004 and 2005, and dropped precipitously to almost minus 6 percent in 2006, presumably due to the serious disturbances in that year (Recall that the TSP series covered the FY03-05 period. So, 2004-2006 could be considered an appropriate period to consider for assessing the effect of TSP on growth).

6.30 With the above caveats in mind, and recognizing that attributing any direct impact of TSP measures to growth is a very questionable methodological leap, one may simply conclude that the economy's overall structure and performance remained quite fragile, fluctuating considerably, depending more on political events and other exogenous shocks than on policy performance in the short- to medium-run, in response to actions under the TSP.

6.31 The impact of the TSP series on ***unemployment and poverty reduction*** is also likely to have been insignificant, despite the lack of data to substantiate such an assertion. In view of the very high population growth of around 4 percent, and the predominantly young population, the growth of employment opportunities could not possibly have been catching up with new entrants into the labor force. This is a very serious problem and a major challenge facing the country. Combined with the troublesome domestic political rifts, this makes pronouncements that Timor-Leste has already achieved ***political stability*** pre-mature, as evidenced by the several civil disturbances that have occurred since independence, including the riots that broke out as late as the summer of 2007, in connection with the presidential elections at that time; and the attempts on the lives of the President and the Prime Minister in February 2008.

Program Achievements

6.32 The above paragraphs (6.1 – 6.26) attempted to provide an overall, bottom-line assessment of outcomes, highlighting the major achievements and major areas of partial or poor progress. In line with this assessment, and based on the above discussions of implementation experience under the three separate operations (chapters 3-4); the outcomes by component of the three operations taken together is summarized in Table 4.

Table 4: Implementation Progress by Component for the Cumulative Three Operations

1) Governance	Overall partial progress. The PF is a major achievement. Budget planning and monitoring good; but budget execution poor. Offices of Ombudsman and Inspector General achieved partial progress, whereas the development of the judicial sector showed very limited progress. The creation and administration of the Petroleum Fund represent important improvements in Timor-Leste institutional settings and are an important ingredient of sustainable growth for the country.
2) Service Delivery	Overall partial progress. The health sub-component performed well. The education sub-component showed partial, broadly disappointing results. On the other hand, there are strong signals that the situation of the veterans of the resistance movement against Indonesia will improve, as important legislation was passed, a database registering veterans was created, and a share of the budget was allocated for pension payments
3) Job Creation	Overall disappointing progress. The development of the private sector in general and the agricultural sector in particular, has been quite limited. The impact, direct or indirect, on poverty reduction seems to have been negligible, if any.
4) Power Sector	This component was only in TSPI, and was not carried through to the next two operations. Overall partial progress. Initial progress made due to installation of new emergency capacity and metering. This has since eroded due to political reasons. Other measures under this component met with limited progress.

6.33 ***Outcome.*** Keeping in mind the dire state of affairs in this new, post-conflict country at the dawn of its independence, and that the main underlying objective of the donor community, including the Bank, was to provide urgently needed bridge, grant-financing to help in developing the basic institutions and planning framework of the state. There were significant achievements in a few key areas. The establishment and proper functioning of the Petroleum Fund, by itself, is a major achievement and success story for the country's governance structure, since it has managed to safeguard the nation's new-found wealth until it develops the capacity to be able to use it better. In fact, the balance of the Petroleum Fund has tripled in a year and half reaching US$ 1.8 billion in September of 2007. The robust achievements in the health sector are also commendable. In addition, there is broad agreement by a cross-section of Government officials, members of the donor community, and operational staff of the Bank that have been intimately involved; that the TSP series has been very helpful to the Government in establishing a process and framework for planning, monitoring and evaluation that has enabled it to better link its economic development objectives to budget allocations, in a coordinated manner with the donor community. Despite clear remaining shortcomings of this process and the poor experience with budget execution so far, the Government has unequivocally expressed its appreciation and gratitude for this achievement. After factoring in the realities on the ground in this nascent, post-conflict country; based on the views of the client (gained from extensive interviews with officials), donor representatives, and Bank staff involved in the operation, this PPAR was able to consider in far more detail the significance of partial progress made thus far.

6.34 However, notwithstanding significant progress made in some areas, the fact remains that only partial results were achieved in most of the other areas of the program. are in line with ratings given by the IEG ICR Review Evaluation Summary (ES) for TSP II and III. The self-assessment ICR's ranking of satisfactory for TSP II and III appears too generous, given that many outcomes fell short of expectations, even if an allowance is made for the claim that the program design was intentionally ambitious to begin with.

6.35 ***Relevance of program objectives and design.*** As indicated in the ICR reviews (for TSP II and III), the overall program objectives were very relevant given the acute lack of capacity in the country, the need to reform the budget and improve public expenditure management, as well as achieve better service delivery. The main thrust of the TSP series was highly relevant as IDA joined forces with other major donors to provide urgently needed bridge grant-financing. This prevented this new, poor country from starting off by incurring debt, or cutting back on an already modest level of public expenditures that were, in any case, used mainly to run a basic public administration and security forces during a period of political uncertainty. The series also aimed at supporting the development of basic policies and institutions needed for the proper functioning of this new state. Although a number of areas for this support were highly relevant, such as health, education, job creation, the proper management of petroleum revenues, setting up and developing basic planning and administrative institutions; the effort was diffused by including many other areas of lesser priority and relevance at that early stage of the country's development. Those included several regulatory and governance matters that are preferably addressed at later stages in a country's development. In short, the resulting project design was too complex for the country and overwhelming for the government. It detracted from the limited capacity of the government to clearly select priorities and perform its key functions. The relevance of program design was, therefore, only modest - hence the overall relevance of the program was modest.

6.36 ***Efficacy – Achievement of Objectives.*** As detailed in the ICR Reviews of TSP II and III, echoed and further elaborated in the previous chapters devoted to individual TSP operations, and summarized in the paragraphs 6.1-6.32 and in particular in Table 4, the program had a number of significant achievements in some areas of improved governance and better service delivery. However, in many other areas envisaged under the project appraisal documents (PADs) for the three operations there was only partial or insufficient progress, especially in the important area of creating new jobs. It is significant to note that the PADs did not contain specific sections that dealt directly and clearly with explicit objectives of the program as a whole. They contained discussions of program rationale (bridge-financing to help set up basic institutions and functions in a period of transition), and moved directly to discussing program components, without an explicit statement of clear, more specific objectives. The PAD for TSP I included a couple of sentences stating that, "The program is broad ranging, seeking to put in place the basis framework for an open and democratic state apparatus in the period immediately after independence. Given limited capacity, the creation of fully functioning institutions is likely to be a much longer process." This absence of a clear statement of specific objectives may explain the "intentionally" broad, and therefore diffuse, program design; and makes it difficult to assess the efficacy of the program as a whole. Overall, the TSP program recorded *modest achievement* in the areas of good governance and better service delivery, and *negligible achievement* in creating new jobs.

6.37 To be fair to Bank staff (and most likely to the staff of other donors as well), there was an intensive debate among those involved in the preparation and appraisal of the projects on this matter, with some arguing for a more focused design targeted on a much smaller number of better defined, more tangible objectives; and others feeling that the Bank should be responsive to the Government's desire to have the donors' support across the whole range of its activities. As one Bank staffer from the second group put it, "had we not gone along with the wishes of the most senior Government officials, we would have most probably lost their interest." In the end, the position of this second group prevailed, and the result was the set of extensive, rather unwieldy, Action Matrices, with an extremely wide range of actions, the so-called "all-of-Government" approach. These matrices seem to have developed a life of their own, and grew in the process. A Government agency that wanted to have its work program included in the national budget felt that it had to have it included in the matrix. The problem was a lack of explicit priorities to be imposed over the measures. The much smaller sub-sets of "prior actions" selected for the three operations seem to have been chosen because they had already been implemented prior to a particular operation's approval, rather than for having obvious priority over many other measures.

6.38 ***Risk to Development Outcome.*** The simplified ICR for TSP II gave it a rating of *likely* for sustainability (which was the criterion used before changing it to "risk to development outcome"), and the full ICR for TSP III gave it a rating of *low or negligible* for risk to development outcome. This review considers the second rating in particular to be too optimistic. In fact, it considers that the justification for this second rating presented in the ICR itself to be inconsistent with the rating. The ICR did express concerns over the unstable political and social situation, the high level of unemployment among the youth, the very low implementation capacity, and the risk of corruption that faces increased petroleum revenues over time (despite the good performance of the Petroleum Fund so far); but still gave a rather optimistic "low or negligible" rating. In fact, the concerns listed in the ICR itself are quite serious; particularly the domestic, political fault-lines that continue to be the cause of serious friction and violence that could spin out of control. As such, this risk to development outcome may be considered increasing. Moreover, some of the successful results achieved so far, as in health sector, have depended so far on the presence of specific individuals in key positions, and may not be rooted in solid institutional commitments. In addition, already in early 2008, there were some concerns being voiced by some well-placed Timorese that considerable pressure is building up to raise the ceiling on budgetary withdrawals from the Petroleum Fund, and also some indications that expatriate advisors who have been proponents of caution within this Fund, may be asked to leave. For all these reasons, this review agrees with the ratings in the ICR Reviews of TSP II and III and assesses the risk to development outcome as *significant*.

6.39 ***Bank Performance.*** The evaluation of the Bank's performance recognizes the realities in the country and the strong desire by the client to follow a broad, all-encompassing approach in the program design. It also takes into account that this matter was seriously debated within the Bank, among the donor community, and with the Government at the program design stage. The fact remains that the Bank gave in and designed a very complex program for a post-conflict country with severely limited capacity. Greater realism and a more careful risk assessment at entry would have suggested a much more streamlined and focused project design, of which the Bank could have easily convinced the borrower. Furthermore, changes could have and should have been made during the implementation of the first operation and in the design of subsequent operations (TSP II and III) to address clear implementation difficulties and focus on the achievement of priority project objectives. Overall, Bank performance in the TSP program is rated *moderately unsatisfactory*.

6.40 ***Borrower Performance.*** Government clear interest in obtaining Bank and donor financial and institutional support for its national development program was not accompanied by true ownership and commitment to achieve the wide-ranging and overly ambitious development objectives set in the TSP operations. Partially caused by the oversupply of donor resources, and weak and unclear Bank/donor feedback, the Government failed to select clear priorities and realize its own implementation capacity constraints. Hence, with ambitious project design, Government limited resources were spread too thinly across too many competing development priorities leading to weak implementation of many actions/components. The *de facto* priorities were established only through implementation leading to partial achievement of project objectives. Unfortunately, little was learned from this experience as it was not used to redesign the subsequent TSP operations or to boost implementation capacity. Overall, Borrower performance in the TSP program is rated *moderately unsatisfactory*.

6.41 The Bank, the other donors and the Government realized from the beginning that the program was ambitious and recognized implicitly that it would only achieve partial success, as it did. To that end, both the Bank and the Borrower devoted considerable, serious and professional efforts in designing, programming and monitoring the implementation of the details of the wide range of measures. The supervision and aid coordination effort was intense and professional; and appreciated by the Government, despite the heavy burden it placed on its limited capacity. For its part, the Borrower was involved in the daunting task of building a new nation following a devastating two and a half decades of fighting an occupation; and it felt the imperative to do so on a broad front. Given the severe capacity constraints that handicapped its abilities, it managed to achieve a few notable successes and partial progress along the broader front, in line with its expectations. The few, competent members of the small political elite and the civil service were directly responsible for the few initial, but notable, achievements. Had the parties involved agreed from the beginning on a more focused approach with tighter priorities, as some of them called for, it is likely that the rate of success would have been higher, and their performance might have been more satisfactory. The rating of satisfactory given by the ICRs for TSP II and III does not sufficiently account for the fact that the programs achievements were only partial.

6.42 ***Monitoring and Evaluation:*** Monitoring was made difficult during the first TSP operation and, to a large extent, remained a problem in the second TSP due to limited capacity and excessive complexity of the project which imposed a large burden on the government. Although the government's TSP Action Matrix was an important resource and an exhaustive organizing framework for a comprehensive M&E system, it did not allow for prioritizing and selecting where to proceed in the absence of adequate progress across the board. Evaluation appears to have been mechanically focused on meeting conditions (prior actions) with little attention to performance indicators and ensuring that the reforms were having an impact on the population. Based on continuous albeit slow progress, a better system for monitoring the implementation of project conditions was in place only for TSP III. The TSP action matrix played a key role in tracking implementation and in identifying priorities for implementation. Quarterly benchmarks helped identify areas of progress, those needing more attention, and areas seriously lagging behind. Despite such clear signals coming out of the M&E system in the third project, the follow-up was missing, especially when it came to selecting clear priorities and following through on the implementation of critical reforms. Overall, the quality of the M&E system for the TSP program is rated as *modest.*

7. Lessons

7.1 The most important lesson from this TSP experience is for the Bank to argue more strongly to try to convince borrowers to agree to more ***focused program design***, with ***tight priorities***, especially for grants or loans that are disbursed in one tranche upon effectiveness, and are provided as generalized budget support. This would normally increase the likelihood of achieving program objectives in a timely and efficacious manner. If faced with a similar situation to that which existed in Timor-Leste where the Government feels strongly that it needs support for a broad-fronted program involving a large number of time-consuming institutional measures with a high technical assistance (TA) content, it would be preferable to provide a specific TA operation with an appropriate implementation horizon, likely to take a few years.

7.2 In cases like Timor-Leste where there is a relatively high, and possibly increasing political risk due in large measure to high unemployment among disgruntled youth, much more attention and effort should be give to creating jobs and achieving 'quick wins" in poverty related services and through work programs. Whereas this was indeed a major objective of this TSP series, the actual effort in this regard was diluted considerably by the inclusion of wide range of measures, many of which could have easily waited for a later stage in the development drive.

7.3 Where capacity limitations are severe, as in the case of Timor-Leste, TA is normally required to help do the work itself, and also to train a large number of personnel. Ideally, it is very attractive if the two can be combined. In practice, however, it is normally inevitable in such cases that, if the same technical advisor is required to do both; the pressures of delivering the work itself outweighs the training objective, and capacity building is short-changed, or delayed. Therefore, consideration should be given to the appropriateness of providing ***TA which is dedicated entirely to training***, in parallel to advisors who actually do part of the work.

7.4 Quite often, but particularly in countries with limited qualified personnel, success is highly correlated with working with the more competent and committed counterparts, as this review has pointed out. This could be a delicate matter in practice, but where possible, it would be better for the Bank to try to ***focus support around proven achievers,*** while seeking to develop institutional capacity.

7.5 Despite its costs to the Government and its development partners, which can be high at times, the benefits of ***active donor coordination*** are worthwhile, as demonstrated by the experience under the TSP program.

Annex A. Basic Data Sheet

FIRST TRANSITION SUPPORT PROGRAM (DEVELOPMENT GRANT FACILITY)

Key Project Data *(amounts in US$ million)*

Financial

	Appraisal estimate	*Actual or current estimate*	*Actual as % of appraisal estimate*
Total project costs	--	50.58	--
Grant Amount	5.0	5.0	--
Cofinancing		27.98	--
Cancellation	--	--	--
Institutional performance	--	--	--

Project Costs and Financing

Project cost by Tranche	*Appraisal Estimate*	*Actual Estimate (Disbursed)*	*Percentage of Appraisal*
First tranche	--	5.0	100
Second tranche	--	--	--
Third tranche	--	--	--
TOTAL	--	5.0	100

Project Dates

	Original	*Actual*
Initiating memorandum	1/4/2002	3/14/2002
Negotiations	6/20/2002	6/20/2002
Board approval	7/30/2002	7/22/2002
Signing	--	7/23/2002
Effectiveness	--	09/23/2002
Closing date	7/31/2007	6/30/2004

Staff Inputs (staff weeks)

Stage of Project Cycle	*Actual/Latest Estimate*	
	No. Staff weeks	*US$ ('000)*
Lending	22.00	170,885
Supervision	11.60	88,144
Total	33.60	259,029

Note: The current MIS does not provide information on the actual staff weeks spent during the project cycle.

Mission Data*

	Date (month/year)	*No. of persons*	*Staff days in field*	*Specializations represented*	*Performance rating*	*Rating trend*	*Types of problems*
Identification/ Preparation							
Appraisal/							
Supervision							
Completion							

* Data not available.

Other Project Data

Borrower/Executing Agency:

FOLLOW-ON OPERATIONS			
Operation	***Credit no.***	***Amount (US$ million)***	***Board date***
Second Transition Support Program	4061	4.17	10/31/2004

SECOND TRANSITION SUPPORT PROGRAM (TSI II) (GRANT NO. 4061 TP)

Key Project Data *(amounts in US$ million)*

Financial

	Appraisal estimate	*Actual or current estimate*	*Actual as % of appraisal estimate*
Total project costs	27.00	35.96	133
Loan amount	--	--	--
Cofinancing	23	31.79	138
Cancellation	--	--	--
Institutional performance	--	--	--

Project Costs and Financing

Project cost by Tranche	*Appraisal Estimate*	*Actual Estimate (Disbursed)*	*Percentage of Appraisal*
First tranche	4.00	4.17	104
Second tranche	--	--	--
TOTAL	4.00	4.17	104

Project Dates

	Original	*Actual*
Initiating memorandum	--	4/01/2003
Negotiations	--	4/21/2003
Board approval	--	7/22/2003
Signing	--	09/05/2003
Effectiveness	10/10/2003	10/10/2003
Closing date	10/31/2004	10/31/2004

Staff Inputs (staff weeks)

Stage of Project Cycle	***Actual/Latest Estimate***	
	No. Staff weeks	***US$ ('000)***
Identification/Preparation	6.18	20.5
Appraisal/Negotiations	9.52	32.8
Supervision	17.26	57.4
Completion	2.00	3.5
Total	34.96	114.2

Note: The current MIS does not provide information on the actual staff weeks spent during the project cycle.

Mission Data

	Date (month/year)	No. of persons	Specializations represented	Performance rating	
				Implementation Progress	Development Objective
Identification/ Preparation	February 4-15, 2003	1	Public Sector	S	S
Appraisal/	April 21 to May 3, 2003	1	Public Sector	S	S
		1	Public Finance		
		1	Governance		
		1	Judiciary		
		1	Education		
		1	Health		
		1	Veterans		
		1	Social Sectors		
		1	Private Sectors		
		1	Agriculture		
		1	Power Sector		
		1	Police		
Supervision	October 20 to November 3, 2003	1	Public Sector	S	S
		1	Public Finance		
		1	Governance		
		1	Judiciary		
		1	Service Delivery		
		1	Veterans		
		1	Private Sector		
		1	Agriculture		
		1	Police		
Supervision	April 19 to May 3, 2004 *(combined with Appraisal of TSP III)*	2	Public Sector	S	S
		1	Procurement		
		1	PEM		
		1	Governance		
		1	Judiciary		
		1	Education		
		1	Health		
		1	Veterans		
		1	Monitoring		
		1	Police		
		1	Gender		
		1	Private Sector		
		1	Agriculture		
		1	Power Sector		
Completion	October-December 2004	2	Public Sector	S	S

Other Project Data

Borrower/Executing Agency:

FOLLOW-ON OPERATIONS			
Operation	**Credit no.**	**Amount (US$ million)**	**Board date**
Third Transition Support Program	H1310	5.0	10/28/2004

THIRD TRANSITION SUPPORT PROGRAM (TSP III)

Key Project Data *(amounts in US$ million)*

Financial

	Appraisal estimate	Actual or current estimate	Actual as % of appraisal estimate
Total project costs	--	75.10	--
Loan amount	4.96	5.0	--
Cofinancing		26.4	--
Cancellation	--	--	--
Institutional performance	--	--	--

Project Costs and Financing

Project cost by Tranche	Appraisal Estimate	Actual Estimate (Disbursed)	Percentage of Appraisal
First tranche	5.0	5.0	100
Second tranche	--	--	--
Third tranche	--	--	--
TOTAL	5.0	5.0	100

Project Dates

	Original	Actual
Initiating memorandum	--	4/13/2004
Negotiations	--	9/20/2004
Board approval	--	10/28/2004
Signing	11/25/2004	11/25/2004
Effectiveness	12/08/2004	12/08/2004
Closing date	--	10/31/2005

Staff Inputs (staff weeks)

Stage of Project Cycle	Actual/Latest Estimate	
	No. Staff weeks	US$ ('000)
Lending	64	291
Supervision	19	112
Total	83	403

Note: The current MIS does not provide information on the actual staff weeks spent during the project cycle.

Mission Data*

	Date (month/year)	No. of persons	Staff days in field	Specializations represented	Performance rating	Rating trend	Types of problems
Identification/ Preparation							
Appraisal							
Supervision							
Completion							

*Please see mission date for the Second Transition Program.

Other Project Data

Borrower/Executing Agency:

FOLLOW-ON OPERATIONS

Operation	*Credit no.*	*Amount (US$ million)*	*Board date*
--	--	--	--

Annex B: TSP I: Implementation Progress of Actions Matrix

First Component: Poverty Reduction Planning and Quick Wins

Completed Actions
Review AAPs and prepare AAPs for FY2004.
Present Road Map for FY03-07 to stakeholders.
Finalize concept paper on participative improvement of NDP.
Increase number of midwives from 135 to at least 214.
Increase DPT3 coverage for under one-year olds from 51 percent to 58 percent.
Staff the Veterans' Affairs Unit.
Develop program for social reintegration and rehabilitation of vulnerable groups.
Train staff involved in social service provision.

Partially Completed and Ongoing Actions
Develop and implement mechanisms for child protection.

Actions Not Completed
Develop social policy on disability, gender, and humanitarian affairs.

Actions Postponed to FY2004
Submit a policy framework and action plan for primary and secondary education.
Verify that the registering of veterans is complete.
Hold a seminar on the international experience regarding criteria and policies on veterans.

Second Component: Governance and Private Sector Development

Completed Actions
Review implementation of FY2003 legislative program.

Partially Completed and Ongoing Actions
Adopt FY2004 legislative program.
Promulgate, after consultation, the decree law on land.
Conduct a feasibility study regarding industrial zones.

Actions Not Completed
Submit legislation regarding public prosecutors and defenders to Parliament.

Actions Postponed to FY2004
Implement legislation on companies, contract, and bankruptcy.
Nominate an Ombudsman.
Generalize the information campaign on the role and functions of the Ombudsman.
Launch a pilot information campaign on fees for basic public services.
Submit civil service statute to Parliament.
Complete studies on decentralization options and discuss with stakeholders.
Implement legislation on foreign investment.

Continue to compile and publicize information on complaints of absenteeism, irregularities, and corruption among civil servants; and investigations and actions taken by concerned ministries and the Inspector General.

Third Component: Public Expenditure Policy and Management

Completed Actions
Maintain macroeconomic stability.
Continue to monitor economic and social indicators and development.
Publish pro-poor FY04 budget in line with FY04-06 Medium Term Fiscal Framework.
Contract auditor for FY03 accounts.
Prepare comprehensive FY04 budget.
Issue a directive on project appraisal and monitoring procedures.
Prepare FY04 Budget Books identifying projects as individual cost centers.
Implement a civil service human resource management and payroll system.

Partially Completed and Ongoing Actions
Set up and make operational the Automated System for Customs Data (ASYCUDA).
Ensure that FY03 budget execution is in line with appropriations.
Submit the recommendations of the study on pay policy to the Council of Ministers.
Approve and publish the vehicle standardization policy.

Actions Postponed to FY2004
Approve capacity building strategy and plan for FY2004.Submit medium-term program for economic and social statistics to the council of Ministers for approval.

Fourth Component: Power Sector

Completed Actions
Submit draft legislation to Parliament for the establishment of a Power Sector Regulator, and the creation of an autonomous power enterprise.

Partially Completed and Ongoing Actions
Install pre-paid meters to start under the Management Contract, if that option is selected.
Conduct a mid-term review of the preparation of a national power development plan.
Formulate TOR for the second phase of the preparation of the national power plan.
Conduct final review of the national power plan.
Discuss draft of this plan with stakeholders and finalize.

Actions Postponed to FY2004
Start contract negotiations.
Mobilize staff and equipment.
Hand over the electricity assets to the management contractor.
Produce management contractor progress reports

Annex C: Prior Actions for the Individual Operations (TSP I, II, and III)

TSP I

a) Approved and published the NDP for FY03-07.
b) Published and disseminated the "popular" version of the NDP.
c) Prepared a draft policy framework for the Ombudsman's office, and initiated civil society consultations.
d) Prepared the FY03 budget, with detailed budget line items, staffing profiles, and performance indicators for Government agencies.
e) Included the guiding principles for the Recipient's oil fund in the FY03 budget.
f) Presented to Parliament the FY03 budget with appropriated core consolidated Fund expenditures of $67.7 million (excluding appropriated and supplementary capital and development expenditures and programmed savings of the Timor Sea Account); with (i) a permanent payroll of less than 16,400 staff, (ii) a share of the health and education sector of more than 35 percent of core Consolidated Fund programmed expenditures, and (iii) expenditure allocations for defense and public order less than 22 percent of core Consolidated Fund programmed expenditures.
g) Prepared a revised chart of accounts for the execution of the FY03 budget, which specifies line items for consumables and temporary employees.
h) Conducted an interim audit of the FY02 financial statements, up to May 20, 2002, the date of independence.
i) Employed an interim management team for the Power Service for the period from may 20, 2002 to August 30, 2002.
j) Appointed a consultant to prepare TOR and performance indicators for the management contract for the East Timor Electricity Authority.

TSP II

a) Approved the Statutes of Ombudsman (Provedor).
b) Promulgated the Public Service Statute, including a framework for management systems and disciplinary procedures.
c) Prepared the FY05 Annual Action Plan and presented the FY05 budget to Parliament.
d) Established the Superior Council of the Judiciary, which had been created by Law 8/2002. This council initiated its functions.
e) The Ministry of Health established annual district health plans. The Ministry of Education, Culture, Youth and Sports developed a pilot program in decentralized financial management by schools and parent-teacher associations.
f) Approved the policy framework for the agriculture sector.
g) Promulgated the law on commercial entities to promote private sector development.

TSP III

a) Established the Ombudsman's Office and appointed the Ombudsman.
b) Approved a directive on the policy and legislative process.
c) The Office of the Inspector General published a summary report on investigations and recommended corrective actions.
d) A study on implementation arrangements for independent audit was submitted to the Council of Ministers.
e) The Budget and Financial Management Law was submitted to Parliament.
f) The Public Procurement Decree Law was approved by the Council of Ministers.
g) A Petroleum Fund Law was submitted to Parliament, together with a savings policy, prepared following an open and consultative process.
h) Disciplinary regulations for the civil service were approved.
i) The Superior Council of the Judiciary carried out inspections, enforced decisions on disciplinary cases, and published resolutions.
j) The FY06 budget and the Medium-Term Expenditure Framework were submitted to Parliament, on a combined sources basis.
k) A pilot grant mechanism for primary schools was implemented, with a view to integrate allocations in the FY06 budget.
l) A Business Forum was established, and two sessions held during FY05.

Annex D: TSP II – Implementation Progress of Action Matrix

Sector	Output / Indicator and Target	Achievement in TSP II (FY2004)	Actions for TSP III (FY2005)
	TSP II Thematic Area: Governance		
Oversight Institutions	• Annual legislative program of Council of Ministers (CoM) Implemented • Guidelines on policy and legislative process developed • Office of the Ombudsman (*Provedor*) operationalized • Strategy for investigation of complaints regarding civil service	• Less than half of scheduled legislation has been finalized, but some progress on prioritization and scheduling • Work on the development of procedures for policy and legislative process has not yet started • Organic Law for the Office of the Provedor approved; Provedor selection underway • Organic Law for Office of the Inspector General (OIG) prepared for submission to CoM; OIG actively pursuing inspections	• Policy and legislative process approved • Office of the Provedor established, equipped and staffed; annual report submitted to Parliament • Organic Law on OIG passed; summary reports published on investigations and corrective measures
Local Government	• Legislation on State Local Administration and Local Government submitted to CoM, with strategy for establishment of local government structures • Legitimized community authorities in sucos and villages • Draft proposal on local government funding mechanism and framework for capacity building and donor financing	• Local Government Options Study completed; comparative study of developing country decentralization experiences ongoing • Decree Law on Community Authorities approved, providing for *suco* elections (elections planned for mid FY2005) • Not completed due to the need for a phased approach; rescheduled to TSP III	• Selection of local administration option • Draft policy and implementation plan for Local Administration
Public Sector Management	• Public Service Statute and Disciplinary Regulation; senior management training in disciplinary procedures • Draft Human Resources (HR) Policy addressing, amongst others,	• Public Service Statute approved; supplementary regulations needed • Manual on basic personnel transactions prepared; HR policy dropped from TSP to allow focus on basic systems	• Plan for Public Service Statute supplementary legislation and regulations; disciplinary regulations approved by CoM

Sector	Output / Indicator and Target	Achievement in TSP II (FY2004)	Actions for TSP III (FY2005)
	recruitment, personnel appraisal and information • Line agency HR Units in priority line agencies created and trained • 25% of permanent staff on payroll registered in HRIS database with supporting personnel files	• HR Units established in most agencies; training underway • Progress slower than anticipated; computerization option selected but not implemented until hard copies in place and staff trained	• Plan for public service personnel filing system approved, funded and implemented
Justice Sector	• Law on Public Prosecutors and Public Defenders • At least 8 sessions of the Superior Council of the Judiciary (SCJ) conducted • Improved ratio of cases resolved and cases lodged • Systems for registration and delivery of registration services, including notary, civil identification, and state property administration	• Draft Organic Laws for Public Prosecutors and Public Defenders under revision based on CoM comments • Regular meetings of SCJ have taken place • Limited progress on information and administrative Systems • Decree Laws on Notary and Civil Registration approved	• Prosecutors and Public Defenders approved • Inspections undertaken by SCJ and resolutions published • Back log in cases reduced across the system • Notary and registrations delivery systems implemented; Public Registrations Decree Law approved
Poverty Reduction Planning	• Annual planning exercise well understood by Ministries; Annual Action Plans (AAP) consistent with policy and budgets • Promotion of a high-level consultative mechanism as a fully independent body	• Workshop held to review prioritizing and sequencing experience; AAPs and quarterly reporting matrixes prepared • Initial progress made in establishing high-level consultative mechanism, including workshop and working groups, but no committee meetings held yet	• AAPs for key institutions incorporate gender sensitive plans • Implementation waiting recommendation of civil society working group
Public Expenditure Management	• HR Development strategy for financial management functions	• No progress	• Short-term training for MPF and financial management cadre; formulation of longer term financial

Sector	Output / Indicator and Target	Achievement in TSP II (FY2004)	Actions for TSP III (FY2005)
	• Formulation of a pro-poor FY2005 budget in line with national priorities • Monitoring implementation and cost-recovery of Power Sector Management Contract • Accurate, Comprehensive, timely data on economic and social indicators • Submission of a revised Budget and Financial Management Law to Parliament; and related revision of Treasury Manuals • Improved timeliness of procurement; development of procurement strategy; procurement staff training; submission of revised Procurement Law	• Good progress in disciplining the budget process (submissions only 3.5% over spending limits); slow budget execution • Management contract signed; team fielded; 10,000 prepayment meters installed; service provision still patchy • Progress in preparing for census implementation (fielded in July/August 2004); regular publication of price and trade • statistics launched • Budget and Financial Management Law under review based on CoM comments; submission to Parliament expected in FY2005 • Timeliness of procurement has deteriorated; Procurement Decree Law being revised based on CoM comments; draft procurement manual distributed to line ministries for comments	management capacity building program • Budget execution in line with appropriations schedule • Progress monitored against management contract performance indicators Progress monitored against management contract performance indicators • Budget and Financial Management Law submitted to Parliament • Procurement plans for education, health and roads approved by MPF; report on procurement processing against targets
Sector	**TSP II Thematic Area: Service Delivery and Poverty Reduction**		
Health	• Formulation of micro-policies in 9 priority areas • Hospital spending below 40% of CFET health spending • DPT3 immunizations, 68% of children under 1 year • Measles vaccination, 58% of children under 1 year • Attended deliveries, 45% • Outpatient visits, 1.8 per capita • District Health Plans in place and monitored in all districts	• Completed • Hospital spending in line with 40% target • 71%, excluding 4 districts and the National Hospital • 68%, excluding 4 districts and the National Hospital • 43%, excluding 4 districts and the National Hospital • 2.3 as of May 2004 • Annual district health plans established as routine tool	• 4 priority health policies/ strategies approved • Hospital spending below 40% of CFET health spending • 72% • 70% • 50% • 2.4 • Six-monthly report on service performance for all districts
Education	• Education sector policy and legislative	• Education policy submitted to CoM; work on the legal	• Basic Law on Education; MOECYS Organic Law;

Sector	Output / Indicator and Target	Achievement in TSP II (FY2004)	Actions for TSP III (FY2005)
	framework • Curriculum framework for primary education developed, adopted and implemented • Training program for pre-secondary education teachers • 50 key managers complete educational management training program • Pilot mechanism for channeling funds through School Councils	framework well advanced • Curriculum working groups established; primary curriculum ready for piloting in FY2005 • Launched with much higher enrolment than anticipated • Rescheduled to FY2005 • Pilot program was designed and supporting manuals prepared, but program was not launched	regulations on tertiary and private education completed • Adoption of new primary education curriculum • 50 key managers complete educational management training program • Pilot grant mechanism implemented and decision on future follow-up
Vulnerable Groups	• Definition, identification and registration of veterans and ex-combatants • Policy for veterans and ex-combatants	• Largely completed after public Consultation • Rescheduled to FY2005	• Veterans policy approved and legislation finalized
Sector		**TSP II Thematic Area: Job Creation**	
Private Sector Development	• Finalization of company and investment laws • Legislation on land administration, mediation, cadastre system, and state-owned property management • Community-based road maintenance program, with 2,762km of roads maintained and 122 working days/km • Commitment from Timor Sea Office to onshore investment • Emigrant worker program, 500 overseas jobs created	• Law on commercial entities promulgated; 2 draft investment laws submitted to CoM; draft bankruptcy law under review; drafts of insurance law and related instructions completed • Draft laws for leasing of private and state land approved for submission to Parliament; draft policy on dispute mediation • Achieved on schedule until mid-year; stalled due to reallocation of funds • Negotiations continued with oil companies but there were no commitments to new investments • Administrative systems prepared; applications	• Improved private sector enabling environment (laws passed on bankruptcy, investment, insurance, collateral, leasing/contract; business registration to MoJ) • Laws on land rights/titling; foreign land ownership claims; cadastre; natural resources; agricultural use; pilot land registration • Programmed road maintenance completed and 1,000 jobs created • Voluntary emigrant worker program operationalized

Sector	Output / Indicator and Target	Achievement in TSP II (FY2004)	Actions for TSP III (FY2005)
		received	
Agriculture	• Agricultural policy framework developed • Fisheries regulations; offshore fisheries licensing; community based fisheries management strategy • Pilot initiatives in commercial crops introduction, farm-level processing of agricultural products and community watershed management	• Policy framework approved in first quarter of FY2005 • Fisheries decree law and supporting regulations approved; low capacity in fisheries management • Draft forestry and watershed management policy and strategy; slow progress on industrial crop programs, as feasibility study is needed	• Strategy, and SIP finalized • Offshore fisheries licensing initiated • Irrigated rice economics assessed; irrigation water policy completed; action plan for food crop seed and tuber multiplication

Annex E. List of People Met and Interviewed

Government and Ex-Government Officials

Ms. Emila Peres	Minister of Finance, Ministry of Finance
Mr. Mari Alkatir	former Prime Minister
Mr. Estanislau da Silva	former Prime Minister and former Minister of Agriculture
Ms. Madalena Boavida	former Minister of Finance
Ms. Aicha Bassarewan	former Vice-Minister of Finance
Mr. Rui Maria de Araujo	former Minister of Health and current Special Advisor in the Ministry of Health
Ms. Rosaria de Cortereal	former Minister of Education
Mr. Sebastiao Ximenes	Provedor (Ombudsman)
Mr. Francisco de Carvalho	Inspector General
Mr. Jim Sutton	Advisor to the Inspector General (UNDP)
Mr. Antonio Freitas	Director for the Budget, Ministry of Finance
Mr. Richard Neves	Lead Budget Advisor, Ministry of Finance (AusAid)
Mr. Manuel Lemos	Director, Petroleum Fund
Mr. Virgilio Gutteres	Director, Electricity Authority of Timor-Leste
Mr. Vicente Ximenes	Vice-President, Timor-Leste Business Forum

World Bank and IMF (Dili)

Mr. Tobias Rasmussen	Resident Representative, IMF
Mr. Antonio Franco	Country Manager, WB Office
Mr. Joao Gomes	Operations Officer, WB Office
Ms. Steffi Stallmeister	Operations Officer, WB Office

World Bank (Washington, DC)

Mr. Jerry Lebo	Country Program Coordinator,
Ms. Amanda Green	Consultant
Ms. Helen Sutch	Consultant
Ms. Barbara Nunberg	Sector Manager, EASPR
Mr. Sanjay Dhar	Lead Economist, EASPR
Ms. Rosa Alonso Terme	Senior Public Sector Specialist, EASPR
Ms. Elisabeth Huybens	Lead Country Officer, ECCU4
Ms. Edith Bowles	Consultant, EACSQ
Mr. Adrian Fozzard	Country Manager, LCCHN

Other Donors

Ms. Carol Hannon	Charge d'Affaires and Representative of. Development Cooperation. Representative Office of Ireland
Ms. Cynthia Burton	Counnsellor (Development Cooperation)
Mr. Arve Ofstad	Policy Director, Governance and State Building, NORAD