

**EAST TIMOR: THE FRAGILE ROAD TO RECOVERY**

**DESKTOP FRAGILE STATES ASSESSMENT REPORT**

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## EXECUTIVE SUMMARY<sup>1</sup>

East Timor has made remarkable strides since its traumatic secession from Indonesia. A constitution has been written and adopted, a president elected, substantial reconstruction has taken place, and unprecedented investment in human capacity has been initiated. Following 25 years of occupation and an armed struggle for independence, East Timor is on the path to recovery with good prospects for becoming a “transformational development” state.

A successful outcome, however, is not assured. East Timor faces numerous obstacles that could derail this recovery and put East Timor at risk of major social and political instability. Many of these challenges have their roots in East Timor’s oppressed past. East Timor is very poor and has little established infrastructure – significantly limiting the resources available to address its many needs. The decades of discrimination under Indonesian rule have severely constrained human capacity affecting the speed and breadth of East Timor’s recovery. As the world’s newest country, East Timor has had to create political, economic, social, legal, and security structures from scratch. These institutions remain weak and vulnerable to manipulation. Simultaneously, they are under great pressure to provide goods and services to the tens of thousands of former independence fighters, militia members, and unemployed youth who are flocking to East Timor’s urban areas. Add to this mix the expectation that substantial oil revenues will soon be flowing to this young country and that UN advisors and security personnel may be phasing out shortly – and the possible scenarios for instability are not hard to imagine.

East Timor’s political leaders enjoy a remarkable degree of legitimacy, owing to the long shared struggle and perception that its leaders, particularly President Xanana Gusmao, have a popular mandate and are genuine representatives of East Timorese society. Consequently, East Timor’s fragility derives almost entirely from its weak effectiveness – the capacity to generate goods and services that benefit the society. This is true in every sector but particularly so in the security realm, where there is little confidence that East Timor’s fledgling army and police units can protect the society from domestic or external threats. Moreover, while the legitimacy of East Timor’s current political leadership is high, democratic processes have yet to be consolidated. Therefore, challenges over political authority still present risks to future instability.

To help address the core vulnerabilities threatening East Timor’s successful recovery, this assessment recommends USAID and the USG consider the following interventions:

- Continue financial commitments to the transition through 2007. USAID and other donors are beginning to phase-down their funding in East Timor. Given the capacity weaknesses East Timor faces across the board – a direct consequence of Indonesia’s policies that denied East Timorese leadership roles for a full generation – scaling back assistance at this time may be premature. Providing

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ongoing support for several additional years will allow more time for the new state to strengthen its capacity, address some of its most acute vulnerabilities from a stronger financial position, and maintain more continuity to East Timor's recovery until its oil revenues come on-line.

- Sponsor nationwide works programs targeting unemployed youth and disgruntled veterans. Aggrieved former fighters and growing legions of unemployed youth provide a ready recruiting pool to the small domestic militias that exist in East Timor. This vulnerability can be lessened by undertaking labor-intensive works programs that take these youth off the streets, put them into a position of making a productive contribution to the development of the country's infrastructure, and provide an opportunity for them to develop certain skills.
- Provide professional training to East Timor's army. Department of Defense-led training to East Timor's small army could strengthen its capacity and professionalism, putting it in a stronger position to confront any would be domestic or external challenges that currently could easily destabilize the country and erase the progress towards recovery that has been made.
- Reaffirm Position on Democratic Succession. The State Department, NSC, and DOD could strengthen prospects for democratic consolidation by clearly signaling to their counterparts in East Timor that continued economic, political, and military support from the United States is contingent on adherence to established procedures of democratic succession. Actors that try to usurp power extra-constitutionally will not be recognized on the global stage.

## **I. WHY IS EAST TIMOR CONSIDERED FRAGILE?**

East Timor does not fit neatly into typical descriptions of vulnerability. It is a highly unified society possessing a common ethnic composition, cultural background, and religious heritage. This unity has been further forged in the fires of the armed independence struggle in which virtually every household took part – and paid substantial personal sacrifices. Over 200,000 East Timorese out of a total population of one million were killed during the 25 year Indonesian occupation. As this conflict was waged against an external enemy and was not a civil war, East Timor does not face the challenge of bringing opposing factions to the table of reconciliation. Rather, in this conflict – the defining event in recent East Timorese history – virtually all of the factions in East Timor were fighting on the same side. The fledgling government in East Timor is also atypical from most fragile states in that it has an astonishingly high degree of support and democratic legitimacy among the general population. Eighty-seven percent voted for President Xanana Gusmao and 76% supported the FRETILIN party in the elections for the constitutional assembly - polls that were internationally administered and deemed free and fair. Both Gusmao and FRETILIN have earned deep reservoirs of legitimacy from their leadership of the independence struggle. For all of these reasons, East Timor is

widely considered to be successfully on the path of recovery and on its way to entering into the transformational development country category.

Despite these very real and positive foundations, East Timor still shows up on the Alert and Tracking radar screen for a number of reasons that bear monitoring. First, East Timor is only five years removed from the end of its armed struggle against Indonesia. Historical experience shows that there is a nearly even probability that a country emerging from war will fall back into conflict within five years – and that rate only diminishes gradually subsequently. Second, East Timor is a very poor country. And, again, historical analysis shows that poor countries are much more susceptible to falling into conflict. This is attributed to a variety of reasons including a weak capacity to fend off insurgents or external aggressors, a myriad of social and economic privations that can be exploited by destabilizing agents, a small middle class that typically serves as a force for stability, and limited resources to forge the broad social compacts that bring competing interests in a society under a common umbrella, among other factors. Third, between militias loosely linked to Indonesia, martial arts groups that provide an organizational structure for some 20,000 youth in what at times amounts to gang behavior, disaffected veterans, and growing youth unemployment there is a ready pool of individuals who could be mobilized to act against the state and its weak security sector. Fourth, East Timor has benefited from the presence of UN peacekeepers since 1999. As these forces and other technical advisors depart (currently scheduled for May 2005), there will be a security and capacity vacuum that will need to be filled. Fifth, East Timor's institutions are still unformulated. Many of the key roles and responsibilities to be played by various branches of government and social actors remain unclear. This ambiguity over the "rules of the game" could undercut East Timor's drive toward stability by allowing legitimate differences among competing political actors to spiral out of control creating major rifts in society. Until systematic codes of behavior and means for addressing differences of opinion are institutionalized in a predictable pattern of rule of law, East Timor's stability is highly dependent on the character, integrity, public-spiritedness, and vision of its current leaders. Any society reliant on the benign intentions of selected individuals, rather than the rule of law and institutionalized checks and balances, is vulnerable. In other words, the absence of established procedures for dealing with political competition provides substantial maneuvering room for political actors who would usurp power through undemocratic means or militia leaders willing to destabilize the society for personal economic profit.

## **II. BACKGROUND: COUNTRY STRUCTURE, INSTITUTIONS, AND RECENT HISTORY**

East Timor became the world's newest country in May 2002. The road it followed to achieve that distinction, however, was a tumultuous one.

East Timor was a Portuguese colony for centuries starting in the early 16<sup>th</sup> century. It was used primarily as a source of raw materials, most prominently – sandalwood and later coffee. Then, suddenly, with a change of government in Portugal in 1974, Portugal took the decision to divest itself of all colonial possessions. Little legal, institutional, or human capacity preparation was made for the post-colonial period. The Portuguese

authorities departed East Timor in August 1975, before a successor Timorese government was in place. Armed conflict among competing factions broke out almost immediately at the cost of several hundred deaths. After a formal declaration of independence by FRETILIN (East Timor's main political party) in November 1975, Indonesia quickly invaded and annexed East Timor as its 27<sup>th</sup> province, despite having had no previous historical claim. Sixty thousand Timorese were killed in the first years of the occupation.

From 1976 to 1999, East Timor was occupied by Indonesia and its armed forces. Indonesian law was applied and language taught in schools. Consistent with its aim of integration, Indonesia invested relatively more than the Portuguese in establishing basic infrastructure in East Timor. Nonetheless, the occupation was met with armed resistance almost from the start. This was led by FALINTIL, the armed wing of FRETILIN. Indonesia employed increasingly severe forms of coercion to bring the Timorese to heel. This included a major outburst of fighting in 1991 that claimed 200,000 lives – one fifth of the entire population. Intent on weakening the intellectual leadership and human capital base to the resistance, the Indonesian authorities prevented the East Timorese from acceding to virtually any leadership positions in government, business, or the academic worlds.

The fall of the Indonesian leader, Soeharto, in 1998 opened the door for the first serious suggestions of East Timor's independence, or at least autonomy, within Indonesia. His (also unelected) successor, Dr. Habibie, calculated that the cost of negative international public opinion resulting from the East Timor occupation was undercutting Indonesian relations with the West and, in particular, Indonesia's access to international capital it so sorely needed following the financial implosion of 1998/1999. A referendum on independence was thus allowed.

To assist the holding of the referendum, UNAMET (United Nations Assistance Mission for East Timor) was established. UNAMET's purpose was to facilitate the vote and also to foster reconciliation between pro-integration and pro-independence movements. On September 4, 1999, 78.5% of East Timorese voted for independence from Indonesia.

Organized violence by the pro-integration militias began shortly after the referendum outcome resulting in massacres of the civilian population, destruction of homes and buildings and large displacements of the population to the interior. Nearly 75% of all physical infrastructure in East Timor was destroyed by these militias. Hundreds of thousands were also forcibly deported to West Timor.

It was later learned that the Indonesian army organized pro-integration militias in anticipation of the referendum. These militias were centrally planned by the Indonesian *Kopassos* (Special Forces Command) and meant to resemble a spontaneous pro-integration movement. Small-scale militia operations such as village raids, arrests, murders had also been conducted in the year leading up to the referendum to intimidate the Timorese population.

An international military intervention was quickly assembled to end the violence. On September 20<sup>th</sup>, an Australian-led force called InterFET arrived and began to establish order in the capital. Indonesia abandoned its claim to East Timor in October after annulling its 1976 annexation of the territory in recognition of the referendum results. The United Nations Transitional Administration in East Timor (UNTAET) was established shortly thereafter to provide peacekeeping services and aid in the transition to local rule.<sup>2</sup> Elections took place in May 2002 and East Timor officially became an independent nation. With that, the U.N. mission evolved into UNMISSET (United Nations Mission of Support in East Timor).

UNMISSET remains in place today. Its primary purpose is to provide some form of provisional institutional architecture to the new state until which time the East Timorese government and institutions develop sufficient capacity to take on the day to day functions of governance and security. UNMISSET was recently extended for another six months (until May, 2005). As in other newly independent states the task in establishing these institutions from scratch is enormous.<sup>3</sup> This objective is further undermined by the widespread lack of capacity, leadership, and governance experience among East Timorese – a direct result of the Indonesian occupation. For example few local Timorese have expertise in the fields of law, accounting, and auditing. Consequently, key bureaucratic positions are going unfilled in the government. In the judicial sector specifically, East Timor requires the services of international judges to fill benches in district courts. A criminal code is still in the process of being drafted, which requires the expertise of UNMISSET advisors. This has been complicated over basic questions such as whether Indonesian or Portuguese civil and criminal law applies.

### **Structural Characteristics**

East Timor's population is estimated to be roughly 1 million. Population growth rate is estimated at 2.4 – 2.6 per cent with 42% of the population under the age of 14. Major concentrations of the population are in Dili, the capital, and the province of Baucau.

The urbanization of East Timor (and in particular Dili) will pose a challenge to the government. An official census taken in July 2004 showed a 40% increase in Dili's population from three years ago. The government will need to expand social and health services to keep up with the capital's rapidly expanding population.<sup>4</sup>

East Timor is ethnically homogenous with little in the way of Islamic or Hindi influences that predominate across the islands of Indonesia. There are still 30 distinct ethno-linguistic groups dominated by two language families – Austronesian and Papuan.<sup>5</sup> Tetum and Indonesian are the most commonly spoken languages although Portuguese is

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<sup>2</sup> Dunn, pgs 303-365

<sup>3</sup> For details see, "Progress Report of the Secretary General on UNMISSET" Nov. 9, 2004. (Report – S/2004/888)

<sup>4</sup> "Progress Report of the Secretary General on UNMISSET" Nov. 9, 2004. (Report – S/2004/888).

<sup>5</sup> Dunn, pg. 3

an official language. Portuguese is also required for senior civil service posts. Christianity is the major religion although animistic beliefs and rituals are still pervasive.

A strong national identity appears to have formed due to the Portuguese colonization and the subsequent occupation by Indonesia. Other unifying factors include Catholicism being the only major religion, the institution of the Catholic Church which serves as a forum for social organization and was a leading voice for independence, and shared resentment against Chinese merchants who have monopolized trade in the area for hundreds of years. Tension between the two communities, however, is low-key mainly due to extensive intermarriage.<sup>6</sup>

East Timor's GDP stood at \$402 million in 2003. Per capita income is approximately \$520 dollars which is substantial lower than other East Asian/Pacific island nations (\$1,267).<sup>7</sup> The official domestic currency is the US dollar.

Disparities in income between urban dwellers and those in rural areas are significant. Using the national poverty standard of \$.55 of income/day, 41% of East Timorese are in poverty. A higher proportion of the poor reside in rural areas than urban: 46% to 26%, respectively. Dili, the capital, claims the lowest poverty rate of 14% in the country.<sup>8</sup>

East Timor's economy is agriculturally based with substantial reliance on subsistence farming. Agriculture accounts for 25% of GDP with 75% of the labor force employed in this sector.<sup>9</sup> Drought is a serious concern as East Timor has distinct dry (May to October) and rainy (November to April) seasons.<sup>10</sup> Negative economic growth in 2003 was in part to blame on an extensive drought.<sup>11</sup> East Timor receives 1,200-1,500 mm of rain annually compared to 2,500-3,000 mm in surrounding islands.<sup>12</sup> Famines are not uncommon with one occurring as recently as 1997.<sup>13</sup>

Coffee is the main export. Coffee accounted for ¾ of total exports in 2002 and employs 25% of the population. The sector is racked with inefficiency, neglect, poor processing and generally poor infrastructure such as roads to growing regions. There is little organization among growers who are mainly individual farmers. The global slump in coffee prices is also negatively affecting this sector.<sup>14</sup> There is substantial potential for high value exports in the form of high grade, organic coffee if some of the production and processing issues can be addressed, however.

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<sup>6</sup> USAID, Office of Conflict Management and Mitigation. "Conflict Assessment: East Timor." May 15<sup>th</sup>, 2004.

<sup>7</sup> IMF Appendix, pg. 3

<sup>8</sup> "East Timor Human Development Report, 2002." pg. 16-19.

<sup>9</sup> CIA World Fact Book

<sup>10</sup> Dunn ,pg. 2

<sup>11</sup> CIA World Fact Book

<sup>12</sup> "Social..." Pg. 13

<sup>13</sup> "Social..." Pg. 25

<sup>14</sup> Oxfam report,

Manufacturing is weak and constitutes a small share of the economy. Mining and manufacturing together account for 3% of GDP. Lack of skilled labor, proper transportation networks, and lack of capital are major obstacles. Manufacturing growth currently comes from low-skilled processing of coffee and sandalwood.

The major issue on the economic horizon for East Timor, however, is its prospects for gaining oil revenues. It is not possible to quantify exactly how much revenue East Timor can expect from its oil and gas reserves, which lie offshore in an area of the sea that is claimed by both East Timor and Australia. The reserve is potentially worth several billion dollars over the next 20-30 years.<sup>15</sup> Even the most conservative estimates place annual revenue at well over \$100 million for an extended period of time. It has been estimated that expected revenues, even with conservative projections, would be enough to cover most public expenditure and permit savings. This would assure a sizeable revenue flow on an ongoing basis. In summary, it seems likely that East Timor will be able to rely on a significant resource base to finance its development needs well into the future, if the resources are well managed.<sup>16</sup>

The downside of the expected oil windfalls is the “oil curse” phenomenon that has befallen many developing countries that gain access to sizeable resource before they democratize and develop sound accountability structures. These benefits are all too easily captured by a few well-connected interests, thus facilitating a monopolization of economic and political power that is very difficult to displace. These countries have a sordid history of underdevelopment, autocracy, and corruption. The prospect of oil revenues, therefore, poses another set of challenges to efforts to promote development and stability in East Timor. The large parliamentary majority of FRETILIN, the judiciary’s lack of experience, the Ombudsman’s lack of independence, and the very limited experience of the population with freedom of expression are all factors that could enable the mismanagement of these potentially valuable energy resources.

On the positive side, East Timor has probably had more public discussion of the oil and gas issue than most countries at a similar level of development. The president has taken an active interest in the matter, as have NGOs and other elements of civil society. The World Bank and certain bilaterals have been actively working with the government to set up an oil trust fund based on the Norwegian model. A further positive factor is that the resource flow is expected to attain a large volume only a couple of years after independence, allowing some time for the government and the international community to establish mechanisms to manage these resources transparently and effectively so as to generate the public goods and services that would benefit all citizens.<sup>17</sup>

### **Institutional Arrangements**

As could be expected for a state that has only been in existence for two years, East Timor’s institutions are weak and fragmentary. The political system is a parliamentary

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<sup>15</sup> “Social and Economic Conditions in East Timor” pg. 13

<sup>16</sup> Yahoo Finance: summary of East Timor

<sup>17</sup> OECD development paper : PPP in development: three applications in East Timor

democracy. There are three branches of government: executive, legislative and judicial. A popularly elected President serves as Head of State. The prime minister performs the function of Head of Government. The prime minister is elected as part of a parliamentary majority, separate from the President.

The constitution, which was created by the Constituent Assembly in 2002 before presidential elections were held, is loosely based on the 1975 Portuguese constitution. Changes to the constitution can only be made with consent of 2/3 of the Parliament. Provisions built into the constitution include universal suffrage for all adult citizens, a politically neutral army and protection of free speech. The legislature is unicameral with 88 members. Thirteen are elected in single seat constituencies and 75 by proportional representation.<sup>18</sup>

The constitution grants executive power to the prime minister and his cabinet. Under the parliamentary system the leader of the majority party becomes prime minister, and head of government. The role of the president is seen as largely symbolic, though he holds some significant powers. The President is head of state, supreme commander of the Defense Forces, he can veto any statute for up to 90 days after its passage, he can request the Supreme Court to review the constitutionality of government rules, and he can put relevant issues up to referendum.

On paper this arrangement, as in many European countries, allows for a considerable measure of checks and balances that hold political leaders accountable. However, in an immature system like East Timor without previous democratic precedents, some have expressed concern that this political structure is highly vulnerable to the monopolization of power. The prime minister effectively controls two branches of government from the start. Plus with a very weak judiciary sector (which is dependent on the parliament for funding), it is not clear whether adequate mechanisms of shared power have been established. The system has worked relatively well, thus far, largely due to the forceful personality, charisma, and clear popular mandate of President Gusmao. It remains to be seen whether a future president would maintain the same influence. Similarly, it is unclear to what extent constitutional provisions and restrictions will be enforced, in practice. In other words, East Timor's political leaders must still establish the norms demonstrate a commitment to the letter and spirit of the constitution and its attempts to create certain checks and balances in the administration of political power.

The current president is Xanana Gusmao. He was elected in 2002 with 82.7% of the vote. The President serves five year terms.<sup>19</sup> Gusmao is considered to be centrist, politically. During much of the occupation by Indonesia, Gusmao was the leader of the main resistance group, the FALINTIL. Gusmao was captured in the early 1990s and jailed for most of the decade, though he remained leader of the resistance struggle from his cell.

The current Prime Minister, Mari Alkatiri, was elected as part of the constitutional assembly (later to become the parliament) in 2001. Mr. Alkatiri is a Marxist by most

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<sup>18</sup> Political Overview, East Timor Review

<sup>19</sup> Political Overview, East Timor Review

accounts. He emerged as FRETILIN's leader in exile during the occupation. Since he was abroad during much of the struggle for independence, some question his claim to represent the Timorese people.<sup>20</sup>

The current government is considered to be highly legitimate in the eyes of the general population. President Gusmao is popular due to his role as resistance leader as is the Prime Minister and the FRETILIN, although opposition from various groups exists. The population is optimistic about self-rule and willing to give the current government an opportunity to prove itself. This opportunity will not last indefinitely though. The government must quickly address the economic needs of ex-combatants, youth, and the rural poor. In certain instances, frustrations felt by such groups have resulted in rioting.<sup>21</sup>

While FRETILIN is by far the dominant political force in Timorese politics, there are a number of other active political parties that have gained seats in parliament and who have some public support. The Council for the Defense of the Democratic Republic of Timor-Leste (CPD-RDTL) claims to have over 6,000 supporters, mainly in the Baucau and Dili areas. The CPD-RDTL believes that East Timor has been independent since the 1975 declaration and promotes the view that Timorese should adopt the symbols and substance of the pre-occupation government. Consequently, the CPD-RDTL has so far refused to register as a political party and does not accept the legitimacy of the FRETILIN-led government and the U.N. missions. The group has roots in the early FRETILIN movement but split off due to conflict over its restructuring in the 1980s. Thus, CPD-RDTL calls itself "the real FRETILIN." It is not certain what CPD-RDTL's goals are beyond simply promoting awareness of East Timor's past. Given their dislike for the current FRETILIN leadership, it remains to be seen if they would support a government led by other political parties. CPD-RDTL demonstrations have, at times turned violent in the past.<sup>22</sup>

Colimau 2000, Sagrada Famili and Osnaco are additional political groups opposing the government. Membership in each is estimated to be small, only a few hundred in each at most. They primarily attract former resistance fighters and unemployed youth not accommodated by the new government. Sagrada Famili, moreover, is a quasi-religious group mixing local animist beliefs with Catholicism. Unsubstantiated reports have surfaced that Colimau has made plans in concert with militias based in Indonesian West Timor to destabilize the country after U.N. peacekeepers have withdrawn.<sup>23</sup>

Reflective of the incomplete and at times inchoate process of establishing governance institutions, the selection process and authority of local governments are still being established. As of a July 31, 2004 deadline approximately 400,000 people had registered to vote in local elections. Currently, the plan is to conduct phased elections throughout

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<sup>20</sup> Shoesmith. "Divided Leadership in a Semi-Presidential System." *Asian Survey*, 43:2 pp/231-252

<sup>21</sup> USAID, Office of Conflict Management and Mitigation. "Conflict Assessment: East Timor." May 15<sup>th</sup>, 2004.

<sup>22</sup> USAID, Office of Conflict Management and Mitigation. "Conflict Assessment: East Timor." May 15<sup>th</sup>, 2004.

<sup>23</sup> See USAID Conflict Assessment

the country starting no later than July 2005. The independent National Electoral Commission is still in the process of determining an electoral calendar and procedures for polling and counting of votes.<sup>24</sup>

### **III. PERFORMANCE: KEY DEVELOPMENT AND POLITICAL OUTCOMES**

#### **Relative socioeconomic performance**

East Timor is a poor country. With gross national income of \$402 million and annual per capita income of \$520, it is in the lowest 10 percent of countries around the world. Some 41% of the population falls below the national poverty line. The adult illiteracy rate is estimated at 57%.<sup>25</sup> With such a large percentage of the population falling under the poverty line, issues of disparity are less dominant. To the extent they arise disparities between rural and urban populations are most sensitive. Whereas 75% of East Timor's residents live in rural areas, they comprise six out of seven of the country's poor.

Much of East Timor's development efforts have been focused on rebuilding infrastructure destroyed when the Indonesian military and militias withdrew. This includes water projects, roads, and loans to local cooperatives to rehabilitate the infrastructure needed for cash crops. Therefore, despite its difficult starting point, East Timor has realized significant progress in recent years. For example, it is estimated that pro-Indonesian militia burned down about 95% of East Timor's schools and 80% of secondary school teachers, returned to Indonesia.<sup>26</sup> Yet, within about 18 months after the destruction, the school system, by and large, was rebuilt. This was accompanied by a major infusion of international assistance and a dramatic increase in enrollment by the poor, girls, and rural children. This has resulted in narrowing the gap in school participation rates between the richest and the poorest quintile, boys and girls, and urban and rural areas. The primary school enrollment ratio has increased to 113% for both males and females since 2001. The literacy rate for people age 15 and above has also increased from 26% (female) and 45% (male) in 1990 to 43% for both males and females in 2000-2004<sup>27</sup>. Increased participation was fostered by the reduction of certain costs such as the abolition of school fees, PTA contributions and requirements for uniforms.

Similarly, infant mortality has declined from 110 per 1,000 live births in 1990 to 89 per 1,000 live births in 2002, cereal yields have increased, and the prevalence of underweight children (under age 5) has reduced from 51% in 1990 to 43% in 2002.<sup>28</sup> This is associated with increased government expenditures in the health and education sectors since independence.

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<sup>24</sup> "Progress Report of the Secretary-General on the UNMISET." Submitted November 9, 2004 (S/2004/888)

<sup>25</sup> World Bank (2003); *The Democratic Republic of Timor Leste, Public Expenditure Review*, World Bank, July 2004.

<sup>26</sup> World bank report: Timor-Leste Education: The way forward

<sup>27</sup> ADB Key Indicators

<sup>28</sup> ADB Key Indicators 2004

Given the almost total lack of regulatory oversight (no banks, postal services, police or judiciary were yet in place when these initial activities were undertaken), there were remarkably few cases of misappropriation. Evidently, peer pressure played a key role in ensuring that the available resources were put to good use.<sup>29</sup> Management of the social sector has been improved by decentralizing oversight of front-line personnel, such as teachers and nurses, to local community councils rather than to the central ministry. The local community could then decide how many teachers or nurses to employ and how much to pay them, with the central ministry providing quality control in the form of training and accreditation of personnel, the setting of core syllabus requirements, and the provision of text books. With local communities having a direct stake in managing the local school budgets, there are also incentives for these populations to contribute more cash, in-kind and labor to the schools, further enhancing cost efficiencies.

The improvement in East Timor's social sectors has gone hand in hand with sound macroeconomic policies – pursued by both the government and UNIMET. With the adoption of the dollar, inflation dropped to 3% from 140% in 1999. Timely, relatively generous, and grants-oriented assistance from bilateral and multilateral donors during the first three years of independence has allowed East Timor to make major inroads on its infrastructural and development challenges without falling deep into debt. This is consistent with the government's "no loans policy" – i.e. the determination of top officials to avoid the debt trap faced by so many developing countries.<sup>30</sup> Institutionally, a nascent banking system is growing stronger and is now comprised of the monetary authority, three foreign commercial banks and a microfinance institution.

East Timor currently has virtually no manufacturing sector. It earns hard currency through its natural resources exports particularly coffee, sandalwood, and marble. Coffee in particular has long been and continues to be a highly valuable commodity for East Timorese society. Some 40,000 families derive a significant proportion of their income from coffee.<sup>31</sup>

### **Level of International Engagement**

East Timor is highly engaged with the broader international community for a country of its size and location. Indeed, East Timor's very existence is a result, to a large part, of the engagement of the United Nations in hosting the referendum on independence, the subsequent Australian-led military intervention after the Indonesia military rejected the results, and the UNIMAET mission that has helped provide basic governmental services, technical advice, security, and financial resources during the difficult transition period as the new government in Dili establishes itself.

This extensive international engagement is reflected in the trade arena. Recognizing that a small country with a limited domestic market and a comparative advantage in its primary and agricultural commodities will be dependent on trade to grow, the new

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<sup>29</sup> OECD development paper : PPP in development: three applications in East Timor

<sup>30</sup> ADI Watch: Holding onto East Timor's Debt Free Start!

<sup>31</sup> Client change in Timor Leste: Science, Impacts, Policy and planning

government has adopted a very supportive regulatory environment for importing merchandise from other countries. It does not have quantitative restrictions on imports. With the exception of selected items (e.g. cigarettes and alcohol with certain limits), a uniform ad-valorem tariff (6 percent) is levied on all imports.<sup>32</sup> Currently, there are no repatriation requirements, no financing requirements, no documentation requirements and no export licenses needed. In addition, the country does not levy taxes on exporting goods. Since independence East Timor's dependence on imports has decreased while the level of its exports has been increasing. The trade deficit shrunk from \$249.4M in 2001 to \$79.3M in 2003.<sup>33</sup>

East Timor currently is not yet a member of the WTO or any other trading bloc. However, the country is in the early stages of the process to become a member of the Association of Southeast Asian Nations (ASEAN). Meanwhile, it is also garnering support from the international community to join the ASEAN Regional Forum (ARF)<sup>34</sup>. East Timor joined the IMF and the World Bank Group on July 23, 2002. Both the IMF and the World Bank have been channeling aid in the form of grants to East Timor to allow the small nation to establish itself without a suffocating debt burden.<sup>35</sup> Resource flows from all sources to East Timor have been increasing dramatically since its independence in 1999 – averaging some \$350 million in recent years.

Given the variety, beauty, and breadth of its unspoiled natural environment, East Timor also has considerable potential to attract international visitors through tourism. This sector also could be a valuable source of employment for the local population. The coastal zone, in particular, remains remarkably untouched. If used in a non-destructive, well-planned and sustainable manner, this ecosystem could provide promising possibilities for economic development, while simultaneously offering sustainability to the coastal population.<sup>36</sup> From the standpoint of fragility, this potential offers another important incentive for East Timor to build and maintain good relations with its neighbors and the international community at large.

### **Protection of civil liberties and access to political rights**

East Timor's constitution provides for freedom of speech and of the press - protections the government generally respects in practice. There are two daily newspapers, two weeklies, and several bulletin newspapers that appear sporadically. Their editorials freely criticize the government and other political entities. There are no legal or administrative restrictions on Internet access. Similarly, there are no prohibitions against the freedom of assembly. As referenced earlier, there are a number of opposition political parties. Universal suffrage has been established as the norm, and as evidenced by the high turnouts in the country's first elections, citizens have exercised this right.

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<sup>32</sup> IMF country statistics

<sup>33</sup> East Timor Review 2004

<sup>34</sup> China Daily news: "East Timor eyes ARF membership"

<sup>35</sup> Global Policy Forum: East Timor joins IMF and World Bank

<sup>36</sup> Yahoo Finance: summary of East Timor

However, as with other still evolving institutions in East Timor, the reality of protecting basic civil liberties is, in fact, much more ad-hoc. This reflects the lack of experience with these elementary democratic principles and the wide spectrum of legal interpretations possible under East Timor's current legal system. East Timor is using the Indonesian Criminal Code it inherited from Soeharto-era Indonesia but its media laws are a complex mix of Indonesian, United Nations, Timorese, international human rights, and Portuguese laws.<sup>37 38</sup> This has resulted in a few instances when government officials have attempted to interfere with the press. For example, in August, a senior government official requested in writing that journalists working for the public broadcasting service be disciplined or criminally prosecuted because of their coverage of the eviction of a popular opposition leader. The Indonesian law's libel fines, in particular, have come under criticism after a controversial decision last year by the Dili District Court to impose a potentially bankrupting fine of \$50,000 on one of the country's two daily newspapers after finding it guilty of defaming an Indonesian businessman. There are also concerns about portions of the Indonesian law that allows journalists to be jailed for critical reporting of government officials and other forms of dissent.

President Xanana Gusmao has denounced the anti-free speech articles in his country's criminal laws that could be used to jail his critics. For example, the law currently states that jail terms of up to five years can be imposed for insulting the President and up to seven years jail for expressing contempt of the government. Citing East Timor's constitution, which directs courts not to use still-applicable Indonesian laws if they are against fundamental human rights, he has requested that these articles not be applied until formal amendments can be made.

Internews is one of USAID's implementing partners in East Timor in this respect. USAID supports its efforts to enhance the skills of journalists, improve the sustainability of media outlets, and encourage public debate on key issues related to legislation and justice.

In sum, while East Timor remains a very poor country, considerable gains have been realized over just a few year time period. Living conditions are improving under the new government as are access to basic goods and services. The economy has also enjoyed a sizeable post-conflict boom and considerable resource inflows from the international community as part of the UN-led rehabilitation effort. Recognizing this, all of East Timor's institutions remain weak and at a formative stage indicating that they may yet evolve in any number of directions. The success of East Timor's post-conflict recovery/nation-building effort, while hopeful, remains far from assured.

#### **IV. ANALYSIS OF THE POLITICAL ECONOMY RELATIONSHIPS ACROSS SECTORAL DIMENSIONS**

As can be seen from Section 3, nearly all of East Timor's economic and social development indicators rank near the bottom of global rankings. However, these sub-par outcomes are almost entirely a reflection of East Timor's tumultuous start. The trends

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<sup>37</sup> USAID program archive <http://www.usaideasttimor.net/DGHighlightsArchives/DGArchive13.htm>

<sup>38</sup> US Department of State <http://www.state.gov/g/drl/rls/hrrpt/2003/27769.htm>

since then are positive – conditions are getting better. Some of this is attributed to the predictable post-conflict “bounce” as conditions return to normal and investment that had been delayed is resumed. However, the degree to which the leading politicians and civil society leaders have been willing to cooperate to make progress on their shared vision of a more prosperous, just, and stable East Timor should also be recognized. Whether or not the momentum behind this positive recent trend can be maintained and accelerated remains to be seen. Much will depend on how well the country can systematize norms for transparency, public spiritedness, and tolerance for dissent in its emerging political and social institutions.

While East Timor’s poverty and weak, nascent institutions make its road to recovery more difficult, the degree to which the respective institutional sectors pose risks to East Timor’s stability varies greatly. Weaknesses in the political and security dimensions appear to pose relatively more serious threats than the widespread, though generally equitably shared, poverty burdens.

### **Political Sector**

East Timor has benefited greatly from the integrity, vision, and high-mindedness of its political leaders, especially Xanana Gusmao. Much as Nelson Mandela did for South Africa, his actions and words have had a profound influence on setting the course for the early norms and attitudes of the new nation. His criticism of deleterious outdated laws as well as his protection for the independent media and political opposition has also served as an indispensable check on potential abuses or temptations to usurp power by other government actors. His contribution is hard to overestimate – it has done much to put East Timor on the trajectory of virtuous cycle of transparency, rule of law, tolerance for dissent, and improved living conditions.

The indispensable role that President Gusmao has played in East Timor’s recovery highlights the importance of current and future tensions between the president and prime minister’s offices for East Timor’s continued advancement. The current relationship between President Gusmao, age 57, and Prime Minister Alkatiri, age 54, is shaped by their shared history. Before the occupation, both men were party members of FRETILIN. In 1977, FRETILIN made an ideological shift to Marxism-Leninism. While Alkatiri was already a proponent of Marxist views before the shift Gusmao never accepted the radical ideology of class struggle and instead believed in a resistance struggle for all Timorese people, regardless of class. Gusmao officially split from FRETILIN in 1987, making FALINTIL, the armed wing of FRETILIN that he led, an independent party. Its goal was to be an instrument for the freedom of all Timorese people. The tensions that exist today between the two leaders can be traced to this 1987 split and the sharp ideological differences it reflects.

While a number of political parties are currently active in East Timor, given the current and long dominance of FRETILIN (it holds 55 seats in the 84 member parliament), there remain doubts over whether FRETILIN will accede to an opposition government if one is elected. Alkatiri and FRETILIN view themselves as the true and only representatives of

East Timor since they led the political struggle against Indonesia. Many opposition politicians thus question whether Prime Minister Alkatiri is committed to inclusion and the idea of a multi-party political system. He maintains very tight, hierarchal control over FRETILIN, which is not operated according to democratic procedures. Moreover, he has challenged the Supreme Courts right to rule on the legality of certain measures passed by parliament. This raises the prospect, among some observers, that FRETILIN could attempt to engineer a *de facto* one-party system – with the slippery slope of reduced checks and balances, policy dialogue, incentives for cooperation, and responsiveness to the public this entails.

President Gusmao has attempted to ensure adequate representation by the opposition by accepting the nomination of nine opposition parties in the run-up to the forthcoming elections. He has also promised to promote an agenda of inclusiveness and reconciliation. He has reached out to the main opposition group, the CPD-RDTL, to start a dialogue about their concerns. He also established several commissions to recognize the role played by veterans in the resistance and to address their economic grievances. Outside observers view President Gusmao as possessing broad-based appeal among all segments of the Timorese people and an effective counter-balance to FRETILIN.<sup>39</sup>

The relationship between these two political actors is complex and fluid – and analyzing this and the motivations that lie beneath each individual and party is beyond the scope of this desktop assessment. However, this analysis does highlight the critical importance the current president plays in counterbalancing the prime minister. This president’s influence, moreover, is largely a reflections of his personal history and charisma – not necessarily a reflection of the office. Should this balance be lost, whether through political maneuvering or the passing from the scene of one of the main protagonists, it could have dramatic implications for East Timor’s continued progress and stability overall. To be clear, this is not an indictment of parliamentary systems. There is ample experience, particularly in Europe, of parliamentary systems enacting adequate checks and balances. However, in a nascent system where the head of government is the leader of a dominant political party, the judiciary is weak, and there is a lack of democratic precedents – the risks of a one party system evolving under the guise of a democratic shell needs to be considered.

## **Security Sector**

On the whole, East Timor’s security services are weak and immature. On paper, the security sector is under civilian control. UNTAET setup a National Security Council to provide civilian oversight and coordination among the various security sector agencies. There is also a Defense Secretary and the President is Commander-in-Chief.

The military (the East Timor Defense Force or F-FDTL) is comprised of only 1,500 personnel – a total of two battalions. There are plans for an additional reserve force of two battalions but resources are short. The F-FDTL is composed mainly of former resistance fighters from the FALINTIL. The first battalion was formed entirely of ex-

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<sup>39</sup> Shoesmith. “Divided Leadership in a Semi-Presidential System.” *Asian Survey*, 43:2 pp/231-252

FALINTIL soldiers and officers chosen by the FALINTIL High Command mostly on the basis of their loyalty to President Gusmao. Recruitment for the second battalion was limited to only 18-21 year olds. The selection process was administered by Brig. General Ruak, a Gusmao loyalist. Ruak was thus able to exclude those (including former FALINTIL fighters) whose loyalty to Gusmao was in question.

The selection process of F-FDTL personnel has invoked claims of ethnic basis. A majority of first battalion personnel are from eastern districts – collectively called “Firaku”. Personnel from the western, “Kaladi” districts are largely absent from the military. The military is thus identified with the president and one ethnic group rather than the government in general.<sup>40</sup>

Some observers believe that the issue of ethnicity in the security forces may be overblown. However, rather than there being outright ethnic bias, the selection process for F-FDTL personnel favored the Firaku districts by default as it was the eastern Firaku districts that bore the greater part of the resistance struggle. Consequently, the composition of the FALINTIL ranks favored the Firaku.<sup>41</sup>

The overall capacity of the F-FDTL remains limited by a lack of professionalism, appropriate training regimes, and a limited logistics capability. Despite these limitations, the F-FDTL will conduct training for its next batch of recruits entirely on its own with UNMISSET advisors serving a limited role.<sup>42</sup>

Specialized training of the F-FDTL in the fields of military policing, engineering, operational staff work, logistic and intelligence gathering by UNMISSET will continue through May 2005. It is hoped that this will make the F-FDTL more competent and effective when the UNMISSET mandate ends.<sup>43</sup>

The Timor-Leste Police Service (TLPS), which includes the regular police, the Border Police Unit, and the Rapid Deployment Service, is a national police force with 3,000 officers. A Special Police Unit that will employ heavier weapons is currently being fielded.

Training the police forces has taken on a higher priority as they have earned a reputation of being heavy-handed and mishandling situations. Human rights abuses have been recorded as has corruption in the ranks.<sup>44</sup> Lack of leadership is a primary source of these problems.<sup>45</sup> The political selection process of police recruits also appears to be another issue of concern. Rogerio Lobato, the Minister of Internal Administration, has attempted to gain the support of disaffected veterans by promising them jobs in the TLPS. By wooing these veterans, Lobato is building a counterweight to FALINTIL in the F-FDTL

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<sup>40</sup> Shoesmith. “Divided Leadership in a Semi-Presidential System.” *Asian Survey*, 43:2 pp/231-252

<sup>41</sup> King “East Timor’s Founding Elections and Emerging Party System.” *Asian Survey*. 43:5, pp. 745-757

<sup>42</sup> “Progress Report of the Secretary General on UNMISSET” Nov. 9, 2004. (Report – S/2004/888)

<sup>43</sup> *ibid*

<sup>44</sup> USAID, Office of Conflict Management and Mitigation. “Conflict Assessment: East Timor.” May 15<sup>th</sup>, 2004.

<sup>45</sup> *Janes Defence Weekly*. 2003. Vol.39, Iss.10, Pg. 47.

who are loyal to President Gusmao. Observers also cite Lobato as building a power base for himself to challenge Prime Minister Alkatiri.

Paulo Martins, the police commissioner, has rejected the attempts by Minister Lobato to appoint these disaffected FALINTIL veterans to positions in the TPLS. Martins has been adamant in defending the recruitment process based on qualifications and merit instead of political allegiance. Violence surrounding this issue is not uncommon including a major riot in Dili on December 4, 2002. Rioters, consisting of unemployed veterans angry at not being recruited by the TLPS, systematically attacked the Prime Minister's home, President Gusmao, and various other buildings.<sup>46</sup>

Tension also exists between the TLPS and F-FDTL themselves (aside from the issue of FALINTIL veterans), resulting in at least one confrontation involving firearms in Lospalos. Legislation has not specifically outlined the roles and responsibilities of the two forces thus creating confusion. There is also jealousy as the police forces are receiving training via a joint Australian/United Kingdom program. The military is not receiving the same type of extensive international training.

The adoption of a penal and criminal procedures code will help to outline the role of the police and more importantly provide them with a basis for discipline and self-control. Advisors with UNMISSET are currently working on this legislation with members of parliament. This is, in part, an effort to compensate for a perception that UNTAET did not sufficiently emphasize the indispensability of transparency and civilian control in its initial training curriculum for the security sector.<sup>47</sup> The ultimate goal for UNMISSET is to transform TPLS into a professional, non-political police service.<sup>48</sup>

The potential threats to internal security presented by the pro-integrationist and Indonesian sponsored militia groups, growing popularity of martial arts organizations/gangs, an expanding pool of urbanized unemployed young men, and reports of growing common crime highlight the challenges faced by East Timor's young security institutions. Given the country's small size and limited resource base to support the security sector, even a relatively minor organized resistance could have a destabilizing effect.

In sum, there is little confidence that the East Timorese police and military are capable of providing domestic security or protection from external forces at this time. It is also open to debate whether the police and military are being exploited for political purposes or being positioned to become professional services. Both the president and prime minister have issued public statements disavowing the use of either force for political gain. Nonetheless, that this is even an issue, reflects the weaknesses of the security institutions – and broader political fragility – in East Timor at this stage of its recovery.

## **Economic Sector**

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<sup>46</sup> See *Shoesmith*

<sup>47</sup> DCAF. "Security Sector Governance Status Report and Needs Assessment on Timor Leste." Sept. 2003

<sup>48</sup> "Progress Report of the Secretary General on UNMISSET" Nov. 9, 2004. (Report – S/2004/888)

As discussed in section three, East Timor is a poor country that is making considerable advances since independence. The lack of available resources is a serious constraint to addressing the pressing socio-economic and capacity-building priorities it faces. However, tensions created by the internal competition for resources are not a major threat to the country's stability. Household income distribution is not terribly skewed, even though there are notable rural/urban distinctions. Nor is there a clear, patronage-based network that controls access to economic opportunities and advancement. While there have been allegations of corruption, collusion, and nepotism within the Alkatiri administration,<sup>49</sup> all in all, the economic grievance underlying instability in other fragile state contexts are not as evident in East Timor.

East Timor's history of colonialism and occupation meant that expatriates normally filled practically all positions of responsibility, higher remuneration, or economic opportunity. The new nation thus faces a very serious shortage of experienced middle and upper-level managers in both the public and the private sectors. The problem in the public sector, though significant, is being met in a more organized manner through the efforts of the UN transitional administration and the seconding of technical staff by donor countries and multilateral agencies. The shortage of private sector management and especially entrepreneurial skills and experience is potentially a much more serious obstacle in East Timor's quest for economic independence. As a sign of this, salaries and skill levels are higher in the public than private sectors.

The government formally recognizes the importance of entrepreneurial activity in a market economy but it has yet to provide an appropriate economic and legal foundation to enable this to flourish. Property rights are not well defined. Competing claims arising from Portuguese- and Indonesian-era titles must be reconciled with customary law, resulting in considerable uncertainty over ownership. This makes land nearly impossible to use as collateral in support of credit activities. This ambiguity and the fact that only nationals may own land is a major impediment to international investment. Contract enforcement is complicated by the inexperience of the judiciary and the ambiguities of legislation in the nascent legal system. Services such as insurance, leasing, accounting and management consulting are virtually non-existent. The establishment of microfinance institutions was delayed by legal and administrative problems and is only now initiating activity. New entrepreneurs are further limited by the virtual non-availability of credit facilities.

Meanwhile, the country is young both politically and demographically and the heavy investment being directed to education will soon be generating large numbers of better-educated youths looking for jobs. The public sector will absorb only a small fraction of school-leavers and graduates, making it essential that the private sector grow rapidly to absorb the remainder. But the private sector is largely informal and poorly developed, with very few large-scale employers. Job seekers have limited opportunities while the population at large faces relatively high costs and low quality and variety of goods and

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<sup>49</sup> Economist Intelligence Unit, October 2004 newswire.

services. All stakeholders could benefit from greater volume and quality of domestic production, greater availability of jobs, and a more stable workforce.

The 800-pound gorilla on the economic front, however, remains how East Timor will handle the oil revenues that are expected to flow into the state's coffers in the next 2-3 years. The government, with the assistance of the international community, has until then to establish viable accounting structures that will be transparent and facilitative of using these resources for the general public interest. Encouragingly, some progress has been made. Government officials have expressed a strong appreciation of the dangers involved and of their commitment to creating such an institutional architecture. Indeed, the World Bank and individual donors are already working the government on establishing an Oil Trust Fund, along the lines of what is employed in Norway. In this way, it is hoped that this resource will be a boon for the population and a stable source for the country's development – and not an easily siphoned revenue source for elite interests that contributes to growing disparities in wealth and political influence.

## **Social Sector**

East Timor benefits from relatively few obvious acute social fissures that could threaten the country's stability. The country is relatively homogenous ethnically and on religious beliefs. Most importantly, it benefits from a strong sense of solidarity stemming from its long struggle for independence (an attitude that can be expected to dissipate over time, however). The key social challenges that East Timor faces pertain to the need to rebuild its social infrastructure in order to address sustainably its grinding privations.

There are, however, certain demographic patterns to keep an eye on. East Timor is grappling with major dislocations in its population with the return of refugees from West Timor to its urban centers. This has sharpened the rural-urban differences in Timorese society and is likely a precursor to a continued rapid urbanization given their relatively greater access to basic amenities.<sup>50</sup> If this occurs and there are insufficient employment opportunities in the urban areas, then the social sector may become more combustible. A large number of unemployed disgruntled youth congregating in towns and cities could be a potential trouble spot. This in a country where 45% of the population is under the age of 15 and the fertility rate is 7.5 per woman – one of the highest in the world. Continued social investments, therefore, will be vital for forestalling future social tensions.

Another issue of potential social divisiveness pertains to language. Portuguese has been declared the national language and is intended to be progressively taught in schools. However, due to the long Indonesian occupation, only 5% of the total population speaks Portuguese currently. Most of these are people above 40 years of age. Language, therefore, exacerbates tensions between rural vs. urban dwellers as well as between generations. The process of reversing this reality will take time given that there are

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<sup>50</sup> *The Security of East Timor in the Regional Context*, Institute of Strategic and International Studies (IEEI), Lisbon, June 2002.

relatively few teachers speaking Portuguese (only 158 teachers, with 44% being in urban centers, were approved for teaching Portuguese in 2002)<sup>51</sup>.

A review of the health system again highlights significant rural/urban gaps. The most significant disease threats are largely due to the prevalence of communicable diseases such as malaria and tuberculosis.<sup>52</sup> Additionally, there is a low level of prenatal maternal care and consequently high maternal mortality<sup>53</sup>. Furthermore, since there is often a lack of proper sanitation facilities and clean drinking water, related diseases are common.<sup>54</sup> In urban areas, 70% of residents have access to these services, whereas, in rural areas, access is relatively limited (25% safe drinking water, 37% for sanitation and 61% for electricity).<sup>55</sup> Many rural East Timorese do not seek healthcare when they are sick due to cost and distance of healthcare facilities.<sup>56</sup>

In summary, a review of the political, security, economic, and social sectors highlights the fact that these vulnerabilities are nearly entirely on the effectiveness side of the effectiveness-legitimacy slate. (See the color-coded sectoral ratings with respect to East Timor’s fragility below). East Timor’s poverty and weak capacity, generated by its long years of underdevelopment and the devastation following its withdrawal from Indonesia continue to pose the most serious obstacles to its successful recovery.

<b>Sector</b>	<b>Effectiveness</b>	<b>Legitimacy</b>
Political	Orange	Green
Security	Red	Yellow
Economic	Orange	Green
Social	Yellow	Green

## **V. STATE CAPACITY: EFFECTIVENESS AND LEGITIMACY**

If we were to rate countries on their effectiveness/legitimacy ratio, East Timor would be a strong contender for the lowest score in the world. By all accounts, the government in East Timor has great legitimacy, having waged a long political and military battle against a far larger country to achieve its independence. Nearly the entire population was involved in this struggle – and virtually every family lost a loved one in the confrontation. The social cohesion generated from this process, has made East Timor a highly unified nation despite its young age. Meanwhile, the country’s first political leaders, led by President Gusmao, are considered by the general population to be highly legitimate due to their own personal sacrifices and risks endured during the Indonesian occupation. They are also seen as having earned the legitimacy to govern through the

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<sup>51</sup> World Bank (2003)

<sup>52</sup> McAuliffe, A. V., Grootjans, J., Fisher, J. (2002). Hasten Slowly: A Needs Analysis for Nurse and Village Health Worker Education in East Timor, *International Nursing Review*, vol. 49 (1): 47-54.

<sup>53</sup> World Bank (2003)

<sup>54</sup> World Bank (2003)

<sup>55</sup> World Bank (2003)

<sup>56</sup> World Bank (2003); World Bank (2004)

overwhelming popular support for the referendum on independence and the presidential and constitutional elections that were subsequently been held. President Gusmao has further burnished the trust and endearment the Timorese population holds for him through his inclusive, transparent, and public-spirited policy stances since being elected.

Despite this remarkable degree of legitimacy, as a brand new country East Timor is facing the daunting challenges of building capable state institutions from scratch. Developing effective delivery mechanisms for priority goods and services will understandably take some time. Not only is East Timor new but it is starting out as a very poor country. Therefore, it does not have the relative availability of resources that would enable it to more readily address the top priorities of the general population (resources, for instance, that the former republics of Yugoslavia had at their inception). East Timor is also severely constrained in its level of human capacity – both in terms of skills and experience. It should be recognized that this is a direct function of the systematic policies of the Indonesian government to decapitate the intellectual capacity of the population and then to destroy the limited infrastructure that did exist at independence. The end result is great strains on the new state. Demands for services are acute, while the resources to generate more positive outcomes are highly constrained. As the depletion of East Timorese human and institutional capacity occurred over a matter of decades, the process of recovery must also be considered in a long term view.

## **VI. EFFORTS TO STRENGTHEN EFFECTIVENESS AND LEGITIMACY**

Given the near total absence of governance structures and institutions in East Timor at independence, nearly all government and donor efforts have been focused on capacity building in some form or another. This has been coordinated under UNMISSET which has been providing governance and technical support to the new government. Donors, including USAID, support the World Bank-managed Transitional Support Program, which provides direct support to the East Timor national budget with benchmarks linked to the five-year National Development Plan.<sup>57</sup> The United Nations agencies represent the largest multilateral donors, followed by the World Bank and the Asian Development Bank. The top five bilateral donors are Australia, Japan, European Union, the United States, and Portugal. Seventy percent of bilateral program support is directed towards capacity building, budget support, health, education, and humanitarian assistance. According to the World Bank, the education sector utilizes 12.4% of total GDP and health sector 7.0% of GDP. As most of the population relies on the public sector for education (87% of students) and health<sup>58</sup>, these sectors have been heavily prioritized in the reconstruction effort. Allocations for agriculture and rural development, basic infrastructure, water supply and sanitation, environmental protection and management, and private sector development have received much less support.<sup>59</sup>

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<sup>57</sup> USAID East Timor. 2004 Congressional Budget Justification.

<sup>58</sup> World Bank (2003)

<sup>59</sup> USAID East Timor, 2004.

As referenced in earlier sections, the security sector has been supported by Australia and the UK. Efforts to establish an oil trust fund have been spearheaded by the World Bank and the Norwegian government.

USAID's East Timor program focuses on two objectives: 1) institutional and policy changes that support private sector development including the revitalization of the local economy; and 2) strengthening democracy and good governance. USAID funds are being used to implement ongoing economic growth programs that support the expansion of coffee and vanilla exports, increase household incomes, diversify agricultural systems, expand technical/vocational training, and improve the enabling environment for private sector growth. The democratic development focus includes increasing public participation in good governance, strengthening the judicial system, supporting the development of political parties, strengthening civil society, and fostering civilian oversight of the uniformed forces.

## **VII. SYNTHESIS: CENTRAL POLITICAL ECONOMY PROBLEM(S) THAT POSE RISK TO STABILITY**

There is much that is hopeful about East Timor's future and the prospects of it joining the ranks of transformational development countries are favorable. Given that East Timor is a new state, however, and that it must create or rehabilitate all of its major political, economic, social, and legal institutions – it is still a fragile state. It could through a number of plausible scenarios, be derailed from its currently successful recovery trajectory and pulled back down into a highly unstable reality. This assessment highlights three primary risk areas to East Timor's continued march toward democratic consolidation, economic development, and political stability.

The first of these involves the failure to ensure sufficient checks and balances on the executive branch (prime minister's office). Under the Timorese constitution, considerable power is vested in the prime minister, who runs the government and is head of the parliament. The president plays largely a symbolic role. For now, the arrangement is working due to the incomparable degree of trust and credibility bestowed on President Gusmao as the undisputed father of East Timor's independence. His emphasis on encompassing themes of unity, tolerance, and reconciliation have had an immeasurable influence on the post-independence psyche in East Timor. The early years of any independent country are heavily shaped by the quality of its leadership – and the norms that it establishes – and in this respect, East Timor has been abundantly blessed. Although the dynamism of President Gusmao's leadership is an undisputed force for stability at the moment, it is also a sign of weakness. Until the institutional checks and balances on power are clearly established and the legal mechanisms for succession fully accepted, East Timor remains a fragile state. In other words, much of East Timor's stability and hope for remaining on the path to recovery depends on one man. If for whatever reason he should be incapacitated, the prospects of East Timor successfully stabilizing would be considerably diminished.

The acuity of this reality is sharpened by the fact that due to the decimation of the Indonesian occupation, the ranks of Timorese leaders is thin. The degree to which other Timorese leaders share Gusmao's vision and commitment to a pluralistic, transparent, and tolerant society based on civil freedoms remains uncertain. Given the current unformulated state of East Timor's institutions, it would be relatively easy for an opportunistic politician to consolidate power, constrain political opposition and civil liberties, and bypass accountability mechanisms including competitive elections. Indeed, while this desktop analysis is not in a position to assess the motivations of any Timorese political or political party, the actions of the current prime minister give cause for concern. He is commonly perceived as preferring a top-down governance style, has limited enthusiasm for the devolution of authority to nascent local government bodies, and has moved to make the police personally loyal to him, compromising the independence of the internal security sector. Should the political differences and competition between Gusmao and Alkatiri further expand, it is conceivable that Alkatiri may attempt to marginalize Gusmao – potentially setting up a conflict between the state's police and army units. Alternately, if Gusmao were to depart from the political scene and a new president selected, the prime minister may be tempted to disregard the oversight function of the presidency altogether, usurping even greater power for himself.

The scenario is made further plausible in that East Timor's current parliament was not elected as a legislative body. Rather the members were elected as part of a special constitutional assembly to write a constitution leading up to independence. In a controversial move, they then went on to declare themselves the nation's first parliament. While some observers defend this action as reasonable given the extraordinary circumstances involved in establishing a national political structure, it could establish an unfortunate norm of elected leaders illegally perpetuating their terms in office - with the end product being that both vertical and horizontal accountability checks on the executive have been removed. The fractious experience of East Timor's political parties in the brief period of independence from Portugal (and prior to the Indonesian invasion) is further evidence of the potential for deterioration. Lacking a clear governance model or method for selecting national leaders and unable to agree on rules for political competition, East Timor fell into civil conflict within months of the Portuguese departure. It was thus vulnerable to both internal and external sources of instability.

A second primary threat to East Timor's stability is posed by domestic militias, disgruntled veterans, martial arts groups, and unemployed youth. The first three of these groups alone comprise several tens of thousands of individuals with military training and loose organizational structures. They, thus, represent a potentially potent disruptive force to a small country with a weak security sector. If these disparate groups were to be radicalized and mobilized by an opportunistic actor seeking to usurp power or gain access to East Timor's expected oil windfall, East Timor could conceivably deteriorate into a Haiti or Liberia-styled fragmentation. Such a mobilization would inevitably involve fanning real and perceived grievances that these groups feel. These include issues of political representation, under-appreciation for the sacrifices made by veterans of the independence struggle, and lack of jobs and economic opportunities for youth with limited skills. These potential fissures are a reflection of the decades of neglect of East

Timor's human capital and the deliberate devastation of its economic infrastructure during the aftermath to the independence referendum – more than any policy actions taken by the fledgling state. Nonetheless, they represent a vulnerability. They also present an economic challenge to the East Timorese government: how to expand and target economic opportunity to those groups who feel relatively deprived while maintaining sound fiscal policies so as not to forestall international investment and long-term economic growth. There is also a communications or social marketing element to this vulnerability. In effect, the government is facing a struggle for the hearts and minds of these alienated groups – against the ploys and misinformation perpetuated by militia leaders and opportunistic politicians. In other words, the government is in need of a strategy to establish a connection with these target groups – through its development initiatives – but also through the messages that it communicates regarding the plans, vision, and strategy it has for these groups. By all accounts, the government's communication efforts on this as well as other public policy initiatives has been woefully inadequate – leaving even supporters unclear what the government is doing on their behalf and how the public can become an active participant in the policymaking process.

Third is the threat of external destabilization by individuals or groups in Indonesia who continue to resent East Timor's independence and wish to reassert Indonesian influence – and failing that to destabilize East Timor out of spite for Timorese ambitions for independence. This vulnerability could play through a number of fronts – for example, with Indonesian actors arming and empowering the militias and disaffected groups described above; through a systematic misinformation campaign that aims to widen and inflame fissures within Timorese society so as to sow division, discord, and instability; or via covert, cross-border military operations by Indonesian-based militias that have the implicit approval of the Indonesian government aiming to fan nationalist sentiment within Indonesia. While the particular form of intervention may vary, they all point to the reality that East Timor's weak security sector makes East Timor highly vulnerable to even a low-grade destabilization effort from its much larger and wealthier neighbor that still harbors considerable resentment over East Timor's secession. This still raw history remains a highly relevant factor for East Timor's stability and should not be overlooked. This vulnerability is likely to grow wider if UNMISSET phases out of East Timor before sufficient capacity in the security sector has been established. In this way, UNMISSET's departure may serve as a trigger to more concerted challenges to East Timor's stability.

## **VIII. POTENTIAL INTERVENTIONS TO FACILITATE RECOVERY**

To address the underlying causes of East Timor's fragility, this assessment recommends USAID and the USG as a whole consider the following four courses of action. Two of these are traditional program interventions, one would bolster the security sector, and the last would be more diplomatic in nature.

**Maintain support to transition.** Two years out from independence, USAID and other donors are scaling back their operations in East Timor with the understandable rationale that progress is being made, the new government of East Timor should be taking over more of the responsibilities of public service provision, and a desire to curtail seemingly

never-ending nation-building interventions. Indeed, USAID East Timor's FY2005 budget request of \$13.5 million reflects a 40% decline in funding from FY2004 levels. This scaling back after a seemingly successful democratic transition is, in fact, typical of international donors since 1990. A considerable volume of assistance tends to go into a democratizing state up until the first democratic elections but then, with the perception that the mission has been accomplished, drops off dramatically afterward.<sup>60</sup>

This analysis contends, from a stability perspective, that the US and other donors should maintain FY2004 levels of engagement in East Timor through at least 2007. Maintaining the FY2004 level of resources provides a broader foundation for the wide range of capacity building measures that are needed for East Timor to enhance the *effectiveness* dimensions of its governance capability, which have been identified as the underlying source of much of East Timor's fragility. A sustained effort at strengthening these capacities would also better balance the exemplary levels of legitimacy the new state has earned and, by so doing, better ensure East Timor's stability as it moves away from its conflict-torn birth.

This recommendation is based on the contention that in certain ways, East Timor is entering into a period of greater risk than it has encountered in the past several years. Research indicates that democratic backsliding is most common three years after a democratic transition. Yet for each year that the transition can be sustained, the probability of backtracking declines considerably.<sup>61</sup> Sustaining resource transfers to East Timor is particularly merited, as it is in other cases of prolonged repression (such as Kosovo, Southern Sudan, Iraq, and Afghanistan), in that the human and institutional capacity levels have been so badly deteriorated over a period of decades that the new state must recover from a much deeper hole than normal. Indeed, a designated objective of the occupation was to eviscerate East Timor of its intellectual and institutional capacity. Accordingly, it is reasonable to anticipate that it will take several years longer to establish the core competencies required to sustain the state. Targeting a phase-down of funding to East Timor in FY2007 would dovetail with the second cycle of presidential and parliamentary elections – another critical benchmark for achieving democratic consolidation. Moreover, it is expected that oil revenues from East Timor's off-shore reserves will not begin arriving until 2007. Organizing a phase-over to coincide with that critical development (and subsequent to the strengthening of the Norwegian-inspired and World Bank supported Oil Trust Fund) would make the phase down of an international presence far less disruptive. If this continued support helps avoid a prolonged economic contraction that many expect to result from the UN withdrawal, it also removes another key determinant of democratic backtracking.<sup>62</sup>

Consistent with this recommendation, the US government should lobby Security Council members to maintain a UNMISET presence in East Timor for at least two years past the

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<sup>60</sup> Pei, Minxin and Merrit Lyon. 2002. "Bullish on New Democracies: Research Notes on Multinationals and the Third Wave," *The National Interest*, No. 70 (Winter 2002/2003), pp. 79-87.

<sup>61</sup> Halperin, Morton H., Joseph T. Siegle, and Michael M. Weinstein. 2004. *The Democracy Advantage: How Democracies Promote Prosperity and Peace*.

<sup>62</sup> Ibid.

current May 2005 target end date. Naturally, the nature and focus of this effort would change as capacities were established within the East Timor government and would be coordinated with the democratic leadership in East Timor so as to ensure that the capacity-building contribution of the international presence were enhanced, the deleterious side-effects were diminished, and a systematic transition could occur.

**Undertake Works Program Targeting Unemployed Youth and Disgruntled Veterans.** One of the most obvious vulnerabilities that East Timor faces is the relatively large number of alienated, young, and unemployed men in the society. Some of these are former combatants who have military training. Others are a part of the growing network of martial arts schools. These groups pose a threat since they are a potent force that if radicalized and mobilized could pose a serious threat to East Timor's weak security sector. All of the progress that has been made in the past several years could be devastated in a matter of days. This problem is likely to only get worse as the youth bulge expands, urbanization accelerates, and the economy faces the prospect of stalling. In other words, this is a multi-year challenge that should be seen as part of an effort to bridge the early years of East Timor's post-independence efforts with the long-term development efforts the country will be facing. This assessment, therefore, proposes that a large-scale works programs be instituted – along the lines of the Indian, Botswana, or Depression-era U.S. models. The youth would be organized into work brigades providing organized labor to address some of East Timor's priority infrastructural needs – e.g. roads construction, road maintenance, dike development, gravity-based irrigation infrastructure, wells, sanitation facilities, schools, clinics, etc. Moreover, the program could serve as a forum for training these youth in technical skills that would increase their prospects for future employment. As such, the program would have multiple objectives – getting unemployed youth off the street and mobilized toward some productive outcomes, infrastructural development, and skills development. All of these would contribute to reducing the vulnerability to fragility East Timor faces.

**Security Sector Reform.** Weaknesses in East Timor's security sector poses multiple vulnerabilities – from potential internal clashes between the police and army, the politicization of the security units, to exposure to destabilizing efforts by either internal or externally-driven militia. The British and Australians have undertaken considerable effort to build the capacity of the police forces. Relatively less has been done to develop the professionalism and capacity of the army, yet given the internal and external armed opposition that could be mounted, this is a priority for ensuring East Timor stays on the path to recovery. Consequently, this is an intervention that the U.S. government should consider. The U.S. DOD has well established officer and enlisted personnel training programs. This effort should be expanded to East Timor. Given the small size and scale of the military forces in East Timor, the cost would be relatively modest, though the benefits for security, stability, and democracy would be significant and long-lasting. To the extent that this effort was deemed to be outside of the realm of priorities for the DOD at this point and time, efforts could be undertaken to ensure funding for this initiative were mobilized so that the Canadians, Australian, or British would take it on.

**Reaffirming Norms of Democratic Succession.** As described in section 7, one of the underlying vulnerabilities East Timor faces is the lack of consolidated democratic institutions. The ambiguity between the roles and influence of the president and prime minister, the weakness of the judicial sector and the expectation that it will be unable to play a role anytime soon in sorting out this inevitable competition between other branches of government, and the fact that the political landscape in East Timor is currently dominated by one party reflects a real vulnerability of a creeping coup. Political power could be monopolized and perpetuated. Economic consolidation could subsequently follow. To avert this outcome, the US State Department and members of the executive branch should clearly communicate to all actors in East Timor that unconstitutional seizures of power will not be recognized. Not only would assistance be cut off but the U.S. would work with like-minded governments to ensure that any individual claiming power through such undemocratic processes would not be recognized as a legitimate head of state. East Timor's applications to any international bodies would be opposed. Experience has shown that clear signals from major external actors shape the incentives for domestic political actors contemplating non-democratic strategies to attain power in states with previously established democratic norms. In short, clear and consistent diplomatic signaling by the U.S. government at this time would be a relatively inexpensive though highly influential means to further undergird the political transition and capacity-building efforts in East Timor until democratic institutions were consolidated.