

INSIGHT

How Timor-Leste Can Increase Private Investment



Changes in Timor-Leste's business policies are expected to help increase private investments. Photo credit: ADB

Timor-Leste can improve its business environment by focusing on investment promotion efforts, strengthening investment facilitation, and using a more problem-driven approach.

Introduction

Stimulating private investment is a key challenge for Timor-Leste. While total investment in the economy has risen sharply since 2007 following a large fiscal stimulus, private investment has not grown significantly and remains low compared with neighboring countries in Southeast Asia and the Pacific.

Improvements in physical infrastructure have made it easier to move people and goods around the country and to access key services such as electricity. However, skills shortages and weaknesses in the business-enabling environment continue to undermine Timor-Leste's attractiveness as an investment destination.

Analysis

Timor-Leste has adopted Strategic Development Plan 2011–2030 that maps out a program of investments in infrastructure, human capital, and institutions to support the development of a sustainable non-oil economy.

However, these long-term efforts will need to be complemented by carefully focused actions to attract

and facilitate new private investment. It needs to focus on investment promotion efforts in areas with clear potential, strengthen investment facilitation, and use a more problem-driven approach when designing reforms to improve the business-enabling environment.

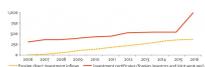
Legal and policy framework for private investment

Timor-Leste has relatively few restrictions on foreign investment and has offered a range of incentives to stimulate investment.

In 2008, corporate and personal tax rates were reduced to 10% from 30%, which compares with an average corporate tax rate of 22.7% in the ASEAN region. Import tariffs were also reduced to 5.1% from 12.4%, which is low when compared to the tariffs applied by some other ASEAN members.

Meanwhile, the 2011 Private Investment Law allowed domestic and foreign investors to apply for an Investment Certificate that would grant additional incentives such as income tax holidays and exemptions from import duties and sales taxes. But an analysis of approvals between 2007 and 2016 showed that many investments were either not completed or did not deliver the expected level of investment, raising questions about the purpose and value addition of the certification process.

Figure 1: Investment Certificates vs. Actual Foreign Direct Investment Inflows in Timor-Leste (\$million, cumulative)



Sources: Central Bank of Timor-Leste; Trade Invest Timor-Leste; ADB staff estimates.

In 2015, a range of reforms were implemented to strengthen investment promotion and facilitation. Timor-Leste's investment promotion agency was restructured, and has led several high-profile initiatives including publication of Timor-Leste's first investment guide and the organization of investor conferences in Dili, Australia, and Singapore.

In 2017, a new private investment law was approved. Under the new law, Investment Certificates have been replaced by a new Declaration of Benefits available for investors in sectors that are seen as a priority for non-oil growth—agriculture, fisheries, forestry, manufacturing, hospitality, and tourism. Investors who successfully apply for a Declaration of Benefits will receive a similar package of benefits as investors who received certificates. This includes income tax holidays of 5–10 years, import duty and service tax exemptions, and a minimum of five work permits for skilled foreign workers.

Strengthening investment promotion

Successful investment promotion relies on effective communication with prospective investors. Timor-Leste has made progress in this area since 2015 and now has a strong foundation to build on. Ensuring that investors can readily access comprehensive information about the legal and regulatory requirements for doing business is a crucial first step. Increasing the breadth and depth of information

available through the investment promotion agency's website is an immediate priority.

Proactive efforts to identify and attract investors can have a large impact if they are realistic and well-targeted. There is strong potential in all priority sectors, but in many cases the underlying policy frameworks and sector plans are still being developed or reviewed.

Promotional efforts should be focused on priority sectors where a clear policy and regulatory framework for private investment is already in place, such as tourism.

Improving investment facilitation

While some investors who received certificates did not complete their investment, there is also an unknown number of prospective investors who did not invest due to actual or perceived difficulties in establishing and operating a business in Timor-Leste.

Improvements in investment facilitation can help address both of these problems by making the process for establishing a new business easier and more transparent. In Timor-Leste's case, there would be significant benefits to adopting a "whole-of-government" approach to investment facilitation.

At the policy level, this would require a high-level commitment to strengthen facilitation with a clear message that all government agencies must help to facilitate legitimate private investments. Regular intergovernmental meetings to review problems as they arise and to check on implementation of agreed follow-up actions would give investors the confidence that problems will be resolved and that they can avoid long delays and unnecessary frustrations.

Implications

Adopting a formal mechanism for whole-of-government investment facilitation would help generate a steady flow of information about the constraints that businesses in Timor-Leste face during establishment and operations. This is especially important in the case of pioneer investors planning to enter a sector that is thought to have broader potential.

Information collected through the facilitation process could be used as input into a more problem-driven approach to designing and implementing reforms to support economic diversification. This could include clarification and streamlining of general regulatory procedures such as taxation, environmental licensing and work permits, and sector specific issues such as licensing. Linking the prioritization of reforms to a steady flow of information about the challenges that businesses face during their establishment and operations would help to ensure that efforts to improve the business enabling environment are well-targeted and would complement the longer-term efforts to improve Timor-Leste's infrastructure, human capital, and institutions.

Resources

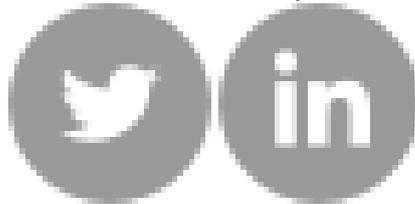
D. Freedman. 2017. Attracting and facilitating private investment in Timor-Leste. Pacific Economic Monitor. July. pp 14–17.



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Last updated: June 2020