Document of
The World Bank

FOR OFFICIAL USE ONLY

Report No. 47556-TN

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED

INTEGRATION AND COMPETITIVENESS DEVELOPMENT POLICY LOAN

IN THE AMOUNT OF US$250 MILLION

TO THE

REPUBLIC OF TUNISIA

February 26, 2009

Social and Economic Development (MNSED)
Middle East and North Africa Region

REPUBLIC OF TUNISIA - GOVERNMENT FISCAL YEAR
FY 2009-2010

CURRENCY EQUIVALENTS
Exchange Rate Effective as of February 26, 2009

Currency Unit	Tunisian Dinar (TND)
US$1.00	1.44 TND

Weights and Measures
Metric System

ABBREVIATION AND ACRONYMS

(as applicable, plus others)

AA	Association Agreement
AFDB	African Development Bank
BCT	Central Bank of Tunisia
BPO	Business Process Outsourcing
CAS	Country Assistance Strategy
CFAA	Country Financial Accountability Assessment
CMF	Conseil du Marché Financier
CPS	Country Partnership Strategy
CNS	Conseil National des Services
EU	European Union
DPL	Development Policy Loan
FSAP	Financial Sector Assessment Program
GDP	Gross Domestic Product
GNP	Gross National Product
IBRD	International Bank for Reconstruction and Development
ICL	Integration and Competitiveness Development Policy Loan
IDA	International Development Association
IFC	International Finance Corporation
ICT	Information and Communication Technology
IMF	International Monetary Fund
LDP	Letter of Development Policy
MFA	Multi-Fibre Agreement
MDGs	Millennium Development Goals
MOE	Ministry of Education
MOF	Ministry of Finance
MOH	Ministry of Health
MTEF	Medium-Term Expenditure Framework
NDP	National Development Plan
PEFA	Public Expenditure and Financial Assessment
SDR	Special Drawing Rights
UNDP	United Nations Development Program
TTN	Tunisia Trade Net

Vice President:	Daniela Gressani
Country Director:	Mats Karlsson
Sector Director:	Ritva Reinikka
Sector Manager:	Farrukh Iqbal
Task Team Leader:	Ndiamé Diop

FOR OFFICIAL USE ONLY

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
PROGRAM DOCUMENT
FOR A
PROPOSED INTEGRATION AND COMPETITIVENESS DEVELOPMENT POLICY LOAN
TO THE
REPUBLIC OF TUNISIA

TABLE OF CONTENTS

This DPL was jointly prepared and pre-appraised by the World Bank, the African Development Bank and the European Commission. The World Bank team is comprised of Ndiamé Diop (team leader), Olivier Cattaneo, Didier Debals, Julien Gourdon, Mariem Malouche, Jean Michel Marchat, Daniela Marotta, Sophie Muller and Peter Walkenhorst; The legal counsel was Jean-Charles de Daruvar and the financial officer David Freese. The work was conducted under the guidance of Farrukh Iqbal (Sector Manager) and Ritva Reinikka (Sector Director). The project document benefited from excellent comments from peer reviewers: Sebastien Dessus, Bernard Hoekman, Robert Keyfitz and Vincent Palmade and excellent inputs from Najy Benhassine, Ingrid Ivins and Eavan O'Halloran. The team is also grateful for comments received from Jean-François Arvis, Rebekka Grun, Fatou Fall and Alaa Sarhan. Excellent administrative support was provided by Khalid Alouane. The team also benefitted from interactions with colleagues from the African Development Bank (Natsuko Obayashi and Hyacinthe Kouassi) and the European Commission (Odoardo Como, Fabian Seiderer and Pilar Blanco Rodriguez) and is greatly indebted to many Government of Tunisia officials who graciously contributed their time and knowledge. Special thanks are due to the Ministry of Development and International Cooperation and Mr. Abdelhamid Triki, Secretary of State in charge of International Cooperation and Foreign Investment and his collaborators for their productive cooperation.

REPUBLIC OF TUNISIA
INTEGRATION AND COMPETITIVENESS DEVELOPMENT POLICY LOAN

LOAN AND PROGRAM SUMMARY

Borrower	Republic of Tunisia
Implementing Agency	Ministry of Development and International Cooperation
Financing Data	IBRD Loan; amount: US$ 250 million Financing terms: Libor-based variable spread; 30 years maturity including 6 years of grace period; Loan currency: USD
Operation type	Two-Tranche Development Policy Loan (DPL). The first tranche is to be disbursed upon effectiveness and the second tranche will be disbursed about 12 months after effectiveness, following the Bank's review of policy actions implemented as per the loan agreement.
Main Policy Areas:	The reform program supported by the loan is based on two key pillars of Tunisia's 11th National Development Plan: (i) accelerating the pace of growth and (ii) preserving macroeconomic stability. Specifically, the proposed DPL will support policy actions in the following areas: (i) reducing trade transaction costs and deepening Tunisia's global economic integration; (ii) further improving the business climate to enhance competitiveness of Tunisian firms, including services; and; (iii) strengthening the financial sector to increase its capacity to finance private investment.
Key expected output/outcome indicators	1) Reduced trade transaction costs and deeper integration • Reduced tariff barriers, simpler tariff regime and greater trade diversification through reduction of tariff gaps between preferential and non-preferential partners • Convergence to EU product and quality standards effective through changes in regulations and effective application of the changes • Reduced time and cost to trade through selective and streamlined technical controls of imports, e-governance of trade procedures and more effective logistics services 2) Further improvement in the business climate • Reduced administrative burden for creating business by reducing the number of activities for which pre-authorization of entry is required. • Improved and transparent market information system through the adoption of the draft law on Registry of Commerce (with effective online access) and of the action plan for the establishment of a unique identifier of businesses • Reduced delays in access to industrial land through a reduction of delay to respond for the division of industrial land lots. • Reduced anti competitive practices through regulatory and competition assessments of competition practices by the Competition Council with a focus on services sector. 3) Strengthened financial sector • Stronger banking sector through a lower rate of non-performing loans and a higher rate of provisioning of those loans • Strengthened venture capital firms through amendment of the law that govern their functioning • Deeper and more liquid stock market through channeling more privatization of public enterprises to the stock market and partial opening of the capital of state-owned enterprises to the public. The loan will also help Tunisia finance its budget deficit and maintain macroeconomic stability in the current difficult and volatile international economic environment especially as the Government does not intend to seek financing from the international bond market in 2009.

Program Development Objectives and Contribution to CAS	The overall objective of the DPL is to support efforts to deepen Tunisia's global integration and enhance the capacity of Tunisian firms to exploit the opportunities offered by greater integration. More specifically, the program supports: • *Reducing trade transaction costs and deepening Tunisia's global integration;* • *Further improving the business climate to encourage private investment and facilitate business operations and;* • *Strengthening the financial sector to increase its capacity to finance investment.* The Integration and Competitiveness Development Policy Loan is a core element of the Bank's Country Assistance Strategy (FY05-08) and the Country Assistance Strategy Progress Report (2007) that set out an indicative program for FY09-10. It constitutes a strong support of the first pillar of the CAS which seeks to "strengthen the business environment to support the development of a more competitive, internationally integrated private sector and improve competitiveness of the Tunisian economy". This operation is also expected to be a major component of the new Country Partnership Strategy currently under preparation.
Risks and risk mitigation	The program faces two main risks. (i) First, the direct impact of the global financial and economic crisis on Tunisia's growth and development remains uncertain. The duration of the recession in Europe is a key factor, affecting Tunisia primarily through exports, tourism, foreign direct investment, and remittances. By accelerating the economic reforms supported by this program, the Government expects to mitigate this risk and reduce its financial vulnerability. In addition, Tunisia's development partners have come together to provide a common platform of support to help the country respond to the more difficult external environment. The continuous macro-monitoring and country dialogue will help respond quickly if needed. (ii) Second, the expected response of the private sector to the reforms may be muted given the global economic downturn and uncertainties about the duration of the recession in Europe. These would affect private investment. To mitigate this risk, the Government is stepping up investment climate reforms, including finance for enterprises, and is undertaking a broad communication campaign on its policy measures to international investors. Although Presidential Elections will be held in October 2009, the political risk is low as the current president is likely to win given the absence of a credible opposition candidate.
Project ID Number	P095388

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED INTEGRATION AND COMPETITIVENESS DEVELOPMENT POLICY LOAN

TO THE REPUBLIC OF TUNISIA

I. INTRODUCTION

1. This Program Document proposes an Integration and Competitiveness Development Policy Loan (ICL) for Tunisia in the amount of US$250 million. This ICL supports the key strategic elements of Tunisia's 11th National Development Plan (2007-11) which seeks to strengthen growth and ensure that this growth is translated into employment. It is also a cornerstone of the World Bank's program in Tunisia as outlined in the Country Assistance Strategy (FY05-08) and the Country Assistance Strategy Progress Report (2007) that set out an indicative program for FY09-10. This operation is also expected to be a major component of the new Country Partnership Strategy (FY10-13). The main thrust of the program is to continue growth-enhancing reforms anchored around a deeper integration of Tunisia to the global economy. More urgently, the ICL will assist the Government in responding to the global financial crisis which is beginning to expose Tunisia's inherent macroeconomic vulnerability to growth in Europe. The immediate objective of the Government is therefore to accelerate reforms, send a strong signal to investors and mitigate recession contagion risks in the coming years. The global financial crisis and economic downturn will no doubt drive policy changes in Tunisia's main competitors for direct foreign investment and trade. Tunisia has decided to respond by accelerating reforms to maintain its competitiveness.

2. Tunisia is a small open economy that is permanently facing challenges from developments in the world markets. So far, the country's global integration strategy has worked well: in 1971, to reduce the anti-export bias inherent in the heavy protection of the economy, an offshore sector was created. This triggered a rapid rise in FDI and the birth of a large labor-intensive textile industry integrated vertically with the EU's production networks. In the middle of the 1990s, trade protection vis-à-vis the EU was scheduled for gradual and systematic dismantling, as part of the Tunisia-EU Association Agreement (AA). Trade liberalization was accompanied by a wide ranging structural reforms supported by the World Bank. A recent Bank report shows that while a new generation of reforms is needed, past integration efforts have led to new exporting sectors emerging in both manufacturing (automobile electrical and mechanical components) and services (business process outsourcing, BPO). That study also found that Tunisia's economic sectors which are highly integrated to the global market have been able to attract investment, converge to EU's labor productivity standards, and boost job creation. [1] The country's average annual economic growth of about 5 percent in 1996-2007 clearly owes much to the Government's solid macroeconomic and integration policies.

3. Tunisia now faces two interrelated challenges. First, it needs to grow at a much faster rate than in the past to reduce high unemployment (14 percent). Tunisia's second challenge is the need to accelerate the structural transformation of the economy from a low-wage, labor-intensive economy to a knowledge-based, skill-intensive and technology-based economy. For a small economy, meeting both challenges requires deeper global integration, i.e., finding niches in global market for Tunisian

---

[1] World Bank (2008a). *Tunisia Global Integration: A New Generation of Reforms to Support Employment.*

products, tapping into global knowledge, technologies and investment, and further reducing protection at home to enhance resource allocation and efficiency. In its 11th National Development Plan (2007-2011), the Government clearly reaffirms its objective to deepen and widen the global integration of Tunisia. Operationally, this means shifting away from just facilitating the economy's adjustment to openness (supported by a series of four Bank structural adjustment loans in the past) towards a more ambitious and deeper global integration agenda.

4. The proposed ICL focuses on a set of mutually reinforcing policies and actions to deepen Tunisia's global economic integration and to promote private sector development. It proposes a selective focus on three key policies areas of the Government's reform agenda where the Bank and the other development partners can bring the most value added, specifically: (i) reducing trade transaction costs and deepening Tunisia's global economic integration. This involves both the move to a more global (i.e., non-preferential) integration and a deepening of the Association Agreement (AA) with the European Union to converge to EU safety and security norms and standards; (ii) Further improving the business climate to enhance competitiveness of Tunisian firms, including services and; (iii) Enhancing the development of the financial sector to increase its capacity to finance private investment. By supporting reforms in these areas, the program would contribute to growth and macroeconomic stability. It would also contribute to the Government's structural reform in response to (i) increased global competition and reduced trade protection, and (ii) the transition to an economy based on knowledge, innovation and diversification.

5. While this ICL is a stand-alone program, the dialogue around its content is de facto programmatic and it is likely that the Government will request another DPL at the end of this one. The program is jointly supported by the World Bank, the African Development Bank and the European Union and the three institutions have jointly worked with the Government to design the program within the framework of the 11th National Development Plan (NDP).

II. COUNTRY CONTEXT

6. Tunisia has had to adjust to several headwinds from the global economy since the beginning of the new millennium: a severe drought in 2001, the impact of September 11th on the tourism sector, the increase in world price of oil, the expiration of the Multi-fibre Agreement in 2005 and, more recently, the dramatic increase in international oil and cereal prices and the global financial crisis. Yet, in the period 2000-2007, the economy adjusted well to these shocks and registered a 4.8 percent average growth thanks to steady structural reforms and prudent macroeconomic management.

RECENT MACROECONOMIC DEVELOPMENTS IN TUNISIA

Trends in Growth and Employment

7. Gradual but steady structural reforms and sound macroeconomic management have continued to promote strong economic performance (6.3 percent real GDP growth in 2007) and greater resilience to adverse shocks. However, due to demographic pressures (rapid increase in the labor supply), the pace of GDP growth remains insufficient to reduce unemployment which hovers around 14 percent of the labor force. The jump in inflation in 2008 eroded the purchasing power of consumers, threatened the competitiveness of firms and made salary negotiations difficult and lengthy. Civil servants got a 4.5 percent annual salary increase for the next 3 years in November 2008 and private sector salary negotiations are ongoing. As world commodity prices declined however, policy concerns shifted dramatically from inflation to the global financial crisis, prompting the Government to announce in December 2008 a series of "presidential measures" to reduce the risk to growth of recession in Europe.

8. Overall, recent growth performance reflects dynamic behaviour of exports, robust private consumption and growing foreign investments. At the sector level, the services sector (59 percent of GDP) has been the engine of growth (7 percent annual growth on average in 2000-2007) thanks to dynamism of telecommunications, transport and commerce—while growth in tourism remained modest. In the manufacturing sector (17 percent of GDP), the mechanical and electrical sector witnessed a double digit growth in both investment and exports. In 2008, the sector accounted for 27 percent of merchandise exports (against 13 percent in 1995) and captured 31 percent of FDI flowing to the manufacturing sector (against 13.7 percent in 1995). The textile sector (33 percent of exports), on the other hand, weathered well to the external shock of the MFA dismantling, as many Western European firms having invested in Eastern Europe switched to countries like Tunisia due to rapid increase in wages following the Eastern European countries' EU accession. It is not clear however if the sector can expand in the future, owing to the complete dismantling by the EU and the US of remaining quotas on Chinese exports scheduled in 2008. The country is still vulnerable to the vagaries of rainfalls as below-average harvests (driven by below-average rainfalls) often claim up 1 to 2 percentage points of growth in Tunisia.

9. While growth has been respectable, it fell short of the 6.1 percent target (except in 2007). Between 1999 and 2008, unemployment was only slightly reduced, from 16 to 14.1 percent (Figure 2). Unemployment is particularly severe for first-time jobseekers with university degree, with the rate hitting 30 percent for the highly educated under thirty. It is estimated that between 80,000 and 90,000 net news jobs would need to be created each year only to absorb new entrants in the labor market, 57 percent of which are university graduates (World Bank, 2008b).[2] Tunisia's 11th NDP (2007-2011) considers that an annual growth rate of at least 6.1 percent is needed to reduce unemployment in the medium term.[3]

Figure 1. Evolution of GDP growth (%)

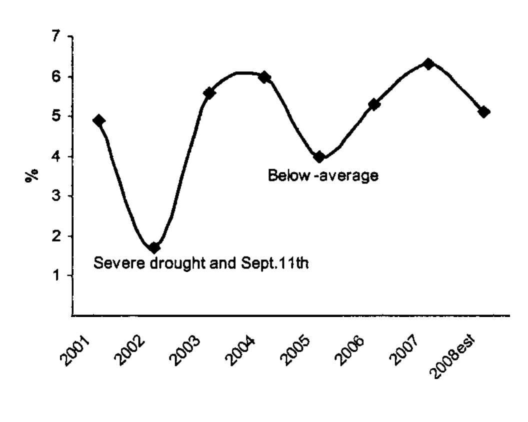
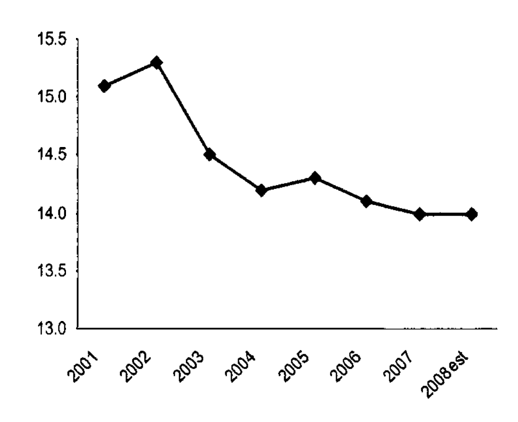


Figure 2. Evolution of unemployment (%)



Source: Institut National de la Statistique

Inflation and Prices

10. Tunisia has a good track record in keeping inflation under control (at or below 3 percent). While this performance partially reflects price controls on key foodstuffs, monetary policy helped reduce liquidity and inflation. For instance, following a surge of inflation to 5 percent towards the end of

[2] World Bank (2008b). *Employment, Skills Development and Social Protection*

[3] The recently released World Bank global poverty numbers indicate a poverty rate of 7 percent for Tunisia, one of the lowest in the region, and down from 40 percent in 1980. However, employment remains a key challenge.

2006 due to high oil prices and abundant money in the economy, the Central Bank of Tunisia (BCT) intervened by raising its key monetary policy rate by 25 basis points and the Banks' required reserves ratio from 3.5 percent to 5 percent, effectively reducing money in circulation and the growth in prices.

11. However, inflation picked up in the half of 2008, reaching a peak in April 2008 (6 percent on a year-by-year basis) before moderating in the last quarter of the year (Figures 3 and 4). Higher food and energy prices and rising liquidity, due to capital inflows from higher foreign direct investments, were the main drivers of inflation. Some of the inflationary pressure has also come from the nominal exchange rate, which depreciated by 2.8 percent in 2007.[4] The sharp decline in international commodity prices in the second semester of 2008 combined with liquidity tightening by the central bank (through two increases in the reserve requirement of banks) led to a sharp deceleration of inflation at the end of 2008.[5]

Figure 3. Overall and food price inflation (CPI)
(Year-on-year growth rate, in percent)

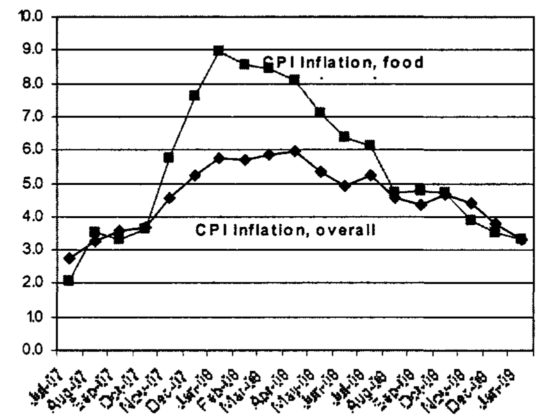
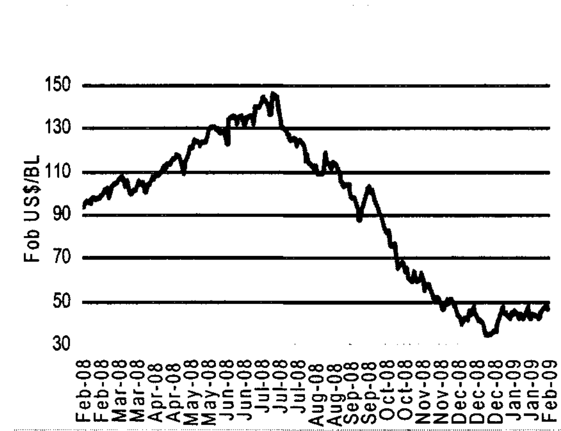


Figure 4. The evolution of Brent crude prices



Source: Institut National de la Statistique (inflation) and Bloomberg (oil prices)

Fiscal and current account deficits

12. The rise in international oil and cereal prices over the last three years has had a strong impact on public finances but offsetting evolution on the expenditure and revenues sides helped the Government maintain the fiscal deficit (excluding grants and privatization receipts) at 3 percent of GDP in 2007. On the expenditure side, total transfers and subsidies surged from 3.7 to 4.2 percent of GDP between 2006 and 2007, owing to a sharp rise in food and energy subsidies (Figure 5).[6] However, thanks to a drop in the public debt ratio, interest payments declined sharply and provided the fiscal space to accommodate a sharp rise in subsidies (Table 1). The favourable evolution of revenues also helped accommodate rising subsidies. Total revenues increased at a slightly higher rate than GDP thanks to a large extent to revenues from the energy sector. Corporate profit tax revenues from energy companies

---

[4] Food price inflation partially reflects the rise in world price of cereals and the indirect of effect of energy price increases on food industry, transport and other sectors' prices.

[5] The CBT announced in late 2006 its intention to move in the medium term towards inflation targeting as part of the overall process of gradual capital account liberalization.

[6] A supplemental budget law was adopted in December 2007 in order to increase subsidies for the *Caisse Générale de Compensation* (CGC) by 0.6 percent of GDP, bringing total food subsidies to 1.5 percent (700 million TND).

jumped to 2 percent of GDP and represented 51 percent of total corporate taxes (from 1.3 percent of GDP in 2006). Non fiscal energy revenues (royalties) reached 0.3 percent of GDP.

13. The impact of the global food and fuel crisis was stronger on the 2008 budget execution. Recent estimates by the Ministry of Finance put food subsidies at 1 billion TND (2.1 percent of GDP), i.e., 300 million TND above the budgeted envelope. Total fuel subsidies will have reached 800 million TND (1.6 percent of GDP) compared with a budgeted 450 million TND (based on an average oil price of US$75/barrel versus an average of US$98 for 2008). Thus the "direct" gross budgetary impact of the sharp rise in food and fuel prices 2008 is estimated at 1.3 percent of GDP, of which one has to deduct the positive impact of increased world oil prices on fiscal and non-fiscal revenues from the energy sector. The government policy since 2005 has been to gradually increase consumer price of energy to keep the subsidy under control. Fuel prices were raised three times in 2006, twice in 2007 and twice in 2008.

Table 1. Fiscal performance 2001-2008

	2001	2002	2003	2004	2005	2006	2007	2008[est]
Fiscal revenues (% GDP)	21.6	21.5	20.6	20.6	21.0	20.6	21.2	20.6
Non-fiscal revenues* (% GDP)	3.0	4.2	3.7	4.2	3.7	5.1	4.3	3.6
Primary expenditures (% GDP)	25.1	25.1	24.7	24.2	24.4	24.2	24.9	24.2
Interest expenditures (% GDP)	3.1	3.1	2.8	2.8	2.8	2.7	2.6	2.6
Fiscal deficit excl. gr. and priv. (% GDP)	-3.5	-3.3	-3.4	-2.8	-3.2	-2.9	-3.0	-3.0
Primary deficit excl. priv. (% GDP)	-0.4	0.0	-0.4	0.2	-0.2	0.0	-0.3	-0.2
Memo: Public debt (% GDP)	*62.4*	*61.6*	*60.4*	*59.7*	*58.4*	*53.9*	*50.9*	

Source: Ministry of Finance
Note: Figures for 2008 are Government estimates;
Non-fiscal revenues (*) include oil royalties, revenues from public participations to private oil companies, receipts from Algeria-Italy gas pipeline, grants and privatization receipts.

14. Tunisia's current account balance has continued to weaken but FDI inflow is significant: A 79 percent increase in the food imports increased current account deficit to 2.6 percent of GDP in 2007—from 2 percent of GDP in 2006 (Table 2). The deficit could have been larger but for a 55 percent increase in energy and mining exports. Preliminary estimates for 2008 show drop in energy and textile exports. Imports have also slowed slightly but remain strong. On the services side, Tourism receipts increased by 8.6 percent in the first quarter. Workers remittances were also up by 8.4 percent in the first three months of 2008 but they will likely moderate as EU economies slow. Current account deficit is projected to weaken to 4.2 percent of GDP in 2008.

Table 2: key balance of payment indicators (estimates for 2008 to be confirmed)

	2001	2002	2003	2004	2005	2006	2007	2008 (est)
Real growth in export of goods & services (%)	11.3	-3.7	0.05	7.7	3.2	3.4	11.8	1.0
Real Growth in import of goods & services (%)	13.5	-3.8	-0.4	3.5	1.1	6.8	9.6	4.0
Current account balance (% GDP)	-4.2	-3.5	-2.9	-1.9	-1.1	-2.0	-2.6	-4.2
Foreign Direct Investment (% GDP)	2.3	3.8	2.1	2.1	2.6	10.4	4.2	4.8
Gross foreign reserves (months of import)	2.1	2.4	2.8	3.1	3.2	4.5	4.5	4.2

Source: World Development Indicators

External financing conditions

15. Tunisia benefited from good external financing conditions in recent years, owing to its stable investment credit ratings (BBB/Baa2). In August 2007, the Government issued a 30 billion Yen

(US$260 million) Samurai bond on the best terms ever for the country: 75 basis points above the benchmark swaps rate and a maturity of 20 years. To put into perspective, Tunisia's previous issue (in June 2005) of a 15-year 400 million Euros Eurobond (US$ 500 million) had a margin of 107 basis points.

16. In contrast to the success that the government had in 2007 when it issued the Samurai bond in the Japanese market, Tunisia's sovereign spreads (EMBI Global spreads), along with other emerging markets, have increased dramatically in the last few months to more than 600 basis points as of December 1, 2008, reflecting a higher country risk resulting from the volatile global financial environment (Figure 5a). The EMBI Global spread for Tunisia is however way below the MENA regional average (close to 900 basis points) and even below the Euro Spread. While spreads are currently mainly driven by external factors and macroeconomic conditions in developed countries and are rising for all countries, the markets seem to give credit to Tunisia's prudent macroeconomic stance and stability. While data on corporate spreads (CEMBI spreads) for loans above US$300 million is missing for Tunisia, figure 7b suggests that they have dramatically increased as they reach 1000 basis points on average for emerging markets. Large firms in emerging countries, including Tunisia, find it hard to obtain cheap financing in the international market today.

17. Tunisia's stock market has followed the global downturn since October 2008 and, as of December 2008 it has lost almost the entire gain realized in 2008 (Figure 5c). Finally, despite a current account in deficit and a high level of debt amortization reflecting the magnitude of past external debts, foreign reserves accumulation has been strong, thanks in large part to FDI inflows. Tunisia's international reserves have risen in the first half of 2008 from its comfortable level of $8 billion (4.5 months of imports of goods and services) in December 2008 (Figure 5d).

Figures 5a to 5d: Tunisia's Current Financing Conditions

Fig. 5a. Soveriegn spreads- Benchmarking Tunisia

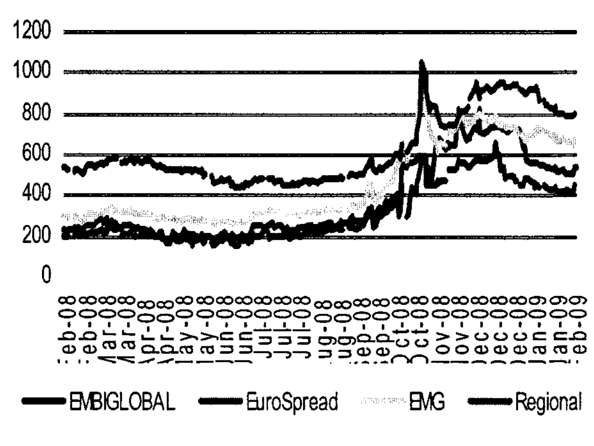
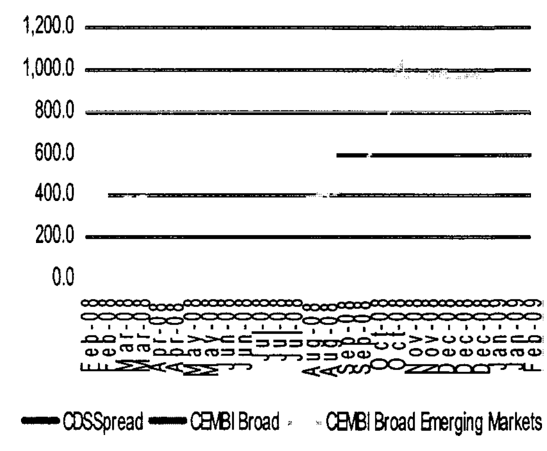
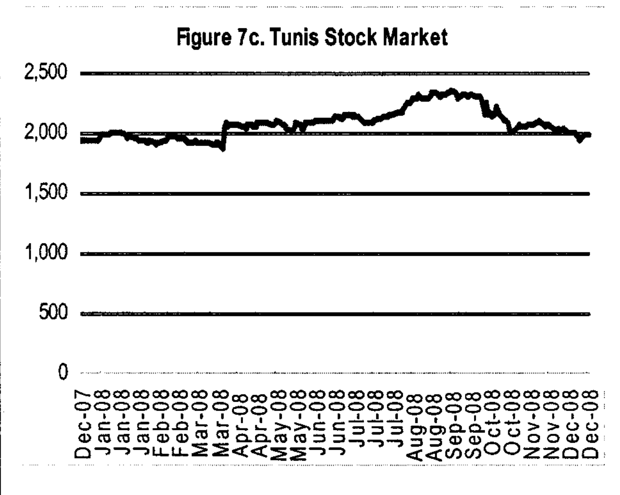
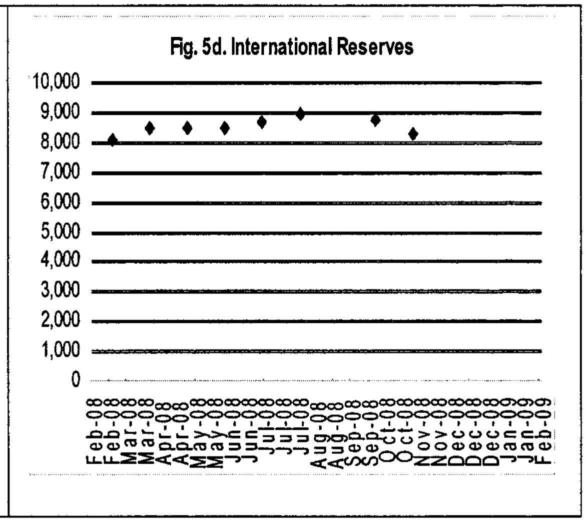


Fig. 5b. Credit Default Swap Spreads and CEMBI







Source: Bloomberg

The Government Response to the Global Financial Crisis

18. The Tunisian authorities have expressed confidence in the ability of the economy to maintain macro stability in the midst of the current global financial crisis. The Governor of the Central Bank said in October that "the factors that have caused the current international financial crisis do not exist in Tunisia". Then, the Prime Minister presented a confident perspective on the resilience of the financial sector and the economy. Officials, including the Prime Minister and Central Bank Governor, gave several reasons for their optimism, noting that: (i) Tunisia does not have a "sub-prime" problem; real estate loans represented only 10 percent of GDP (compared with close to 90 percent in the US) and most of them were long-term and fixed-interest; (ii) local banks have little foreign exposure; (iii) the money market is still highly liquid, and at the beginning of October the central bank had US$1.2bn available to inject into the market if needed; (iv) foreign participation in the stock market is "relatively low", at some 28 percent; (v) public debt has been reduced; (vi) Tunisia's foreign reserves have been managed prudently. The amount held in banks (mostly with double- or triple-A ratings) had been reduced to some 35 percent, and the rest was held in sovereign funds; and (vii) the dinar is non-convertible for most capital-account transactions.

19. A main Government argument is that features of the local financial system traditionally regarded as weaknesses, such as Tunisia's lack of integration into global financial markets and the low foreign participation rate in the stock market, are currently working in its favor, by shielding it from the turmoil in the outside world. Nevertheless, it is acknowledged that it is highly unlikely that the local economy can escape negative repercussions from the expected global economic slowdown, given Tunisia's reliance on Europe as a buyer of its exports (as discussed in the outlook section below). If the export sector is badly hit, it could adversely affect the financial sector that finances it. This is all the more so that the banking system has important structural weaknesses. The priority banking reforms discussed below (see Government Program section), chiefly those related to reducing the Non-Performing Loans (NPL) and enhancing prudential norms, are thus important for Tunisia.

20. In fact, by December 2008, it became evident that the real economy cannot escape the effects of recession in Europe. Growth in the volume of exports declined sharply in the second semester to 1.5 percent (against 14 percent in 2007). This triggered a swift government response. A series of "Presidential Measures" were announced following a Cabinet meeting on December 23rd. The "Presidential Measures" include both emergency measures aimed at assisting exporting firms already

adversely affected by the slowdown in Europe and measures to be implemented in 2009 and 2010, discussed with the Bank, the EU and the AFDB and contained in the matrix of this program. The emergency measures include: (i) subsidy of 50 percent of the employer's cost of social security for firms witnessing a dramatic fall in exports to Europe; (ii) a subsidy of 100 percent of the employer's cost of social security for firms that have to stop production and run down stocks; (iii) a subsidy of 50 percent of the cost of export insurance. In addition, the government announced the measures in the first pillar of this proposed DPL's policy matrix, aimed at reducing trade transaction costs. These include reducing customs duties, accelerating the trade procedures related to technical controls to reduce non-tariff barriers and improving logistics services.

21. Another element of response is contained in the budget law for 2009. The Government decided to increase public investment by 20 percent (mainly infrastructure projects: road, energy, port and airport). To avoid delays related to Tunisia's complex procurement procedures, an acceleration of procurement procedures for public contracts granted to the local private sector was planned. As discussed below, to keep the budget deficit around 3 percent, the budget law anticipates a sharp reduction of subsidies due to the decline in the world food and energy prices.

MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

22. Today's external environment presents exceptional challenges to economic forecasting. International oil and cereal prices, growth in Europe, regional security, and the impact of the global financial crisis are all elements of uncertainty. Nevertheless, for Tunisia, there are reasons for optimism. For more than 20 years, the country has been a consistent good performer. In the face of recent dramatic external shocks, it has demonstrated impressive resilience. The country has a clear and comprehensive development strategy and a tradition of pragmatic economic management. These underlying factors augur well for a continuation of the respectable performance of the past 25 years despite the difficult structural challenges at home and in the global financial and economic crisis.

Medium-term growth outlook (2009-2011)

23. The base case scenario of the macroeconomic framework takes account of (i) the projected growth in the EU following the global financial crisis; (ii) the projected evolution of the US dollar, the international price of oil and interest spreads; (iii) heightened competitive pressure on Tunisia's textile sector following complete dismantling of MFA quotas on Chinese exports to Europe in 2008; (iv) the impact of structural reforms supported by the reform program on private investment and productivity growth and; (v) a 20 percent rise in public investment in the 2009 Budget Law to finance large infrastructure projects to offset the potential negative impact of the global financial crisis on growth (stimulus package).

24. Under the above assumptions, Tunisia's real GDP growth is expected to weaken further to 4.2 percent in 2009 (stimulus duly taken into account), following a slow down in 2008 (estimated at 4.5 percent against 6.3 percent in 2007), before recovering to 5 percent in 2010. Agricultural sector growth is expected to pick up in 2009, following a sluggish performance in 2008. Economic growth will be driven in part by the expected continued expansion of domestic services such as commerce and information and communication industries. Tourism, textiles and clothing as well as the mechanical and electrical engineering sectors are expected to suffer from weaker demand from the EU..

25. Domestic demand, especially public investment, will thus be the main drivers of growth. It is expected that the major public investment efforts in 2009 and 2010 will impact growth in 2010 and 2011. The major infrastructure projects that are expected to boost growth include a new airport in Enfhida (150 kms South of Tunis), a new refinery in Gabes and the Tunis-Medjes-Beja-Boussalem

highway. In 2008, foreign direct investment (FDI) increased by 40 percent thanks to significant investment from the EU (France, Germany, Italy and the UK mainly) and the Gulf Arab countries. In sharp, in 2009, FDI will be highly vulnerable to the spreading impact of the credit crunch even if Tunisia remains an attractive FDI destination.[7] Domestic private investment is expected to expand in 2010, thanks to structural reforms supported by this program, including reduced trade and business entry transaction costs and better access to non-bank finance. However, given the continuing strong growth of the labor force and assuming no significant growth of employment in the public sector, the unemployment rate will be reduced only marginally, to around 13.5 percent by 2010 from 14.1 percent in 2007.

26. In the base case scenario, despite rising world oil prices, inflation is expected to remain under control, thanks to responsive monetary and economic policies. Tunisia's subsidy and import costs will ease although they will remain a heavy burden. The current account deficit would stand around 3.2 percent over the projection period.[8] No major terms-of-trade shock or reversal of capital flows is foreseen.

27. Compared to the above base case, possible downside risks include:

- A more durable recession in Europe. Growth in Tunisia may slow down temporarily or persistently, depending on the duration of the recession in Europe. Hence the importance of accelerating structural reforms now in order to mitigate the potential growth risk from EU contagion;
- Persistent uncertainties and muted private investment response to structural reforms due to heightened global economic uncertainties;
- Droughts that could reduce agricultural output, adversely affecting private consumption and exports and therefore requiring greater quantities of food imports and ;
- Regional insecurity which could affect Tunisia in the coming years, with tourism failing to reach the expected levels, and the country losing some of its attractiveness for foreign investors.

[7] Potentially, a large number of mega projects in real estate, not included in our projections, could substantially increase FDI. According to the Government, several Gulf countries intend to invest more than USD 25 billion in Tunisia over the next 15 years. It is not clear how much of these amounts will actually be invested over the next three years, especially given the current financial crisis and the global credit crunch and the drop in petroleum prices.

[8] The Government expects the private sector to play an important role in these investments (concessions) and the share of the private sector in total investment (gross fixed capital formation) to increase from 59 percent in 2007 to 62 percent in 2011.

Table 3: Tunisia's Medium-Term Macro Outlook

	Actual	Estimate	Projection		
	2007	2008	2009	2010	2011
Growth of Real GDPMP	6.3%	4.5%	4.2%	5.0%	6.2%
Growth of Real Exports GNFS	14.1%	1.5%	0.1%	7.0%	10.4%
Growth of Real Imports GNFS	12.1%	6.0%	4.0%	8.3%	6.9%
Inflation (GDP deflator)	2.4%	5.0%	4.0%	3.0%	3.1%
Gross Domestic Investment (real growth rate)	6.4%	6.5%	3.0%	6.9%	6.1%
Gross Domestic Investment (% of GDP)	24.8%	25.5%	25.5%	26.1%	25.8%
Fiscal Balance (excluding grants and privatization, % of GDP)	-3.0%	-3.0%	-3.1%	-3.0%	-2.9%
Primary Balance (excluding grants and privatization, % of GDP)	-0.3%	-0.7%	-0.8%	-0.7%	-0.6%
Current Account Balance (% of GDP)	-2.6%	-4.4%	-3.0%	-3.1%	-2.9%
Outstanding Foreign Debt (millions of US$)	19,308	19,855	20,125	20,374	20,230
Outstanding Foreign Debt (% of GDP)	55.2%	51.9%	51.6%	48.2%	44.1%
Outstanding Domestic Debt (% of GDP)	20.5%	20.2%	21.2%	21.2%	23.6%
Outstanding Debt, Total (% of GDP)	75.6%	72.1%	72.8%	69.4%	67.7%
of which: Public (% of GDP)	50.9%	51.7%	51.8%	50.6%	49.6%
Private (% of GDP)	24.7%	20.4%	21.1%	18.7%	18.1%
Gross Foreign Reserves (in months of imports of G&NFS)	4.5	4.2	4.3	4.4	4.6
Gross Foreign Reserves (millions of US$)	7,850	8,769	9,525	10,152	11,169
Nominal Exchange Rate (TD/US$)	1.281	1.295	1.376	1.378	1.377
For Reference: Oil Price ($/barrel)	71.1	97.0	47.8	52.7	57.9

Source: World Bank LDB and Bank Staff projections using RMSM-X based on Government's projections and assumptions. Figures for 2008 are Government estimates.

Fiscal deficit financing options

28. The context of global financial crisis has recently led the Government to revise its sources of fiscal deficit financing for 2009 and 2010. Initially, given the excess liquidity in the market in recent years (credit growth of 10 percent versus a deposit growth of 15.9 percent in 2008), the objective was to increase net financing from domestic sources by 32 percent and 13 percent for 2009 and 2010 respectively (Table 4). The consequence would have been an important reduction in gross *external* financing needs. However, in a context where liquidity in the market might be less abundant than in the past few years, that financing option may significantly suck up liquidity otherwise available for the private sector and other economic agents ("crowding out effect"). That in turn could adversely affect private investment and undermine growth and job creation.

29. To address financing needs in 2009 and 2010 without crowding out the private sector in the domestic market and without having to issue new bonds in the international market, the Government has decided to reduce significantly domestic financing in 2009 and increase external borrowing in 2009 (scenario 2). This is the main reason behind its desire to request a larger amount for the proposed program, from USD 150 to 250 million. The cumulated amount for this program of about USD 600 million (the Government has requested USD 250 million from the AfDB and the EU has agreed to provide 70 million Euros in Grants) will allow the Government to face its financial needs comfortably and without undermining access to finance by the private sector. Scheduled amortizations of external debt are indeed estimated to increase by 32 percent in 2010 and 56 percent in 2011 (Table 2).

Table 4. Fiscal deficit financing sources options

	2008	2009	2010
Fiscal deficit (TND)	-1,518	-1,656	-1,810
% of GDP	-3.0%	-3.0%	-3.0%
Outstanding public debt (TND)	23281	25057	27363
% of GDP	45.7%	45.4%	45.4%
Fiscal deficit financing sources (TND)			
Privatization and grants	337	200	83
Net domestic financing:			
Initial scenario:	1015	1,752	2,047
Revised scenario:		1,352	1,647
- Treasury bonds issuance			
Initial scenario:	2,325	3,087	3,516
Revised scenario:		2,687	3,116
- Amortization of domestic debt	1,310	1,335	1,469
Net external financing:			
Initial scenario:	166	-296	-320
Revised scenario:		104	80
- Long-term debt			
Initial scenario:	1,050	869	1,500
Revised scenario:		1269	1,900
- Amortization of foreign debt	884	1,165	1,820

Note: Net financing = Debt or bond issuance - amortization
Source: Ministry of Finance

Debt sustainability

30. The Tunisian government is committed to continue fiscal consolidation efforts and the fiscal deficit is projected to decline slightly to 2.9 percent of GDP in 2011—in line with the authorities' intentions as shown in the Medium-Term Expenditure Framework (MTEF). Fiscal consolidation will come, despite the expected rise in public expenditure, from future acceleration of GDP growth which will lead to a decline in the debt ratio and, on the revenue side, from increased tax revenue collection.[9]

31. The government intends to continue its pro-active public debt management through different instruments: (i) using privatization receipts for early repayment of high-interest debts (in 2007, TND358 million were repaid); (ii) active management of the risk related to the interest rate (in 2007, a total of 97 million TND were converted from variable to fixed rates and in 2008, only 8 percent of external debt had a variable rate); (iii) active management of exchange (the share of debt in euro has increased from 55 percent in 2006 to 59.5 percent in 2007) and refinancing risks (new emissions in the local market target long-term maturity bonds). The public debt ratio is estimated at 51.7 percent of GDP in 2008. Continued fiscal consolidation is expected to slightly reduce that ratio to 49.6 percent in

[9] Current expenditures are expected to increase in the immediate future but come back in 2011 just slightly above the level of 2007 (20.3 percent of GDP) thanks to a planned gradual phase-out of petroleum subsidies and increased domestic cereal production. On the revenue side, the tax revenue collection is forecast to increase in proportion of GDP growth.

2011.[10] Total foreign debt as a share in GDP is projected to decline to 44.1 percent of GDP by 2011, from 51.9 percent in 2008 (Table 4).

32. Keeping debt increases way below the rate of growth of the economy will help reduce debt-to-GDP ratios, freeing foreign exchange reserves and allowing the maintenance of reserves to 4.5 months of imports of goods and non-factor services through 2011. The current account deficit is projected to increase to stabilize at 3 percent of GDP by 2011 to maintain overall external financing needs around 8 percent of GDP (Table 5).

Table 5. External Financing Needs and Requirements (million US $)

	Actual	Estimate	Projection		
	2007	2008	2009	2010	2011
Financing Requirements	**2,920.7**	**3,572.8**	**3,281.6**	**3,214.6**	**3,648.2**
in % of GDP	*8.3*	*9.3*	*8.4*	*7.7*	*7.9*
Current Account Deficit	925.0	1,763.4	1,323.3	1,295.0	1,384.1
Long-term Debt Amortization	1,995.7	1,809.3	1,958.3	1,919.6	2,264.1
Financing Sources	**2,920.7**	**3,572.8**	**3,281.6**	**3,214.6**	**3,648.2**
Foreign Direct Investment (net)	1,560.2	2,038.3	2,053.0	2,300.0	2,548.0
Long-term Debt Disbursements	1,395.2	2,356.6	2,228.2	2,168.6	2,119.8
Government	1,395.2	2,260.6	2,066.2	1,980.6	1,919.8
Official	1,073.1	1,320.3	1,394.1	1,314.8	1,266.5
Private (Government Guaranteed)	322.8	940.3	672.2	665.9	653.3
Private (Non-Guaranteed)	0.0	96.0	162.0	188.0	200.0
Other Capital Flows	695.5	96.0	-396.8	-473.8	-95.3
Reserve Changes of the Central Bank (+ *denotes an increase*)	730.2	918.2	602.9	780.2	924.3

III. THE GOVERNMENT PROGRAM

33. The Government's Integration and Competitiveness Reform Program (ICRP) is part of its 11th National Development Plan (NDP). The framework sets out the broad package of policies, strategies and programs for implementation over the period 2007-2011. The 11th NDP supports the overall vision, goals and outcomes of Tunisia's Vision to 2016 and is the vehicle that transforms these long term goals and outcomes into short term priorities, strategies, programs and measures over the period 2007-2011. Employment generation is the highest priority of the 11th NDP. To achieve this, the 11th NDP focuses on: (a) accelerating private-sector driven growth; (b) maintaining macro stability; (c) upholding social achievements and human development; and (d) preserving natural resources. While not featuring strongly in the 11h NDP, regional development including through development of competitiveness poles that integrate production, research and innovation in the same space to attract private investment is emerging as an additional way of supporting job creation.

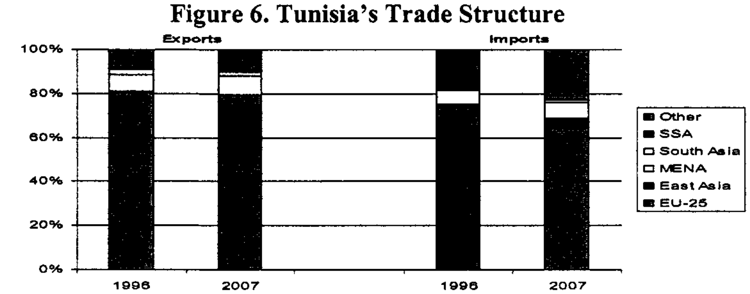
34. The integration and competitiveness reform program is composed of core elements of the two first pillars of the NDP, namely "accelerating the pace of growth" and "enhancing macro stability".[11]

[10] The Bank has supported the Government (through an IDF grant) in strengthening public debt institutions in 2005-2007. This support helped strengthen capacity for debt management, the creation of a "middle office" responsible for debt strategy and the publication of an annual report on public debt management.

While all the policy actions supported by the ICRP fall under "accelerating growth", they indirectly serve macro stability. Indeed the ICRP centers around 3 pillars, all crucial for growth and macro stability: furthering trade integration, improving the investment climate and fostering a development of the financial sector. In other words, to accelerate the pace of growth with macro stability, the Government counts on a significant increase in exports and investment. Robust exports and FDI over the long-term are expected to expand markets, enhance technological diffusion boost and productivity and growth. However, in the context of Tunisia, for the private sector to exploit fully the opportunities offered by greater global integration, pursuing financial sector reforms will be crucial as well. It is important to note that by boosting exports, investment and growth, global integration policies will help macroeconomic stability (maintain fiscal balance below 3 percent, improve current account balance and generate jobs).

FURTHERING TRADE INTEGRATION

Figure 6. Tunisia's Trade Structure



Source: Comtrade

35. Tunisia's key objective in the area of trade is to boost exports and competitiveness. Today, exports represent 52 percent of GDP and are an important engine of growth. However, Tunisia's export activity is still largely confined to manufacturing sectors (textiles, electrical and mechanical engineering). In the area of services, call centers and business process outsourcing activities are emerging but tourism and export-oriented transport services still largely dominate. Moreover, the country has not managed to diversify its markets. In 2007, the EU accounted for 80 percent of exports and 64 percent of imports, a situation that has barely changed over the last 10 years, especially for exports. Regional (MENA) trade remains limited in spite of progress in recent years (Figure 6).

36. To improve trade performance, the Tunisian Government's program focuses on three main subcomponents: (i) tariff reforms, non-tariff barrier reforms through regulatory convergence of norms and standards and more efficient import controls; (ii) preparation of services sector liberalization and (iii) trade logistics reforms.

37. **Tariff and non-tariff reforms**. The move to free trade for industrial products with the EU has introduced a substantial wedge between the duties applied to imports from the EU and those which are applied to third countries. For industrial goods, EU exporters face a zero tariff while non-preferential partners face an average Most-Favoured Nation (MFN) tariff of 21.4 percent. A recent World Bank study (World Bank 2008a) shows that this tariff gap not only creates costly trade diversion but also

---

One of the characters of Tunisia's development strategy is that growth should not be obtained without regards to fiscal and external equilibrium. The country has limited fiscal space and is highly exposed to shocks. Therefore, to maintain macro stability, it imposes itself a hard budget constraint. Tunisia's fiscal policy rests on a restriction of the general budget deficit to 3 percent of GDP to decrease vulnerability to shocks. To that effect, the Government's strategy is (i) further reduce public debt ratio and interest payments which stood at 2.6 percent of GDP in 2008; (ii) enhance the efficiency and effectiveness of public expenditures through gradual implementation of MTEF and performance budgeting and monitoring and evaluation (M&E) operational in key line ministries and (iii) enhance tax revenue collection.

encourages fraud and the development of parallel markets.[12] A key objective of the 11th NDP is to reduce tariff gaps by gradually reducing the MFN rates. The latter is scheduled to decline to 15 percent by 2009 in the NDP. The Government is also committed to scrap the number of tariff bands in order to simplify the tariff structure and facilitate its administration by customs. The number of tariff bands was reduced stepwise from 54 in 2003 to 9 in 2008 and it is planned to continue this reform in 2009 through 2011.

38. But as tariffs are reduced, non-tariff barriers have become more prominent. In spite of the several initiatives to streamline trade procedures and remove non-tariff impediments to trade, including through the internet platform Tunisia Trade Net, import controls and procedures remain cumbersome. There are numerous public actors controlling imports for safety, security, technical standard compliance, and so on. Unfortunately, the actions of these different actors (e.g., taking a sample and examining it at laboratory) are not well coordinated and this leads to delays and important transaction costs for importers and exporters. The Government plans to operationalize one-stop shops at major ports, and further harmonize norms and standards with international practices to facilitate trade. Much of the reform on standards and norms is embedded in the EU neighbourhood agenda, which offers Tunisia regulatory convergence and technical assistance (e.g. twinning of institutions for instance).

39. These reforms build on the progress made since the establishment of the Tunisia Trade Net (TTN). The TTN operates an automated system that provides a one-stop trade documentation and processing system, linking all major actors in the chain. The central bank, commercial banks, customs, chamber of commerce, and all licensing authorities are linked to this electronic network, and a prospective exporter or importer only has to submit one document to TTN. The automated system then channels the information to where it is needed. The introduction of TTN in Tunisia has allowed cutting the average time of document processing from eight days to three days. But the TTN is not yet fully operational as there are a number of relevant institutions that need to be connected to the network for more efficiency (transporters, trade commissioners known as "transitaires").

40. **Services integration**. In the 11th NDP, services are assigned a major role in the achievement of the country's growth and development objectives. It is forecasted that services will grow at an annual average rate of 8.7 percent during the 2007-2011 period, to contribute to 68.4 percent of the country's economic growth, and to represent 49.9 percent of the GDP at the end of the period. International trade will serve as a growth engine for a number of services sectors and largely contribute to the achievement of these objectives. Services exports are anticipated to grow by an average 9.6 percent (compared to 5.2 percent for the 10th Plan), to represent 24.3 percent of total exports in 2011. Sectors where Tunisia has a strong potential include health, professional services, transports, tourism, and information and communication technologies (ICT) services.

41. Reforms identified to unleash this potential are threefold. First, the Government plans to develop a strategy for exporting services and put in place coordinating mechanisms and statistical database to implement this strategy. Second, it plans to open many backbone services sectors –telecoms, banking, insurance, distribution, transport – to competition and trade. This entails specifically relaxing or removing entry and competition barriers to these sectors. A recent World Bank study finds these pervasive (World Bank 2008a). Bilateral negotiations with the EU are underway, as part of the Tunisia-EU Association Agreement. And finally, related to the future opening of the services sector, the Government plans to put in place *Mise a niveau* programs – upgrading programs —in order to enhance the degree of competitiveness of local services firms. Concretely, firms will be given financial support to invest in training, production organization, compliance with norms and investment in new machineries and equipments.

[12] World Bank (2008a). *Tunisia Global Integration: A New Generation of Reforms to Support Employment.*

42. **Trade logistics**. For a country whose competitiveness is closely linked to its proximity to its main export market, i.e. Europe, efficient transport logistics are of paramount importance. At current projections of GDP growth, the volume of trade is expected to double over the coming decade, thereby putting substantial strains on the existing trade and transport infrastructure. Tunisia has among the best logistics indicators in the MENA region but lags behind Turkey and Eastern European competitors which have benefited from regulatory convergence and institutional twinning with Europe in recent years.[13] It faces several constraints related to the limited availability of modern logistics platforms and warehouses. Exporters are small and atomized and often cannot by themselves fill a whole container, putting the onus on the efficiency of grouping and coordination by the logistics providers. Unfortunately, the latter are also small and they have not been able to minimize coordination failures. As a result, total logistics costs (transport, storage, delay, administration) are relatively high in Tunisia. They are estimated at 17 percent of total sales in the pharmaceutical and chemical industries, 12 percent in many industries and in the distribution sector, and 10 percent in the agro-industry (Table 6).

•

43. The Government has an ambitious plan to reduce logistics costs. This plan includes the building of large trade-related infrastructures, including a deep water port and an airport in Enfidha. The deep-water port and the airport of Enfidha, to be built close to Tunisia's main north-south motorway and railway line would make Enfidha one of Tunisia's main transport hubs. The project will also increase local port capacity, which is saturated, helping to fill a shortage of deepwater ports in the central Mediterranean. Reforms also include establishment of logistics platforms (including in Enfidha), opening the logistics services sector to entry of large firms that can overcome coordination failures and promoting strong partnerships between logistical operators and the customs administration in the context of a new customs code whose implementation will start in 2009.

Table 6. Logistics costs in percentage of sales, percent

Sector	% of total sales
Chemicals, pharmaceuticals and cosmetics	17
Products of mass consumption	13
Distribution	12
Other industries	12
Construction and civil works	11
Agri-business	10
Automobile	8

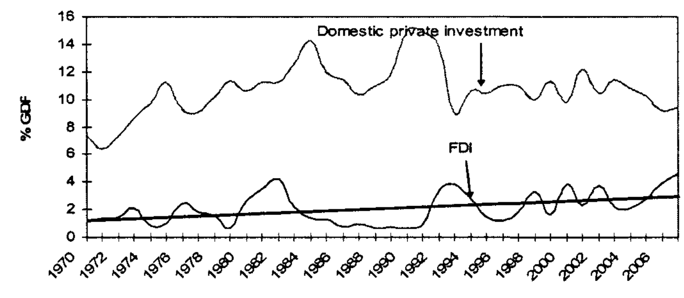
Source: World Bank estimates (Transport and Logistics Technical Assistance 2008)

IMPROVING THE INVESTMENT CLIMATE

44. The Tunisian authorities have maintained a policy of generous privileges for investments in selected economic activities and for exporting, by supporting the creation of an offshore regime. Under the offshore regime, firms were given an enclave business environment, with duty-free raw material and equipment imports, 10-year corporate tax holiday, free repatriation of profits and trade facilitation services (e.g., in-house customs clearance). Over the years, this strategy has helped address the import substitution bias of Tunisia's trade policy and thus contributed to promoting export-oriented growth. Indeed, export growth in Tunisia has been led almost exclusively by the offshore industry that has benefited from preferential export policies, leaving the onshore industry behind. Now that onshore firms are less protected by high tariffs than in the past, their survival depends on the improvement of their business "environment" and the reduction of the dichotomy in the economy.

[13] Tunisia is ranked 60th among the 150 countries in the Logistics Performance Index (LPI), a composite index developed by the World Bank (see www.worldbank.org/lpi).

Figure 9. Private Investment Trends, 1970-2008



Source: Bank Staff based on INS data

45. In the 11th NDP, the Government intends to sustain the reform momentum of the recent years. Indeed, several changes to the Tunisian tax system, including alterations to corporate taxation and the value-added tax, were introduced in 2007. The standard rate of corporation tax was reduced from 35 percent to 30 percent in order to increase the competitiveness and encourage investment. To encourage more firms to list on the local stock exchange, the corporate tax rate for listed companies was reduced to 20 percent. The top VAT rate of 29 percent imposed on luxury goods was abolished, reducing the number of VAT rates to three (18, 10, and 6 percent). The Ministry of Finance introduced a new option for paying taxes - "*téléliquidation*" that allow firms to file their tax returns online and determine the exact amount of their payment before paying the taxes at the tax office. Furthermore, a new Law on Economic Initiative enacted in December 2007 includes many provisions to ease business, including the abolition of the paid-in minimum capital requirement for limited liability companies, allowing minority investors to request a judge to call into question transactions judged contrary to the interest of the firm (protection of investors) and extending the scope of borrower's credit history at the central bank. Still, domestic private investment is quite sluggish in spite of its upward trend since 2006 and in spite of dynamic FDI (Figure 9). Indeed, Tunisia's private investment performance pales compared to East European competitors (18-19 percent in Bulgaria and Romania), fast-growing East Asian countries (28-30 percent),[14] and many MENA countries (Morocco 25 percent in 2007).[15]

46. A key objective of the 11th NDP is thus to go further in removing constraints to private operators in the onshore sector. The main axes of the reform agenda are: (i) reducing further administrative barriers to investment, including pre-authorizations to create a business, (ii) enhancing diffusion of information on market conditions and opportunities through an operational and accessible firm registry system, (iii) ensuring a better matching between labor supply and demand, (iv)reducing delays in access to industrial land and (v)enhancing the role and impact of the competition authorities.

FOSTERING THE DEVELOPMENT OF THE FINANCIAL SECTOR

47. **Banking sector**. Tunisia's 11th NDP acknowledges that for investors to exploit the opportunities offered by greater global integration, Tunisia will need to fix the lingering weaknesses of the banking sector. An important constraint to the capacity of the banking sector to finance the economy is the high level of non-performing loans (NPLs). Although they have declined over the last three years, they still stood at 17.4 percent in June 2008. Furthermore, the proportion of these risky loans provisioned is limited by international standards, as only 53.8 percent of them are provisioned on average. The key objective of the Government is thus to reduce the level of NPL and increase the extent to which those are provisioned. More specifically, the objective is to reduce the ratio of NPLs further to 15 percent and increase the percentage of NPLs provisioned to 70 percent by the end of 2009. To reach these targets, policies undertaken over the last two years by the Central Bank (*Banque Centrale de Tunisie* –

[14] Private gross capital formation increased at an average annual rate of 8.9 percent in Malaysia and 7.6 percent in Thailand after 1965.

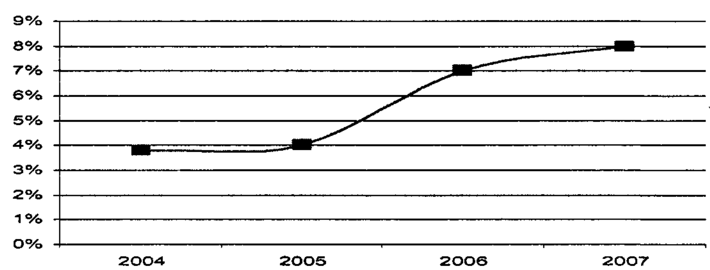
[15] Private investment averaged 20 percent in Morocco in 2001-2005.

BCT) will be continued. These include banning dividend distribution for banks with insufficient provisioning, making provisions fully tax deductible, and strengthening banking supervision.

48. In line with the 2006 Financial Sector Assessment Program (FSAP) Update, the authorities have taken initial steps to improve the credit culture, promote good governance, and strengthen the legal framework for banks. The BCT has been given (by a 2006 law) new powers to monitor the financial system, ensure alignment with prudential norms and regulations, enforce transparency, and supervise publication of financial and economic data. It also aims to bring regulation closer to Basel II norms. In preparing for the transition to Basel II by 2010, several preparatory measures to energize the banking sector were planned, some of which are adopted by now. For instance, the requirement that banks transfer their end-of-day foreign exchange balances to the Central Bank (*nivellement*) has been abolished, and banks can now manage up to 20 percent of residents' foreign exchange holdings without surrender requirements. Banking sector reform priorities in the coming years include (i) enhancing prudential norms in order to increase the capacity of the sector to finance the private sector and reduce risk of instability. This is expected to help reduce NPLs and increase NPLs provisioning; (ii) ensuring that Basel II prudential standards are adopted by 2010 and (iii) encouraging further bank mergers to reduce the fragmentation of the sector.

49. **Non-banking finance (securities and venture capital markets).** Partly due to the weaknesses of the banking system, non-banking finance is largely underdeveloped in Tunisia. It contributes to only 8 percent of gross capital formation (Figure 10). The stock market capitalization is only 17 percent of GDP in 2008, against around 90 percent in Morocco and 87 percent in Egypt and only 50 companies are listed in the stock market. The development of the securities market has been hindered by excessive reliance on easy bank financing for large companies, and by weaknesses in Tunisia's corporate sector (dominated by small family-owned firms and holdings). Other factors that have impeded the development of securities and venture capital markets are the limited scope of the privatization program so far, which has not privileged public offerings and remains timid in terms of opening the capital of public enterprises, and the limited role played by contractual savings and collective investment schemes.

Figure 10. Contribution of securities and venture capital market to gross capital formation



Source: EU's Security Market Study (2008)

50. As stated in the 11th NDP, the Government is keen in developing securities and venture capital and envisages a number of reforms. These include: (i) the revision of the regulatory framework of capital-risk institutions to transform them into real risk-takers (currently they operate mainly like banks, providing capital under pre-determined exit conditions); (ii) enhancement of fiscal and financial transparency, (iii) improving the functioning of the stock and bonds market and (iv) channelling more privatizations to the stock market in order to enhance the depth and liquidity of the latter. Government policies aimed at developing the capital market are an integral part of the objective of gradually opening the capital account. A strong capital market is a pre-requisite for opening the capital account. Other complementary policies involve a shift towards a floating exchange rate, fiscal consolidation and a new monetary policy framework (inflation targeting).

51. To address the need of micro-firms, the regulatory framework of micro-finance (today marked by the quasi-monopoly of *Banque Tunisienne de Solidarité*) also needs revision in order to allow the entry of more players in the market.[16] The limited scope of Government actions to fix the weaknesses of the non-banking finance sector largely explains the Government insistence in including that sector in the reform program supported by this loan.

IV. BANK SUPPORT TO THE GOVERNMENT STRATEGY

LINK TO CAS

52. The Bank's program in Tunisia is set out in the current Country Assistance Strategy (FY05-FY08) that was approved by the Board of Executive Directors in 2004. The CAS proposes three pillars:

- Strengthen the business environment to support the development of a more competitive, internationally integrated private sector and improve competitiveness of the Tunisian economy
- Enhance skills and employability of graduates and the labor force in order to prepare them for a knowledge economy
- Improve the quality of social services through enhanced efficiency of public expenditure.

53. The CAS Progress Report (CAS-PR) was completed in August 2007 and has concluded that the main development challenges and the CAS pillars remain valid. The CAS-PR laid out an indicative program for the FY08-10 period (Annex B3 of the CAS-PR) that proposed a fifth Economic and Competitiveness Adjustment Loan (ECAL V) for $150 million in FY09. This ECAL has been adapted into the ICL proposed here and continues the Bank's strategy of providing budget support as a core element of the Bank's program in Tunisia. The context of the global financial crisis led the Government to be prudent about its financing needs in 2009 and 2010 and to request a larger loan amount of $250 million. Indeed the Government is keen to avoid crowding out the private sector in the domestic market for finances by issuing large amounts in treasury bonds. The new Country Partnership Strategy (2010-2013) is currently being prepared and will reiterate the importance of pursuing reforms for accelerating the pace of growth, maintaining solid macroeconomic management and enhancing the incentives for increased private investment. Thus, while formally this program is set within the context of the 2005-2008 CAS and the CAS-PR with its indicative program for FY09-10, its content will feature prominently in the FY10-13 CPS which is being prepared. The ICL is a cornerstone of the Bank's support to reforms in growth and macro stability policy areas.

54. The ICL is designed to be fully complementary with the current lending portfolio, particularly in the area of export development through the synergies with the Second Export Development Project (which supports export development through trade facilitation and promotion). The ICL also creates significant synergies with the Bank's technical assistance activities in the area of trade, transport and logistics. The program also provides a platform for cooperation with other donors, as evidenced in the significant parallel technical assistance support provided to complement the ICL by the EC (trade logistics). Finally, the Government has used the ICL program as a vehicle for its own internal coordination on this agenda.

[16] A part from the BTS, there is only one player in the micro-finance market in Tunisia: Enda-Inter Arab, an international non-governmental organization.

COLLABORATION WITH THE IMF AND OTHER DONORS

55. The Bank has good collaboration with the European Commission (EC) as well as the African Development Bank (AFDB), both of which have a strong local presence in Tunisia. The IMF has no local office in Tunis and Tunisia has no formal program with the Fund, though relations are close. The Fund undertakes two Article IV missions a year and has technically assisted the Central Bank on monetary policy issues (e.g. inflation targeting). The IMF policy discussions as part of the recent Article IV Consultation mission (June 2008) centred on how to strengthen Tunisia's macroeconomic position and advance structural reforms to achieve higher growth and lower unemployment in the context of deeper integration to the world economy. More specifically, the discussions focused on: (a) consolidating the fiscal position; (b) adapting the monetary and exchange rate policy framework to the gradual liberalization of the capital account and transition toward inflation targeting; and (c) strengthening the financial system. The Bank has discussed with the IMF about the content of the program and will continue to do so in the near future. The Fund's Assessment Letter of the Government's reforms is in Annex 3.

56. The proposed ICL is being prepared jointly with the EC and the AFDB, building on the successful experience under the ECALs. Its formulation has allowed these institutions to deepen the policy dialogue with the Government on key economic issues. The ICL has also provided the vehicle for coordination between the World Bank, the EC and the AFDB and is expected to provide an additional US$200 from the AFDB and Euro 70 million from the EC in parallel financing on the basis of the same program matrix. All preparatory missions have been jointly conducted even if some flexibility was needed to respond to different internal processes. The EC and the AFDB have asked the Bank to play a leading role in the three institutions' communication with the Government and in elaborating a macro framework for this program.

RELATIONSHIP TO OTHER BANK OPERATIONS

57. The proposed ICL complements the Bank's other activities in Tunisia which encompass investment lending, AAA, technical assistance and a range of trust funds. The ICL serves as a vehicle for policy reform in critical growth-enhancing areas and is instrumental to enhanced policy dialogue and effective donor coordination.

58. The ICL would build on the achievements reached through the series of previous Bank loans which supported Competitiveness and Private Sector Development. The Economic and Competitiveness Adjustment Loan (ECAL) has successfully implemented its fourth phase. Through the first ECAL, Tunisia introduced wide-ranging first generation actions aimed at promoting private sector development; ECAL II supported improvements in the soundness, efficiency and competitiveness of the banking system. ECAL III consisted of a broad range of second generation measures aimed at enhancing private sector development; and ECAL IV has developed a set of policies including: (a) Fiscal policies, (b) Private Investment Climate Policies, including reduction in the number of prior authorization for private investors, and (c) Financial Sector Development Policies, including enacting a law on financial security that promotes financial transparency and aims at enhancing the quality of the financial statements of companies.

59. The ICL would also consolidate the results of the Export Development Project II which supports the development of exports through trade facilitation and trade promotion. It would also provide a platform for addressing reforms identified through ongoing dialogue and technical assistance in the area of trade logistics, access to industrial land and the business environment. Finally, it would also support and complement the Bank's ongoing dialogue on future operations (including a potential Export Development Project III) and analytical activities that will be identified during the elaboration

of the Country Partnership Strategy through identifying and addressing other key building blocks to enhanced competitiveness of the Tunisian economy.

LESSONS LEARNED

60. Lessons learned from implementing development policy loans in Tunisia and elsewhere show that country ownership of the proposed policies and actions is key for success. Country ownership is also emphasized in the draft CAS Completion Report (2008) as being critical for the success of the Bank's program. As a consequence, the ICL and the overall dialogue and program of the Bank in Tunisia are firmly embedded in supporting the objectives of the 11th National Development Plan.

61. A lesson from the experience in implementation of the ECAL reforms is that the Bank needs to be flexible, to allow sequencing of the reforms and to be sensitive to the country realities as regards the time-frame of reform implementation. This is particularly important given the uncertainties presented by the global financial crisis and the future impact of this on the economy. Accepting partial reforms in some areas and building on partial success to deepen them in subsequent operations paid off. Drawing from this, the proposed program focuses on reforms that are feasible politically in the timeframe of the program and will consolidate those set of reforms before broadening further. The ICL thus aims to pave the way for future reforms in areas where the level of dialogue and analysis is not yet mature or comprehensive enough to warrant specific reform measures.

62. The use of development policy lending is appreciated within Tunisia and will continue to remain central to the Bank's program. An important element is that the program aims to prioritize and tailor the expected results accordingly, especially because the Bank is just one of many development partners active in Tunisia. The Bank is currently elaborating its future Country Partnership Strategy (CPS) for Tunisia with the goal of continuing to prioritize areas where the Bank can provide most value-added and providing a package of services to reforms that includes lending, TA and other support.

ANALYTICAL UNDERPINNINGS

63. The proposed program is underpinned by a series of analytical work recently completed (Table 7). The Global Integration report played an important role in shaping the Government's program in trade and, through that, the content of this program. That study took stock of Tunisia's integration policies since the early 1970s, examined the key remaining integration challenges that the country's manufacturing sector is facing and proposed further reforms to enhance the competitive position of the country; and (ii) identified the specific policy reforms needed to realize the largely untapped potential in services. Using a well-focused regulatory questionnaire, the restrictions to entry, business, and trade in key backbone service sectors were calculated (telecommunication, banking, air transport, accounting, auditing, and legal services).

64. The Global Integration report found that Tunisia's economic sectors which are highly integrated to the global market have been able to attract investment, converge to EU's labor productivity standards, and boost job creation. On the other hand, the performance of domestic market-oriented firms (those in the onshore sector) has been lacklustre as evidenced by the slow growth of domestic private investment due to lingering business climate constraints (heavy administrative burden, difficult access to credit, unfair competition and anti-competitive practices). Finally, an important finding of the report is that Tunisia's trade integration drive has largely bypassed non-tourism service sectors, hence the slow pace of structural transformation of the service sector where the country has a large potential. This is mainly because many barriers to entry and competition are still prevalent there, reducing the scope for investment and trade, thus job creation.

65. The preparation of the program benefits also from a large number of other analytical work. These include two critical pieces: a Trade Logistics Services Policy Note (2008c) and two Policy Notes on Employment (World Bank 2007 and 2008b). The Trade Logistics Services Note summarizes the conclusions of a Bank technical assistance provided to the Ministry of Transport of Tunisia in 2007-2008, on the formulation of an Infrastructure and Logistics Services Development Strategy. If found that: (i) Tunisia's average logistical performance is insufficient and not meeting current challenges; (ii) important international and domestic infrastructures constraints in ports and logistics zones are prevalent; (iii) the dissemination of the culture of logistics in the private sector is limited due to insufficient skills and training; (iv) logistics services are fragmented, provided often by small operators using non-transparent procedures and that (v) several ongoing projects and reforms (customs code, concession, and deep water port, etc.) are key to bring about positive changes. The Note also proposes a policy and institutional reform agenda which is the basis of the measures proposed in this DPL on logistics.

66. The first Bank Employment Policy Note completed in 2007 has integrated the main conclusions from the Bank's multi-year program of economic and sector work program designed to address Tunisia's unemployment problem. It covered labor market regulations, social protection, and performance of the education system. The Policy Note derived important policy recommendations, mainly focused on the macro level, and supported (i) policies that focus on the accumulation of production factors, (ii) policies that enhance the ability of entrepreneurs to appropriate the returns on their investments and (iii) policies that promote innovation and productivity growth. The second Employment Policy Note in 2008 made use of new evidence, had a more micro-focus and made concrete and time-bound policy recommendations. It found, inter alia,: (i) a link between unemployment and entry barriers to formal markets; (ii) that skills supplied by the education sector do not fully match the demand of the labor market, in part because the education sector has difficulties responding; (iii) that there is a link between the rapidity of professional insertion and the fields of study, technical and engineering studies leading to much more rapid insertion than humanity studies in general and (iv) that most active labor market policy instruments are ineffective.

67. The other analytical pieces that have fed into the DPL policy dialogue are numerous, including the Development Policy Review (in finalization stage), the Small and Medium Enterprise Finance Study (in finalization stage), the FIAS Firm Enterprise study (just completed), and the 2006 Government's (IEQ) competitiveness study, and an EU-commissioned study on security markets in Tunisia, and so on. Furthermore, an intense dialogue on Tunisia's macroeconomic framework and outlook has occurred during the preparation of the program. The Government has sought feedback from the World Bank and the IMF on its macro projections and has taken into account Bank's comments. To enhance capacities in responding to shocks from the global economy and within the framework of 2009 budget preparation, a training course on development macroeconomics was delivered by the World Bank in October 2008.

68. The Government has also requested the Bank's technical assistance on tariff reforms to anticipate on reforms to be supported by this program. A well-attended TA workshop on tariff reform simulations and ex-ante analysis of the impact of tariff changes was delivered in September 2008. A follow-up module focused on the sectoral impact of tariff reform is scheduled. Finally, in order to implement one specific measure of the program, the unique identifier, the Government has requested Bank technical assistance within the framework of this program.

Table 7: AAA, TA and Project Activities Underpinning the Operation

Policy Area	AAA, TA and Project activities	Institution	Status
Macroeconomic framework	2007 and 2008 Article IV PEFA 2009 Development Policy Review Development Macroeconomics course Employment PESW 2008 Study on tax expenditure 2009	IMF EC/ WB/ AfDB World Bank World Bank World Bank WB/AfDB	Completed January 2009 Final stage Completed Completed Proposed
Trade integration	Global Integration Study 2008 Trade Logistics Study 2008 TA on tariff reform simulations 2008 TA and studies under Export Development Project II Firm Enterprise Competitiveness Study 2008 UTICA's Study on Services Trade 2006	World Bank World Bank World Bank World Bank FIAS/ WB UTICA (employers' union)	Completed Completed Completed Completed Completed Completed
Non-banking finance	Security Market Study 2008 SME Finance Study 2009 Study on the Impact of the *Banque Tunisienne de Solidarite* (Employment PESW) 2008 Study on micro-finance in Tunisia 2009	EU Commission World Bank World Bank EU Commission	Completed Being finalized Completed Proposed
Investment climate	IEQ's Competitiveness Report 2006 Doing Business 2008 and 2009 Competitiveness Study 2007	IEQ (Tunisian institute) World Bank/ IFC/AfDB	Completed Completed Completed

V. THE PROPOSED INTEGRATION AND COMPETITIVENSSS LOAN

OPERATION DESCRIPTION

69. The proposed DPL is squarely linked to the first strategic pillar of the Government's reform program (11th NDP), "accelerating growth". It is also linked indirectly to the "preserving macro stability" pillar given the strong correlation between pillar 1 and 2. The overall objective of the DPL would be to support efforts to deepen Tunisia's global integration and enhance the capacity of Tunisian firms to exploit the opportunities offered by greater integration. More specifically, the program would support mutually reinforcing development objectives:

- *Reducing trade transaction costs and deepening Tunisia's global integration;*
- *Further improving the business climate to encourage private investment and facilitate business operations and;*
- *Enhancing the development of the financial sector to increase its capacity to finance investment.*

70. The Bank has maintained a continuous dialogue in all the above policy domains and hence has a high degree of confidence regarding their strategic importance. Reforms in these mutually reinforcing policy areas will not only support growth, but also macroeconomic stability, which will be jointly monitored during supervisions. Moreover, policy reforms in the three areas above will pave the way for accelerating the structural transformation of the Tunisian economy. Indeed, weak integration of the services sector, weaknesses in the financial sector and lingering investment climate constraints are the main factors behind the sluggish trend domestic investment in Tunisia (World Bank 2008a).

71. Within each of the chosen policy areas, the Government has been keen in inserting only measures which are in the 11th NDP and which they are confident of being politically able to implement within the timeframe of the program. Thus the proposed program takes into account the lessons learnt from past programs in Tunisia which point to the desirability of not pursuing too many reforms too quickly, especially given the current country and global context. In the area of services sector integration, the ongoing bilateral trade liberalization negotiations with the EU explains the focus of the program on critical first steps to the future liberalization of Tunisia's services sector rather than bolder "opening" reforms, which could be supported by a future program. In sum, the scope of the program is deemed adequate given current circumstances and Tunisia's development partners share a high degree of confidence in the feasibility of the measures in the program's policy matrix.

LOAN AMOUNT AND TRANCHING

72. The Government is requesting a loan amount of US$ 250 million from the World Bank. The AfDB is expected to provide the same amount (US$250 million) and the EC plans to support the program through a 70 million euro grant in parallel financing. These three institutions will use the same matrix as the basis for disbursement of the loan and plan to disburse around the same time. The World Bank's first tranche is expected to be disbursed upon effectiveness whereas the second tranche would be disbursed upon the satisfaction of the second-tranche conditions as testified by an assessment of the progress made.

73. In terms of the program structure and tranching, initially, a programmatic approach with prior actions and triggers was proposed by the World Bank and other donors. Ultimately, given strong government preference, agreement was reached on a stand-alone, two-tranche operation, covering the period 2009-2010. The Government considers however this program to be the first in a series aimed at supporting Tunisia's global integration. In its indicative program for Tunisia, the EC has allocated a grant of 77 million euros for a possible follow-up program in 2011/2012.

POLICY AREAS

74. The program matrix (Annex 2) describes the logic of the program by showing for each of the three components of the program, the main axes through which the main objective is expected to be attained, the key actions and the specific measures to be implemented during the course of the program. The matrix shows two types of measures: (i) disbursement conditions that are considered as critical for the achievement of the program's objectives and (ii) accompanying measures that are intended to support each reform and set the stage for further reforms in subsequent operations. Moreover, to guide the supervision of the program, efforts were made to specify baselines and expected outcomes. Given that this is a two-tranche operation, the matrix is explicit about the measures to be implemented by the Government under each tranche.

75. The program includes six prior actions and 10 conditions of second tranche release. The total 16 conditions for this operation were chosen with three "best practice" principles in mind: (i) ownership (they are all in the government's 11th NDP), (ii) criticality (they are critical to the realization of the objectives of the program) and (iii) predictability (their effective implementation can be adequately monitored). The right balance has been struck between the critical importance of ownership, the required ambition of the reform program as well as realism and effectiveness of implementation within the timeframe of the program.

Box 1. Prior Actions and Second-tranche Release Conditions for Loan

Prior actions:

The government has agreed upon and implemented the following prior actions before the presentation of the loan to the Executive Board (see "policy areas" section for more details):

Prior Action 1. The Borrower's budget law for 2009 which revised the Customs tariff regime by reducing the number of Customs tariff rates from 9 to 6, including the tariff rate "zero", has been enacted

Prior Action 2. The Inter-Ministerial Council has adopted a draft law related to standards and quality norms applicable to all products imported or utilized in the Borrower's territory, consistent with international best practices

Prior Action 3. The Inter-Ministerial Council has adopted a draft Decree amending the Decree No. 2006-1826 dated June 26, 2006 regarding the National Council on Services (NCS), in order to: (i) mandate NCS to prepare a strategy for services development; (ii) formalize the creation of thematic commissions within NCS; and (iii) strengthen the role of the Permanent Secretariat of NCS through the establishment of a performance-based budgeting unit

Prior Action 4. The Inter-Ministerial Council has adopted a draft law amending the Urban and Regional Development Code (Code de l'aménagement du territoire et de l'urbanisme), in order to reduce the time necessary for businesses to acquire industrial land.

Prior Action 5. The Inter-Ministerial Council has adopted a draft Law amending the Law No. 95-44 dated May 2, 1995 regarding the Registry of Commerce, in order to ensure an effective updating of the information contained in such Registry

Prior Action 6. The Law No. 2008-78 dated December 22, 2008 has been enacted. Such Law amends the Law No. 88-92 dated August 2, 1988 regarding venture capital companies (Sociétés d'Investissement à Capital Risque), and mutual venture funds (Fonds Communs de Placement à risque), in order to: (i) encourage venture capital companies' risk taking by eliminating pre-determined exit conditions and basing exit from financed projects on the performance of the venture capital company at the time of the exit; (ii) simplify taxation of venture capital companies; (iii) encourage venture capital companies to invest in regional development areas; (iv) eliminate the requirement that mutual venture funds must liberate the totality of the subscribed funds in order to benefit from tax exemption.

Second-tranche release conditions:

Since this is a two-tranche operation, the following second-tranche release conditions apply (for details please see the "policy areas" section and the Program matrix in annex 2):

Condition 1. The Borrower's budget law for 2010 which shall revise the Customs tariff regime by reducing the number of Customs tariff rates from 6 to 5, including the tariff rate "zero", shall be enacted

Condition 2. The Ministry of Commerce shall put in place a system of selective management of imports control based on the risks presented by the imported products and the importers in order to allow speedier controls for non-risks products and importers.

Condition 3. The Customs Authorities and the Rades Port Authorities shall make the first one-stop trade control procedures office (guichet unique) at Rades Port operational and the Ministry of Transport shall make the electronic platform (liasse transport) which shall connect all operators in the transport chain operational.

Condition 4. The Inter-Ministerial Council shall adopt an action plan to reform the regulatory framework of the services sectors, to be prepared on the basis of a regulatory assessment to be carried out by NCS

Condition 5. The Prime Minister shall sign an executive order (arrêté) reducing by half the number of activities where operators are required to obtain a prior authorization in order to start their businesses.

Condition 6. The Inter-Ministerial Council shall adopt an action plan for the establishment of a unique common identification number for businesses to be used by the National Statistics Institute, the tax authorities and the social security authorities, based on a feasibility study to be conducted with the support of the Bank.

Condition 7. The Competition Council shall be requested by the relevant sector Ministries to conduct a regulatory and competition assessment of businesses in two new sectors within the services sector

Condition 8. The Central Bank of Tunisia shall publish statistics for 2010 that shall show a decrease in the rate of non-performing loans to fifteen percent (15%), and an increase in provisioning of non-performing loans to seventy percent (70%)

Condition 9. The Stock Market shall publish its annual reports that shall show an increase of the stock market capitalization to at least twenty percent (20%) of the Borrower's Gross Domestic Product, due in particular to the increased number of privatizations implemented through the stock market

Condition 10. The Borrower shall adopt institutional and regulatory provisions in order to improve the performance of the Borrower's micro-finance market, to be adopted on the basis of a study to be carried out by the Ministry of Finance.

The prior actions and second-tranche release conditions are discussed in more detail in the paragraphs 78 to 103.

Reduce Trade Transaction Costs and Deepen Trade Integration

76. The main objective of this component is to reduce trade costs and deepen Tunisia's integration through the following three axes, which are all critical elements of the government trade integration program:

- Deepen international integration for trade in goods
- Strengthen the effectiveness of trade facilitation and logistics services
- Foster trade in services

77. The prior actions for this component are (see more complete formulations in box 1 above):

- Reduce the number of tariff bands (including the zero rate) from 9 to 6
- Adopt a law related to product standards and quality norms applicable to all products imported or utilized in Tunisia
- Adopt a draft Decree amending the Decree No. 2006-1826 dated June 26, 2006 regarding the National Council of Services in order (i) mandate NCS to prepare a strategy for services development; (ii) formalize the creation of thematic commissions within NCS; and (iii) strengthen the role of the Permanent Secretariat of NCS through the establishment of a performance-based budgeting unit.

78. **Reduction of tariff bands** continues reform efforts by the Government over the past five years, and will involve a further reduction in tariffs on imports from non-preferential partners. Challenges arising from this trade liberalization are related to possible reductions in tariff revenues and adjustment needs of domestic producers. Regarding tariff revenues, they now represent a small share of the budget (3 percent) as the Government successfully managed to increase corporate and income taxes to compensate for declining tariff revenues. The Bank has worked through a technical assistance program with the Ministry of Finance to develop a hands-on tariff reform simulation tool tailored to the envisioned reforms in order to help the authorities to better anticipate the likely fiscal and economic effects of tariff reform. The simulations show that tariff reduction is good for consumers and overall welfare while the adversely affected sectors — wood and paper products, metals and products, and transport equipment — would see only a small contraction in output of less than 10 percent over 10 years that is expected to be more than compensated for by the output expansion in export-oriented sectors.

79. Moreover, the Government has a number of well-developed trade assistance programs at its disposal to assist vulnerable domestic producers, as Tunisia has just completed the transition towards a free trade area with the EU in January 2008. The expected outcomes of the planned reforms are that the tariff structure of Tunisia will be simplified, the average level of protection will be reduced and trade will be more diversified. In particular, it is expected that the simple mean of most favored nation import duties at the Harmonized System 6 digits level will drop from 21.7 percent in 2008 to less than 18 percent in 2010. This fall in MFN tariffs will reduce the wedge between preferential and generally applicable tariffs, and as a result will tend to lower adverse impacts from trade diversion and incentives for fraud on product origin and smuggling.

80. **The second prior action, adoption of a draft law on product standards and quality norms**, is a critical step in Tunisia's convergence to EU norms and standards and deeper integration following the completion of the duty free area in manufacturing in January 2008. The legislative reform and subsequent implementation has been an administrative challenge and a considerable burden on the respective service within the Government, but preparations are well under way and the agencies involved are committed to a quick and thorough application of the new regulations. The resulting changes in norms and standards might involve adjustment costs for some enterprises that have based

their production processes on the existing regulatory framework, but for many firms, especially those producing for export to the EU, the regulatory reforms will lower compliance costs.. The major expected outcome from this law (together with accompanying measures identified in the program matrix) is to make it possible for Tunisia's standards and quality norms to converge to international best practices. It is expected that the number of divergences (109 in 2008) will falls by more than one third by the end of 2010. While this reform falls under the Tunisia-EU integration deepening agenda, the Government is committed to apply the reform in a non-discriminatory manner.

81. **The third prior action concerns the revision of the decree No. 2006-1826 of 26 June 2006 regarding the National Council of Services (NCS)** in order to prepare a strategy for services development; formalize the creation of thematic working groups; and strengthen the role of the Permanent Secretariat. The aim of this measure is to support initial steps in fostering services exports in the sectors where Tunisia has demonstrated its international competitiveness in recent years (e.g., medical and paramedical, legal, accounting, and engineering services) and to provide the Government of Tunisia with the institutional and analytical tools necessary to elaborate and implement an export promotion strategy for services trade. The main challenge will be to ensure that a sufficient number of services experts can be recruited for the Permanent Secretariat, and that regular, effective consultations with other ministries concerned and private sector counterparts can be undertaken within the NCS. But to address this challenge, the Ministry of Trade has already identified a number of suitable experts and the fact that the Permanent Secretariat will likely be moved to and hosted within a new results-oriented management unit in the Ministry of Commerce should strengthen interest and ownership of the various stakeholders. The expected outcome is that the consultation process between the government agencies and private sector representatives concerned will improve, as measured by the number of meetings organized annually, including sessions of thematic working groups that is expected to double between 2008 and 2010.

82. Second tranche disbursement conditions are (see box 1 for complete reference):

- Tunisia's budget law for 2010 which shall revise the Customs tariff regime by reducing the number of Customs tariff rates from 6 to 5, including the tariff rate "zero", shall be enacted
- The Ministry of Commerce shall put in place a system of selective management of imports control based on the risks presented by the imported products and the importers in order to allow speedier controls for non-risks products and importers;
- The Customs Authorities and the *Rades* Port Authorities shall make the first one-stop trade control procedures office (guichet unique) at *Rades* Port operational and the Ministry of Transport shall make the electronic platform (liasse transport) which shall connect all operators in the transport chain operational;
- The Inter-Ministerial Council shall adopt an action plan to reform the regulatory framework of the services sectors, to be prepared on the basis of a regulatory assessment to be carried out by NCS.

83. The first disbursement for the second tranche, i.e. the **reduction of the number of tariff bands** from six to five, is a continuation of the trade policy reforms discussed under Prior Actions, and the analysis of challenges and outcomes applies correspondingly.

84. The second disbursement condition concerns the implementation of a **system of selective import control management**. The main challenge for the effective implementation of this measure consists of overcoming the reluctance of agents in charge of border control to accept a risk-based control ratio of less than 100 percent as providing sufficient security. This challenge will be addressed through information and training events organized by the respective services. The expected outcome is that cost and delays due to technical controls will be reduced. It is expected that the share of imports transactions subjected to technical controls will decrease from 100% in 2008 to less in 2010.

85. The third disbursement condition refers to the operationalization of a **one-stop shop on trade control** procedures at Radès port, and the establishment of an **electronic platform** for trade documents ("liasse de transport"). The port of Radès is Tunisia's largest port, handling 90 percent of national merchandise container traffic and 22 percent of total maritime traffic. The challenge here is that these reforms require the collaboration of all the agencies that are intervening at the border, and some agencies seem to date better placed than others to put the systems in place on time. But the Government has indicated its determination to work with all the agencies in order to achieve the objectives in a timely manner. The measure is among the "Presidential Measures" announced in December 23rd, 2008. The building construction of the one-stop shop has begun and is advanced and preparatory legislative work is underway. The expected outcome from this reform is that delays between entry and exit in the port of Radès will be reduced. It is expected that the average time of port clearance will fall from 5.6 days in 2008 to less than 3 days in 2010.

86. The fourth disbursement condition calls for the adoption of an action plan for a **regulatory reform of services sectors** based on the regulatory diagnostics. This measure is aimed at upgrading the capacity and capability of firms in services sectors with strong export potential. The main implementation challenge results from the very specific profiles and needs of firms in the target sectors (e.g., medical and paramedical, legal, accounting, and engineering services) and correspondingly different upgrading requirements. In order to address this challenge, the Government is developing an information system that will comprise statistics on sectoral characteristics and trade flows, as well as documentation on the regulatory environment. The expected outcome is that the reform program will be allocated sufficient funds to carry out envisaged activities such as advisory services and financial support for firms in the target sectors and that at least three activities proposed in the action plan are reflected in official documents.

Further Improve the Business Climate

87. The objective of this component is to further improve the business climate through the following three axes, also all critical elements of the government's program in the area of investment climate:

- Ease business entry and operations
- Strengthen the application of the competition law
- Improve regulation and information on labor

88. The prior actions for this component are:

- The Inter-Ministerial Council has adopted a draft law amending the Urban and Regional Development Code (Code de l'aménagement du territoire et de l'urbanisme), in order to reduce the time necessary for businesses to acquire industrial land;
- The Inter-Ministerial Council has adopted a draft Law amending the Law No. 95-44 dated May 2, 1995 regarding the Registry of Commerce, in order to ensure an effective updating of the information contained in such Registry.

89. The main objective of the **revision of the urban code** is to reduce the complexity and time cost involved in accessing industrial land. The government has already taken measures to increase the supply of industrial land but an important issue is the current complexity of the procedures involved in dividing up existing lots in industrial zones. In effect, lots are standardized and are often too large for the needs of firms. A revision of the relevant articles of the Urban Code would make it easier to divide lots into several smaller parts and would therefore greatly improve the attractiveness of industrial zones for firms and improve access to land for business use. The expected outcome is that by 2010, the average delay for approving an industrial zone outside of the areas with existing urban development plan will be reduced from three year and half in 2008 to 6 months (average delay

reduced by 3 years!). Furthermore, the average delay for allotting land within an approved industrial zone would be cut by 6 months.

90. The objective of the new legal framework on the **Registry of Commerce** is to allow for the building an integrated, up-to-date electronic registry and making it operational. Existing firms' registries are regionally-based (from the statistics bureau, the Chamber of Commerce, the tax administration, etc.) and are outdated and display large mismatches across sources. This is a major impediment since information on firms in operation is key to adequate policymaking, essential for business development and important for transparency and governance. The expected outcome of this reform is that the business registry will be improved, as measured by the number of companies recorded with updated data and the number of online consultations of the registry. This prior action would also prepare the ground for the subsequent creation of a unique identification system across different public agencies (see second tranche condition for this component).

91. The second-tranche disbursement conditions are :

- The Prime Minister shall sign an executive order (arrêté) reducing by half the number of activities where operators are required to obtain a prior authorization in order to start their businesses
- The Inter-Ministerial Council shall adopt an action plan for the establishment of a unique common identification number for businesses to be used by the National Statistics Institute, the tax authorities and the social security authorities, based on a feasibility study to be conducted with the support of the Bank.
- The Competition Council shall be requested by the relevant sector Ministries to conduct a regulatory and competition assessment of businesses in two new sectors within the services sector.

92. The **reduction of prior authorizations** is a continuation of a policy that has been implemented for years and supported by similar programs. Under ECAL IV, the list of activities subjected to prior authorization was brought down to 115, from 225. Under this program, the number of remaining authorizations would be reduced to 48 by 2010 and replaced with the requirement to comply with the terms and conditions of specified business conduct rules ("cahier des charges"). The Government has already established lists of activities concerned and has started working with the professions. A challenge would be to select the activities where prior authorizations present big constraints and result in large forgone investments. The Government's objective is to boost private investment and private sector development and that the focus will be on the most important sectors. The expected outcome of this reform (along with accompanying measures identified in the program matrix) is that the growth of the number of companies created in the sectors where prior authorizations have been eliminated will be superior to the national average.

93. The adoption of an action plan for the establishment of the **unique identification number** is a key building block to a reform crucial for transparency and governance. A unique identification number for businesses to be used by the National Statistics Institute, the tax authorities and the social security authorities would go a long way in enhancing fiscal revenue and transparency. The main challenge is however that this measure requires the collaboration of several entities within the government and is a challenging reform to implement technically. It is also a politically challenging reform as many will resist the reform within the Government and protection of private data provisions is another obstacle. The Government has requested a TA from the Bank to help bring international experience on how to implement this. The expected outcome from this measure is the identification by a government's official document of the institution in charge of the implementation of the unique identification number.

94. The third disbursement condition calls for the **Competition Council** to conduct a regulatory and competition assessment of businesses in two different services sectors, by a request from the Government Authorities. Since its creation in 2005, its financial and administrative independence has been reinforced but its activity and impact in services sectors have remained limited. The objective of the proposed measure is to foster competition, which will in turn contribute to increasing productivity and enhancing competitiveness of Tunisian firms as well as encouraging private sector investment. Strengthening the role of the Competition Council is a key component of this objective. The main challenge concerns the limited human resources of the Council and will be overcome by another measure supported by the ICL program (see program matrix) and designed to increase the number of rapporteurs in 2009 and 2010. The expected outcome is that anti-competitive practices will be reduced in the two sectors where the Competition Council has conducted an assessment. Bank's supervision missions will review the results of the assessments conducted by the Council and monitor whether the sectoral competition assessments contain concrete actionable recommendations on pro competitive policy or regulatory changes

Enhance the Capacity of the Financial Sector to Finance Investment

95. The objective of this component is to strengthen the financial sector with a strong focus on non-banking finance. It is pursued through the following four pillars:

- Improve the performance and the risk management of the financial sector
- Enhance the development of venture capital and regulated mutual funds
- Strengthen the Tunis Stock Exchange depth and liquidity
- Develop the microfinance market in Tunisia

96. The prior action for this component is:

- The Law No. 2008-78 dated December 22, 2008 has been enacted. Such Law amends the Law No. 88-92 dated August 2, 1988 regarding venture capital companies (Sociétés d'Investissement à Capital Risque), and mutual venture funds (Fonds Communs de Placement à risque), in order to: (i) encourage venture capital companies' risk taking by eliminating pre-determined exit conditions and basing exit from financed projects on the performance of the venture capital company at the time of the exit; (ii) simplify taxation of venture capital companies; (iii) encourage venture capital companies to invest in regional development areas; (iv) eliminate the requirement that mutual venture funds must liberate the totality of the subscribed funds in order to benefit from tax exemption.

97. Tunisian SICARs (venture capital companies) currently operate like banks, providing capital under pre-determined exit conditions. The objectives of **amending the law on SICARs** are to make exit conditions dependent on the actual performance of firms and not on a predetermined price ("contrat de portage"). The challenge is that the success of the implementation is in the hands of the banks as most of the SICARs are owned by banks. The banks would probably overcome some of their reluctance by investing more resources in the training of their specialized staff and their potential clients on venture capital financing. The expected outcome of this new legal framework is that it will encourage SICARs' risk taking and enhance access to non-banking finance to accompany firms' development as measured by the volume of projects financed. Another objective of the law is to support regional development of SICARS outside of Tunis. The challenge here will be to convince the SICARs to invest in regional projects based on return on investment. The new law will also include provisions to improve return on investments for the FCPR.

98. The second-tranche disbursement conditions are :

- The Central Bank of Tunisia shall publish statistics for 2010 that shall show a decrease in the rate of non-performing loans to fifteen percent (15%), and an increase in provisioning of non-performing loans to seventy percent (70%).
- The Stock Market shall publish its annual reports that shall show an increase of the stock market capitalization to at least twenty percent (20%) of the Borrower's Gross Domestic Product, due in particular to the increased number of privatizations implemented through the stock market.
- The Government shall adopt institutional and regulatory provisions in order to improve the performance of the Borrower's micro-finance market, to be adopted on the basis of a study to be carried out by the Ministry of Finance.

99. Reducing the rate of **non-performing loans** (NPLs) to 15 percent and increasing **provisioning** to 70 percent are crucial to shore up the banking system and enhance its competitiveness and effectiveness. With the growing global financial crisis facing all economies, the challenge will be, on the one hand, to stick to these targets and to implement a dynamic approach to reducing NPLs, including a better risk management system and, on the other hand, to avoid a credit crunch which could lead to higher level of companies defaulting and therefore higher level of NPLs. An added risk would be related to the consequences of the global financial crisis on the tourism sector, which could inflate NPLs. However, the Central Bank remains confident that these targets will be met, given past trends and the effectiveness of their NPL-reducing plan. The expected outcome would be to strengthen bank's balance sheets and put access to finance on a strong footing, so the intermediation margin would fall from its baseline level (2007).

100. The increase in **stock market capitalization** rests critically on revitalizing the privatization process through the stock exchange. The objective is to significantly develop the capitalization of the stock exchange with a target of at least 20 percent of GDP by the end of 2010. This is sought primarily through a shift in the Government's mode of privatization of public enterprises. The Government is determined to channel a large proportion of planned privatization operations through the stock market and to open partially the capital of some public enterprises to the public. The challenge here lies in the feasibility of the privatization process with a market under the stress of the actual financial crisis. However, the government is committed to pursue these objectives. The expected outcome is that the depth and the liquidity of the financial market will be reinforced.

101. The third disbursement condition refers to the development of the **market for microfinance.** In Tunisia, the Microfinance Law currently provides that the only legal entity that can carry out micro-lending activities is the BTS (*Banque Tunisienne de Solidarité*) through a network of microcredit associations to which it provides finances. Close to 90 percent of microfinance clients are served by the BTS, the remaining borrowers are being served by a micro-lending program operated by an international NGO, currently operating outside the law under permission by the Tunisian Authorities. This legal and regulatory framework poses major constraints to the development of microfinance activities, including interest rate caps imposed on all relevant types of lending and lack of competition. The objective of the measure supported by the ICL program is to reassess institutional and regulatory arrangements with the view to increase the effectiveness of microcredit provision. The main challenge would be to build strong ownership of these reforms among Tunisian stakeholders who prefer this status quo. This challenge will be addressed by making sure that the study carried out in 2009 is undertaken by an independent expert with relevant international experience and good knowledge of particularities of the Tunisian model. The expected outcome is that new institutional and regulatory measures will support the establishment of a level playing field for different players and make it possible for these players to offer their services to different segments of the microfinance market.

Box 2. Good Practice Principles for Conditionality

Ownership - Reinforce ownership
The Government's program supported by this operation is well articulated in Tunisia's 11^{th} NDP. The Government's strategic vision is to (a) accelerate the pace of growth in order to reduce unemployment, boost incomes, and consolidate Tunisia's progress in the reduction of poverty; (b) Preserve macroeconomic stability; (c) uphold social achievements and human development; and (d) Preserve natural resources. All the measures supported by this operation fall under (a) and (b). The policy actions supported by this operation are basically measures identified with the Government to reach specific outcome targets of the 11^{th} plan. They focus on key measures that the Government believes are necessary and politically possible.

Harmonization - Agree up front with the government and other financial partners on a coordinated and accountability framework

The program is jointly supported by the World Bank, the African Development Bank and the European Commission and there has been very effective collaboration between these development partners throughout its preparation. The content of the program and its underpinnings have thus been naturally coordinated with institutions. The policy matrix was carefully discussed and coordinated

Customization - Customize the accountability framework and modalities of Bank support to country circumstances

The policy matrix reflects the Government's priorities and lessons learnt by the three institutions in supporting similar programs of the Government. The Bank has been flexible in both the loan amount, Government preference in terms of tranching and preparation schedule. With the global financial crisis context, the Bank is moving quickly to accompany the Government's commitment to accelerate reforms in this context.

Criticality - Choose only actions that are critical for achieving results as conditions for disbursement

The Government has asked the Bank to maintain the focus of this program on three areas: trade integration, business climate and financial sector, i.e., all crucial part of the Government growth and job creation program. This focus allows the Bank's efforts to be more effective and to choose prior actions and second-tranche conditions that are both critical to the success

Transparency and Predictability - Conduct transparent progress reviews conducive to predictable and performance-based financial support

The selected prior actions and second-tranche disbursement conditions can be effectively monitored, providing predictable and performance based financial support. Tunisia has always strived to implement all the measures of its program matrix in the past, not to mention prior actions and disbursement conditions. Recourse to waiver has been exceptional in the past.

VI. OPERATION IMPLEMENTATION

POVERTY AND SOCIAL IMPACTS

102. The actions supported by this operation-- enhancing Tunisian firms' competitiveness through reducing trade transaction costs, increasing access to finance and enhancing the business climate are expected to support growth and provide employment opportunities for the youth and university graduates (one of the key objectives of the Government). In other words, to the extent that the reforms succeed in helping Tunisia withstand the consequences of the global financial crisis and in increasing growth in the medium term, employment opportunities should increase and the poor should benefit.

Generally speaking, faster growth would lead to increased job creation, thereby supporting household income (7 percent of the population is considered as poor).[17]

103. More specifically, the program does not support any reforms that are expected to have significant negative impact on the poor and a Poverty and Social Impact Analysis (PSIA) was considered not to be warranted. At this stage, there are no specific measures aimed at changing subsidies (which are a central element of Tunisia's public finance program) although this would of course present an important need for PSIA if reforms were to be carried out in the future. The tariff reform—reduction of tariff bands and of non-preferential tariff rates- will, with a high degree of probability, benefit the poor through lower prices of clothing, footwear and other items that feature prominently in low income consumption bundles.

104. The distributive effects of tariff reforms were analyzed thoroughly in the World Bank Global Integration Study (World Bank 2008a). The starting point of the analysis is that Tunisia's main tariff issue is its dispersion, in particular the large gap between preferential and non-preferential tariffs. For instance, the tariff vis-à-vis the EU, where Tunisia derives 60 percent of its imports, is zero for industrial goods compared to 21.6 percent for non-preferential partners. Simulations in the GIS showed that the welfare cost of tariff dispersion now dominates gain from further preferential tariff dismantling. Tariff gaps indeed create a trade diversion phenomenon and fuel fraud and parallel markets. Gradually reducing tariff gaps is therefore overall welfare-enhancing.

105. However, while tariff reduction is good for consumers and welfare overall, it will affect Tunisia's economic sectors differently. The GIS found that the worst affected sectors — wood and paper products, metals and products, and transport equipment — would see a contraction in output of less than 10 percent after about ten years as a result of cutting tariffs on imports from non-EU sources by 25 percent (much higher than the implicit 17 percent tariff reduction supported by the program). The report found that even when import competing sectors contract in response to tariff cuts, the production units that remain are more competitive, and can also improve their export performance, albeit sometimes from a very low base.

IMPLEMENTATION, MONITORING AND EVALUATION

106. **Implementation and coordination responsibilities**: The responsibility for implementing the program in Government rests with the Ministry of Development and International Cooperation which will coordinate all relevant activities with other Ministries. The Government will take the lead in monitoring progress in implementation, both in the context of this operation as well as in the overall context of the NDP implementation.

107. **Supervision by the Bank:** Regular supervision will allow the Bank to continue providing policy advice and technical assistance to the institutions involved in the implementation of the program of reform. The Bank will continue to maintain continuous dialogue with the relevant Government ministries and will conduct regular reviews in close collaboration with other partners. This will take the form of joint missions with the EC and the AfDB and shared analytical underpinnings.

108. **Monitoring and Evaluation:** The monitoring and evaluation of the program and its expected results will be fully embedded in the M&E framework of the NDP. The World Bank and other development partners will continue to provide support to the Government to strengthen M&E, improve data quality and management and enhance capacity for using development outcomes to inform policy making. The Bank's program of investment lending incorporates aspects of M&E in

[17] According to the World Bank Global Poverty numbers recently released. The Government's official poverty incidence number is 3.8 percent. This is however based on a low poverty line (1.2 dollar a day).

each of the sectoral operations and it also administers trust funds in support of M&E; this work will naturally feed into the overall dialogue on the ICL.

FIDUCIARY ASPECTS

109. The Country Financial Accountability Assessment (CFAA), a core diagnostic undertaken by the Bank in 2004, shows that the fiduciary framework of the Government of Tunisia is basically sound and provides a strong control environment. The main findings of the CFAA are that the Tunisian public financial management system is reliable and that the related fiduciary risk is low. The complete budget process (preparation, planning, and negotiation with line-ministers) is sound. The budget execution is also of good quality and reliable.

110. The reporting and accounting are reliable, even though there is a room for improvement and modernization; the computerization of the budget and accounting is rather simple, but well spread among the public operators and its architecture allows a timely reporting. The cash and debt managements are made in a professional way, due notably to a strong technical assistance of the Bank. The whole area of control and audit is comprehensive and reliable, but still lacking sufficient public disclosure, notably for the annual report of the Cours des Comptes which is only partially disclosed.

111. Although the CFAA was conducted about five years ago, yearly CPIA assessments based on Bank expert knowledge continue to point to a low fiduciary risk. However, the CFAA did identify a few areas of improvements that are still relevant. As part of the DPL dialogue, the Government has accepted to launch a PEFA in the first quarter of 2009 with the support of the World Bank and the EC. This planned exercise will be an opportunity to assess the progress on the PFM reform agenda and would be used by the Government to monitor areas where performance will need to be improved.

DISBURSEMENT AND AUDITING

112. The proposed loan will follow the Bank's disbursement procedures for development policy support and will be disbursed in two instalments. Once the loan is approved by the World Bank's board and becomes effective, the proceeds of the loan will be disbursed in compliance with the stipulated tranche release conditions. Once the loan is approved by the Board and becomes effective, the proceeds of the first tranche will be deposited by IBRD in an account designated by the Borrower and acceptable to the World Bank at the Central Bank of Tunisia at the request of the Borrower. The proceeds of the second tranche will be deposited after all the conditions of the second tranche release are met. The Borrower should ensure that upon the deposit of the Loan into said account, an equivalent amount is credited in the treasury current account at the Central Bank. The approved tranches releases will not be tied to any specific purchases and no procurement requirements. The administration of this loan will be the responsibility of the Ministry of Finance.

113. The Borrower will report to the Bank on the amounts deposited in the foreign currency account and credited to the budget management system. If the proceeds of the loan are used for ineligible purposes as defined in the Development Loan Agreement, IBRD will require the Borrower to promptly upon notice refund an amount equal to the amount of said payment to IBRD. Amounts refunded to the Bank upon such request shall be cancelled. The administration of this loan will be the responsibility of the Central Bank.

ENVIRONMENTAL ASPECTS

114. The ICL program is a development policy loan in support of a program of reforms for which the environmental requirements of OP/BP8.60 apply. Overall, policies supported by the proposed loan are not likely to have any significant direct effects on the environment and natural resources and safeguard policies (such as OP 4.01 Environmental Impact Assessment) do not apply to this operation.

115. There is however one measure supported by the ICL program whose possible environmental impact deserves attention. The measure is related to the revision of the urban code, which is intended to allow for the creation of smaller lots of industrial land in order to reduce the time required to obtain industrial land. Tunisia's legal framework provides for the necessary measures to monitor and mitigate the likely effects of the new lots allocation system on the environment or natural resources of Tunisia. Article 11 of the urban code and decree No. 2005-1991 dated July 11, 2005 provide that, depending on their size, all types of adaptation or construction work are subject to either a prospective impact evaluation study or a set of specific rules determined by the Ministry of Environment. Based on the findings of the impact evaluation study, the Ministry of Environment might request modifications of the proposed work in order to avoid or mitigate any impact on the environment. Tunisia's legal framework in the area of environment thus provides for reasonable safeguard for avoiding/mitigating the possible negative environment impact of the revision of the urban code.

RISKS AND RISK MITIGATION

116. At this critical juncture, the program faces two main risks. The first risk is related to the direct impact of the global financial crisis on Tunisia's growth and development. Slow growth in Europe is bound to affect Tunisia through various channels, chiefly exports, FDI and remittances. Growth in Tunisia may thus slow down.temporarily or persistently, depending on the duration of the recession in Europe. By accelerating the series reforms through this program, the Government expects to mitigate the potential growth risk from EU contagion. The Government's strategy is to recognize that Tunisia's economy is small compared to the European market, and that enhanced competitiveness in these difficult times may help Tunisia seize opportunities out of the global crisis. In addition, Tunisia's development partners have come together to provide a common platform of support to help the country respond to the more difficult external environment.

117. The second risk relates to the expected response of the private sector to the reforms which may be slow or muted given the global economic uncertainties. This would translate into lower increases in private investment. To mitigate this risk, the Government expects to step up investment climate reforms, support access to finance for enterprises and improve its communication strategy in order to enhance private investment. Furthermore, as discussed above, Tunisia's offshore sector has an exceptional "enclave" business environment, and is expected to continue to attract FDIs.

118. Yet, other risks to growth and this program's objectives cannot be ruled out. These include droughts, regional instability and concerns of terrorist attacks in the Maghreb Region. Regional insecurity could affect Tunisia in the coming years, with tourism failing to reach the expected levels, and Tunisia losing some of its attractiveness for foreign investors. On the other hand, drought typically reduces agricultural output significantly and can claim up to 1 percentage point of growth. However, as shown in the macroeconomic section of this document, Tunisia has been extremely resilient to these types of shocks and the economy has always rapidly rebounded thanks to pro-active macroeconomic policies and continuous structural reforms.

119. Major risks related to the implementation of specific program components are not foreseen because the reforms are mature, underpinned by sound analytics, supported by technical assistance

(for instance tariff reform) and widely discussed within the Government and with donors. The synergy between reform areas is crucial. For instance, developing non-banking finance will critically depend on the pace of reforms in the banking sector advancing well. Indeed, the banking sector overwhelmingly dominates the financial sector and is the largest player in the non-banking segment of the financial sector. Rapid progress on banking reform measures is thus needed for an impact of non-banking finance measures. In particular, the level of non-performing loans should decrease from their current level (17.4 percent) and the 2006 banking law should be fully implemented.

120. The proposed program provides a key underpinning to the results-based framework in the new CPS that is under preparation. Policy dialogue with the Government in the context of the preparation and implementation of the CPS should help maintain the reform momentum to achieve the key expected outcomes and thus mitigate some of the risks attached to specific components of the program. The Bank will continue to work with the government of Tunisia to design and implement tailored technical assistance program as needed to ensure effective implementation of the proposed reforms.

ANNEX I: LETTER OF DEVELOPMENT POLICY

REPUBLIQUE TUNISIENNE
MINISTERE DU DEVELOPPEMENT ET DE
LA COOPERATION INTERNATIONALE

LE MINISTRE

09-055

17 février 2009

Monsieur Robert B. Zoellick
Président du Groupe de la Banque Mondiale
Washington, DC

Lettre sur la politique de développement

Monsieur le Président,

Le processus de développement de la Tunisie a été marqué par l'importance des progrès enregistrés au plan de la libéralisation et la modernisation de l'économie, la valorisation des ressources humaines, la consolidation du bien-être social et l'avancement sur la voie de la consécration des fondements du développement durable ; autant d'acquis qui ont favorisé l'accès de notre pays à des rangs avancés dans le peloton des pays émergents.

Ces performances ont pu être réalisées grâce aux efforts consentis et à la détermination affichée en vue de persévérer sur la voie des réformes dans différents domaines économiques et sociaux garantissant la continuité et l'efficacité de l'œuvre de développement et contribuant à améliorer la capacité du pays à relever les défis et à résister aux chocs exogènes.

La Tunisie, qui a entamé depuis l'année 2007 l'exécution du XIème plan de développement pour la période (2007-2011), se trouve confrontée à un environnement international contraignant marqué par l'exacerbation de la concurrence au niveau mondial surtout avec le démantèlement des accords multifibres à partir de 2005, la hausse importante des prix des hydrocarbures et des produits de base à partir de 2007 et plus récemment le déclenchement de la crise financière internationale, qui a rapidement engendré une récession économique notamment dans les pays développés.

1 Place Ali Zouaoui - 1069 Tunis

La sphère réelle de l'économie tunisienne a subi les contrecoups de cette crise du fait du repli de certaines activités exportatrices en liaison avec la contraction de la demande internationale, notamment en Europe. Face à cette situation et afin de soutenir les entreprises touchées par la crise, d'appuyer l'activité économique et d'améliorer la compétitivité de l'économie, le Gouvernement tunisien a décidé un programme spécifique, comportant des mesures conjoncturelles et d'autres structurelles.

La concrétisation des objectifs tracés et le renforcement de la capacité d'adaptation de l'économie nationale requièrent davantage d'efforts afin d'accélérer le rythme de croissance du PIB, de promouvoir les secteurs innovants à forte valeur ajoutée et d'inculquer la culture de la qualité dans tous les domaines ; ce qui appelle la mise en œuvre d'une nouvelle génération de réformes structurelles à même de permettre de relever les défis et d'exploiter au mieux les nouvelles opportunités.

Ces réformes constituent le prolongement des politiques et programmes de développement passés et reposent sur les réalisations des années antérieures tout en s'inspirant des orientations futures, notamment la consolidation du positionnement compétitif de l'économie nationale, la préparation du secteur des services à l'ère de l'ouverture, le renforcement de la finance directe et la promotion de la dynamique privée. Ces actions devraient concourir au renforcement de l'intégration de l'économie nationale dans la sphère économique mondiale.

Partant de ces considérations, le Gouvernement tunisien sollicite l'appui de la Banque Mondiale pour initier un nouveau Programme d'Appui à l'Intégration (PAI) dont la finalité est de consolider les acquis réalisés suite aux réformes et mesures mises en œuvre notamment dans le cadre de quatre programmes d'amélioration de la compétitivité de l'économie (PACE I à PACE IV) appuyés par la Banque Mondiale, la Banque Africaine de Développement et l'Union Européenne et de soutenir les réformes initiées dans le cadre du XIème plan de développement visant un ancrage substantiel de l'économie nationale dans la sphère mondiale.

I- Acquis et réalisations des dernières années

La Tunisie est parvenue, durant plus d'une décennie, à réaliser des performances appréciables malgré les pressions résultant d'une conjoncture contraignante marquée au niveau interne par des conditions climatiques peu favorables et des pressions croissantes sur le marché de l'emploi et, au niveau mondial, par des événements d'ordre politique et sécuritaire, l'exacerbation de la concurrence, l'augmentation vertigineuse des prix des hydrocarbures et des matières premières et le déclenchement de crises financières dont l'ampleur a affecté l'économie mondiale dans son ensemble.

Ces performances traduisent la solidité acquise par l'économie nationale, attestent de sa capacité de résistance aux aléas de la conjoncture tant nationale que mondiale et mettent en exergue l'efficacité des stratégies, des programmes et des politiques adoptés dans les domaines économique et financier et en matière de développement des ressources humaines, d'impulsion de l'emploi et de promotion des secteurs sociaux.

Plus particulièrement, les performances enregistrées par l'économie tunisienne se sont reflétées à travers la réalisation d'un taux de croissance moyen de l'ordre de 5.2% depuis 1996, date d'entrée en vigueur de l'Accord d'Association avec l'Union Européenne, ainsi que la diversification de la base de production avec un renforcement de la part des secteurs des services (58.2 % en 2008 contre 47.2 % en 1996). Un tel résultat est imputable particulièrement à l'émergence de nouveaux secteurs porteurs, innovants et caractérisés par un fort contenu en savoir, dont la part dans le PIB n'a cessé de s'améliorer passant de 12.8% en 1997 à 23.4 % en 2008.

Ces performances ont été également accompagnées par une amélioration de la contribution de la productivité globale des facteurs (PGF) qui s'est hissée à environ 41 % durant les cinq dernières années contre 36 % en moyenne pour la période du IXème plan de développement (1997-2001) et ce, grâce à l'élan des réformes engagées en vue d'améliorer l'environnement des affaires et d'assurer une allocation optimale des ressources disponibles.

L'investissement a connu une évolution appréciable et s'est élevé à 25.1% du PIB en 2008 contre 23.2% en 1996, avec une contribution de plus en plus renforcée du secteur privé (61.5% en 2008 contre 53.4% en 1996) témoignant de l'intérêt croissant accordé au renforcement de l'initiative privée.

L'investissement direct étranger a également connu une nouvelle dynamique grâce aux efforts déployés en vue d'améliorer l'environnement des affaires d'une manière générale, et de développer des mécanismes susceptibles d'attirer davantage une nouvelle catégorie d'investisseurs et de les orienter vers les domaines porteurs et prioritaires pour l'économie nationale à l'instar des industries manufacturières, les communications, le secteur financier et les projets d'infrastructure dans le cadre des concessions. A ce titre, les IDE ont augmenté de 65.4 % en 2006, 35.1 % en 2007 et de 50 % en 2008 compte non tenu des opérations de privatisation. Ainsi, leur part dans le PIB s'est renforcé et a atteint 5.6 % du PIB en 2008 contre 1.6 % en 1996 et leur part dans l'investissement global a atteint 20.8 % contre 6.2 % en 1996.

Les créations d'emploi se sont intensifiées ; elles ont atteint 79.8 mille emplois en 2008 permettant de couvrir 90% de la demande additionnelle. Le taux de chômage demeure cependant élevé se situant aux alentours de 14% bien qu'une baisse ait été amorcée par rapport au niveau enregistré en 1997 (16.8%).

De surcroît, les équilibres financiers intérieurs et extérieurs ont été préservés. Le déficit courant et le déficit budgétaire ont été limités, respectivement, aux alentours de 2.6% et 2.9% du PIB au cours de la période (1997-2007) contre 5.9% et 3.7% au cours de la période (1992-1996) et l'inflation a été maîtrisée en se limitant à 3.1% en 2007 contre 3.7% en 1996

Ces performances ont été le résultat des efforts déployés pour améliorer la compétitivité de l'économie tunisienne et renforcer son intégration dans l'économie mondiale. Les parts de marché sur l'UE sont passées de 0.59% durant la période 1997-2001 à 0.62% actuellement et l'indicateur de rattrapage des pays de l'U.E a attient 30.2% pour la période (1997-2007) contre 25.1% au cours de la période (1993-1996). Dans ce cadre, le taux d'ouverture s'est élevé à 102.6% en 2008 contre 86% en 1996 en raison de la dynamique qui a caractérisé les échanges extérieurs, particulièrement au niveau des exportations dont la part dans le PIB s'est renforcée pour atteindre environ 47% au cours de la période (1997-2007) contre 42.4% au cours de la période (1992-1996).

Par ailleurs, les écarts de productivité par rapport aux pays de l'U.E paraissent relativement bas, de l'ordre de 27%, dans les secteurs les plus ouverts à la concurrence tels que les industries mécaniques et électriques et le secteur des textiles, tandis que ces écarts atteignent 55% pour les autres secteurs. Le programme de mise à niveau du secteur industriel qui a accompagné le processus de libéralisation et d'intégration dans l'économie mondiale a contribué à l'amélioration de la capacité concurrentielle du tissu industriel tunisien. L'économie tunisienne dispose ainsi d'importantes marges pour accroitre sa compétitive et, partant, accélérer le rythme de la croissance.

Au terme de l'année 2008, le programme de mise à niveau a enregistré l'adhésion de 4145 entreprises industrielles dont 474 entreprises durant la période 2007-2008 contre 500 prévues par le XIème Plan pour la même période ; Le total des dossiers approuvés s'est élevé à près de 2843 dossiers pour un montant global d'investissement de 4670 MDT et les primes accordées ont atteint 652 MDT.

L'évaluation du programme a révélé que ce dernier a largement contribué à la modernisation des outils de production, la mise en place de systèmes qualité et informatique et l'organisation des méthodes de gestion. Le programme a, également, contribué au relèvement du taux d'encadrement qui est passé de 9% à 17%.

Par ailleurs, afin d'améliorer davantage l'environnement de l'entreprise, un important programme de modernisation industrielle a été mis en œuvre ; Ce programme a pour objectif principal de soutenir les efforts de restructuration industrielle et de modernisation du secteur privé à travers le développement par l'innovation et la créativité, la consolidation de la qualité, de la métrologie et de la normalisation, la promotion de la propriété industrielle ainsi que l'amélioration et la facilitation de l'accès au financement des petites et moyennes entreprises.

A fin octobre 2008, le programme de modernisation industrielle a engagé 570 actions dont 417 ont été achevées pour des investissements de l'ordre de 27,4 millions d'euros, soit 86 % de son budget opérationnel qui s'élève à 32 millions d'euros ; il importe de relever que près du tiers des investissements réalisés correspondent à des programmes d'amélioration de la qualité.

Parallèlement, d'importants acquis sociaux ont été enregistrés durant cette période et qui se reflètent à travers l'amélioration des indicateurs relatifs à l'éducation, l'enseignement supérieur, la formation professionnelle, la santé et les conditions de vie d'une manière générale. A titre indicatif, l'espérance de vie à la naissance a atteint 74.8 ans en 2008 contre 71.6 ans en 1996, le taux de scolarisation de la tranche d'âge 6-14 ans a évolué de 86.2% en 1996 à 94.8% en 2008 et le taux de couverture sociale effective est passé de 77% en 1996 à 93.3% en 2008.

Ces résultats probants au plan économique et social sont le couronnement d'un effort soutenu de réformes d'envergure et de leur application progressive et clairvoyante. Cet élan de réformes s'est focalisé particulièrement sur la poursuite de la libéralisation de l'économie tunisienne à travers l'achèvement depuis Janvier 2008 du programme de démantèlement des tarifs douaniers pour les produits industriels initié dans le cadre de l'Accord d'association avec l'Union Européenne. Cette action a été accompagnée d'une baisse progressive des droits de douane avec les autres pays partenaires de la Tunisie en vue de réduire le détournement des trafics. Ces différentes mesures ont permis d'harmoniser les différentes règles et procédures et de réduire les coûts de transaction pour l'entreprise. A ce titre, la protection effective s'est réduite à 16% en 2007 contre 73% en 1997.

Cette intégration à l'économie mondiale s'est poursuivie également grâce à la signature d'accords de partenariat avec d'autres groupements régionaux à l'instar de l'AELE ainsi que l'accord arabo-méditerranéen de libre échange (accord d'Agadir), et au niveau bilatéral avec notamment le Maroc, l'Egypte, la Jordanie, la Syrie, la Lybie et la Turquie.

L'élan de réformes a également concerné la promotion de l'exportation à travers le renforcement des institutions et des mécanismes de promotion des exportations, l'adoption d'un nouveau code de douane et la poursuite des réformes engagées dans le cadre de deux programmes consécutifs de développement des exportations appuyés par la Banque Mondiale et visant le renforcement des capacités exportatrices des entreprises, incluant la mise en œuvre d'un projet de liasse unique à l'importation et à l'exportation et de liasse relative au transport. L'élan de réformes a aussi concerné la simplification des procédures de dédouanement et d'enlèvement des marchandises, ainsi que la facilitation et le développement de la logistique de commerce. Les efforts ont été, également, axés dans ce cadre sur l'accompagnement des exportateurs en vue d'accéder à de nouveaux marché et le renforcement des mécanismes de garantie du financement des exportations avant expédition.

Une attention particulière a été également accordée à la promotion de l'initiative privée et à la création d'entreprises à travers l'intensification de l'appui et de l'accompagnement des nouveaux promoteurs, le développement et la modernisation des organismes d'appui, la simplification et la réduction des procédures administratives, la création de guichets uniques et d'un réseau de pépinières d'entreprises et de centres d'affaires, de pôles technologiques et de structures d'appui à l'échelle régionale.

A cet égard, la promulgation de la loi sur l'initiative économique en décembre 2007 constitue une avancée décisive sur la voie de la libéralisation des investissements et l'allègement des procédures de création d'entreprises, la protection des investisseurs, la facilitation de l'accès au financement et la promotion des micro-entreprises ouvrant de nouveaux horizons aux promoteurs.

L'instauration des fondements de l'économie du savoir constitue une des principales caractéristiques de l'œuvre de développement de la Tunisie. Les efforts dans ce domaine se sont intensifiés en vue d'une meilleure exploitation des sources disponibles d'intelligence et de connaissance à travers la modernisation des systèmes d'éducation, de formation et de l'enseignement supérieur et leur insertion dans l'économie du savoir, la promotion de la recherche scientifique et de l'innovation technologique et la facilitation de l'accès aux différentes composantes de l'économie du savoir, outre le développement et l'intensification des services à distance dans divers domaines.

Les réformes ont également porté sur l'amélioration du rendement du système fiscal et la modernisation du secteur financier. En effet, la réforme fiscale a été marquée par la promulgation du code des droits et procédures fiscaux, la révision des taux d'imposition directe et indirecte ainsi que la modernisation de l'administration fiscale notamment sur le plan du recouvrement et du contrôle.

De son côté, le secteur financier a fait l'objet de réformes d'envergure qui ont touché l'ensemble de ses composantes. Dans le domaine bancaire, les actions ont porté sur la mise en place de règles de gestion prudentielle conformes aux standards internationaux, la restructuration du secteur par la consécration de la banque universelle et la privatisation de certaines banques. La consolidation des assises financières des banques à travers l'assainissement du portefeuille des créances accrochées et le provisionnement des créances. Les efforts se sont focalisés également, sur la modernisation des prestations offertes à travers l'élargissement de la monétique, l'instauration de la télécompensation, le développement des centrales de données et la diversification des produits financiers. Le cadre organisationnel de la Banque Centrale de la Tunisie a été, également, aménagé dans l'objectif de maitriser davantage la politique monétaire et de moderniser ses mécanismes notamment à travers l'orientation vers une politique de ciblage de l'inflation.

Le marché financier a connu une expansion grâce aux mesures adoptées tout au long des dernières années dans le sens de la diversification des valeurs, la modernisation des organismes de placement collectif, l'incitation des sociétés à la cotation en bourse, le développement de la sécurité financière, l'amélioration du marché des titres de créances, le développement du capital risque et la mise en place d'un marché alternatif.

Le secteur de l'assurance connaît de son côté une vraie dynamique de progrès et de développement grâce à la refonte du cadre législatif et institutionnel du secteur qui a touché le renforcement de la règlementation prudentielle, la réforme de l'assurance automobile, le développement de l'assurance vie et des autres branches prometteuses telles que l'assurance exportation et l'assurance agricole, outre l'amélioration des prestations offertes par la réduction des délais et des procédures d'indemnisation, le renforcement de la gestion interne des compagnies d'assurance, ainsi que l'octroi de l'autonomie de gestion au comité général des assurances pour veiller au bon fonctionnement du secteur.

Sur le plan du développement humain, dans le but de mieux répondre aux exigences de la croissance économique et aux besoins de développement et de favoriser l'instauration des fondements de l'économie du savoir, il a été procédé à l'amélioration du rendement des systèmes d'éducation, de formation professionnelle et d'enseignement supérieur. C'est dans ce cadre que fût promulguée la loi d'orientation de l'éducation et de l'enseignement scolaire, outre la révision du régime des diplômes universitaires par l'adoption progressive du système LMD en cohérence avec les normes et standards internationaux y afférents et l'augmentation de la capacité d'accueil dans les filières porteuses et à forte intensité d'emploi. Les dispositions portent également sur la diversification des filières de la formation professionnelle, l'accroissement des capacités des centres de formation en plus de l'appui à la recherche scientifique et de l'ouverture de l'entreprise sur les structures d'enseignement et de recherche afin d'améliorer son rendement et son efficacité.

L'emploi a bénéficié d'une attention particulière et a été hissé au premier rang des priorités nationales. Cette position privilégiée s'explique par l'intérêt accordé au facteur humain dans l'impulsion de la croissance et la concrétisation des objectifs de développement. Elle s'explique aussi par l'augmentation au cours de la dernière décennie de la demande additionnelle d'emploi et par l'évolution de sa structure.

La politique de l'emploi préconisée s'est basée particulièrement sur l'accélération du rythme de croissance, la promotion de l'investissement, l'encouragement de l'initiative privée ainsi que sur la mise en œuvre et le renforcement des programmes et des mécanismes visant à améliorer l'employabilité des demandeurs d'emploi et à faciliter leur insertion dans la vie active. Ces mécanismes qui ont trait, particulièrement, à la création de la Banque Tunisienne de Solidarité et du Fonds National de l'Emploi et à l'instauration d'un système de microcrédits, ont touché depuis leur création et jusqu'à la fin de l'année 2008 près de 528 000 bénéficiaires.

Parallèlement, diverses mesures ont été décrétées en vue d'inciter les entreprises à recruter les diplômés de l'enseignement supérieur et à encourager l'initiative privée et de consolider des interventions des programmes de promotion de l'emploi des jeunes.

Le développement régional a également bénéficié d'une attention particulière à travers la promotion de l'investissement privé dans les régions prioritaires et le renforcement de l'infrastructure et des équipements collectifs, en plus de la consolidation des projets et programmes destinés à la préservation de l'environnement, la protection des ressources naturelles et l'amélioration du cadre de vie.

L'élan des réformes se poursuit dans le cadre du XIème plan à une teneur plus vigoureux, d'abord au vu des objectifs fixés pour répondre aux aspirations nationales notamment en matière de croissance et de création d'emplois et ensuite au vu de l'évolution défavorable de la conjoncture internationale enclenchée à partir de l'année 2007 avec la flambée des prix des hydrocarbures et des produits de base et qui continue avec le déclenchement de la crise financière qui a ébranlé les marchés financiers et affecté de nombreuses banques internationales.

II- Les perspectives de développement pour la période 2009-2011

La Tunisie aborde une étape nouvelle et cruciale de son processus de développement forte des acquis accomplis et des performances réalisées dans tous les domaines tout en aspirant à aller de l'avant et à progresser vers de meilleurs horizons.

Sur cette base, les objectifs de développement retenus pour le XIème plan de développement (2007-2011) ont été élaborés en conformité avec les priorités tracées, reflétant les aspirations nationales et portant l'empreinte des mutations profondes au double plan national et international.

Au niveau national, il y a lieu de signaler l'importance des mutations démographiques et des défis qui en découlent aussi bien au niveau des créations d'emplois, qu'au niveau du système de santé et du maintien des équilibres financiers et des pressions sur les ressources naturelles. Au niveau international, l'environnement économique est marqué par l'accélération des mutations eu égard à l'élargissement du phénomène de la globalisation, l'exacerbation de la concurrence, outre les évolutions défavorables qui caractérisant la scène économique internationale ainsi que les fluctuations des cours des produits de base et la volatilité des taux de change.

Les principaux objectifs tracés dans le XIème plan de développement ont trait essentiellement à :

- L'accélération de la croissance du PIB pour le porter à un taux moyen de 6.1%. La concrétisation de cet objectif dans un contexte plus difficile repose sur la contribution de tous les secteurs productifs. Elle sera tributaire des performances du secteur des services modernes et de la consolidation du poids des activités à haute valeur ajoutée, basées sur les connaissances dont la part devra attiendre 27.5% du PIB en 2011 contre 20.4%, en 2006.

  Le rythme ciblé de la croissance suppose également la poursuite de l'amélioration de la PGF dont la contribution à la croissance sera de l'ordre de 48% contre 41% réalisés durant les cinq dernières années. Ce qui requiert notamment la poursuite de la valorisation des ressources humaines, la généralisation de l'utilisation des nouvelles technologies de l'information et des communications, le développement de la recherche et de l'innovation pour diversifier le produit et améliorer sa compétitivité.

- La poursuite d'une politique de redistribution des revenus visant à améliorer l'indicateur de développement humain, à consolider la classe moyenne et à réduire le niveau de pauvreté.

Compte tenu des mutations profondes qui caractérisent la scène nationale et internationale et des aspirations et choix nationaux, la concrétisation des objectifs susvisés nécessite :

- Le renforcement de l'intégration de l'économie nationale dans l'économie mondiale à travers la promotion des exportations, l'insertion dans des réseaux internationaux de production et de distribution, la mobilisation des investissements directs étrangers, le développement de rapports de partenariat avec des investisseurs stratégiques, la facilitation des investissements nationaux à l'étranger et l'accès des entreprises nationales aux sources de financement extérieur.

- L'optimisation de l'allocation des ressources disponibles tant financières que naturelles et la valorisation des ressources humaines et ce, dans l'objectif d'assurer l'efficience des ressources disponibles en vue d'améliorer la productivité globale des facteurs et de garantir la soutenabilité de la croissance économique.

- La préservation des équilibres financiers susceptible d'assurer la solidité de l'économie, d'améliorer ses capacités à faire face aux chocs exogènes, de limiter les répercussions des retournements de conjoncture et de répondre au mieux aux exigences de la mondialisation de l'économie. Cet objectif repose sur la maîtrise du déficit courant, la réduction de l'endettement, la préservation des équilibres budgétaires et la maitrise de l'inflation.

- La consolidation du progrès social et l'optimisation de la politique de revenu dans le sens de l'équité et de la réduction du niveau de pauvreté ainsi que l'instauration d'un climat social favorable et le renforcement des programmes destinés à la préservation du pouvoir d'achat et au soutien aux catégories à besoins spécifiques.

Ainsi, l'accélération du rythme de la croissance économique, la garantie de sa pérennité et l'intensification de son contenu en emploi tout en préservant la stabilité des équilibres financiers et en optimisant l'allocation des ressources disponibles constituent les piliers fondamentaux du schéma de développement pour le présent plan de développement (2007-2011).

Toutefois, alors que la période transitoire pour la mise en place de l'Accord de Libre Echange entre la Tunisie et l'Union européenne s'est achevée en janvier 2008 et l'économie s'intègre davantage dans l'espace euro-méditerranéen, de nouveaux défis s'ajoutent en raison de la volatilité des prix des produits de base et des matières premières et de la crise financière ayant ébranlé les marchés financiers avec de lourdes conséquences sur l'activité économique mondiale.

Cette crise n'a pas affecté la place financière tunisienne pour plusieurs raisons : le système de titrisation demeure fort limité et ne concerne que deux opérations bien encadrées pour un montant inférieur à 300 millions d'USD. Les prêts fonciers sont accordés à des taux d'intérêt fixes prenant en compte la capacité de remboursement des bénéficiaires, et ne représentent que 10 % des engagements bancaires. La capitalisation boursière ne représente que le cinquième du PIB. Les placements des réserves tunisiennes en devises sont quant à eux régis par des règles prudentielles strictes et sont sous forme de titres souverains en dollars et en euros et dans la limite de 30 % de dépôts auprès des banques de premier rang.

Au niveau de la sphère réelle, des conditions de crédit défavorables et une confiance des ménages et des entreprises fortement dégradée pèsent sensiblement sur la demande dans les principaux pays partenaires de la Tunisie. De ce fait, les principaux secteurs d'exportation de la Tunisie se trouvent affectés, en l'occurrence le secteur des composants automobiles, le textile et le tourisme.

Dès l'apparition des signes précurseurs de cette crise, la Tunisie a observé une vigilance soutenue pour prévenir ses conséquences et cerner ses retombées sur l'économie nationale à travers la création d'une commission pour suivre la conjoncture financière et économique internationale et proposer les mesures correctives adéquates.

Dans ce cadre, d'importantes actions ont été décidées par le président de la République Tunisienne le 7 novembre 2008 et un programme a été adopté avec des mesures à court terme pour soutenir les entreprises qui connaissent des difficultés notamment les entreprises exportatrices et des mesures d'ordre structurel qui s'articulent autour de 5 axes principaux, en l'occurrence l'amélioration des prestations fournies par le secteur public, l'optimisation des procédures du commerce extérieur, l'accélération des programmes d'investissements publics essentiellement dans le domaine de l'infrastructure et des équipements collectifs, le renforcement de la formation professionnelle et la consolidation des fondamentaux dans les domaines économiques et financiers.

Grâce à ces mesures et malgré la récession économique notamment dans la Zone Euro (-2 % en 2009 et 1 % attendu pour 2010), la croissance du PIB est projetée à 4.5 % en 2009 et s'accélérera pour attendre 5.5% en 2010 et 6% en 2011. Ces niveaux restent toutefois en deçà de l'objectif de 6.1% par an retenu dans le XIème Plan et s'explique par le ralentissement de la croissance des exportations estimée à 1% en 2009.

Les efforts se poursuivront en vue de maitriser l'inflation et la limiter au niveau de 3 % par an pour les trois prochaines années.

La préservation des équilibres financiers interne et externe sera poursuivie ; l'objectif est de limiter le déficit courant et le déficit du budget de l'Etat à des niveaux raisonnables compatibles avec les moyens de financement de l'économie nationale. Les montants économisés du fait de la baisse des subventions alimentaires et aux produits pétroliers permettraient d'augmenter les dépenses d'investissement et de soutien aux entreprises économiques en 2009.

Une attention particulière sera accordée à l'investissement privé grâce à la poursuite et l'approfondissement des réformes en vue de l'amélioration du climat d'investissement. En l'occurrence, le Gouvernement tunisien est fermement engagé à intensifier et accélérer davantage les réformes économiques et financières dans une logique d'intégration poussée dans l'économie mondiale afin de saisir les opportunités offertes par un environnement en pleine mutation.

A cet effet, et en vue de concrétiser les objectifs assignés et de renforcer la capacité de résistance aux chocs, le Gouvernement tunisien a préparé en étroite concertation avec les bailleurs de fonds, un nouveau programme d'appui à l'intégration et souhaite obtenir un appui substantiel de la Banque Mondiale sous forme d'une opération à décaissement rapide.

III- Le programme d'appui à l'intégration

Le programme d'appui à l'intégration économique, conçu en collaboration avec la Banque mondiale, la Banque africaine de développement et l'Union Européenne, vise à appuyer davantage l'économie tunisienne sur la voie de l'intégration à l'économie mondiale après avoir franchi des pas importants au plan de l'amélioration de la compétitivité, grâce à un train de réformes introduites dans quatre programmes consécutifs d'appui à la compétitivité économique.

Le programme est d'une importance capitale compte tenu de sa concordance avec un nombre d'échéances décisives pour l'économie tunisienne, à l'instar de l'instauration effective de la zone de libre échange avec l'Union Européenne à partir de 2008 et la préparation des négociations concernant la libéralisation des secteurs des services et de l'agriculture outre l'orientation vers la consécration de la Tunisie en tant que place régionale d'affaires et de services.

Ce programme intervient dans un contexte particulier marqué par l'avènement de la crise financière mondiale dont les effets se font sentir par l'économie nationale résultant de la contraction de la demande extérieure. En l'occurrence, les mesures et les actions de réformes prévues par le programme viennent en appui aux objectifs arrêtés par le XIème plan de développement, et ont trait à l'amélioration de l'environnement de l'entreprise, la facilitation de son insertion dans les marchés extérieurs et la modernisation de ses modes de gestion, et la consolidation des secteurs prometteurs générateurs d'emplois qualifiés.

Sur cette base, le programme comporte trois axes :

1. La réduction des coûts des transactions et l'approfondissement de l'intégration commerciale ;
2. L'amélioration de l'environnement des affaires ;
3. L'amélioration de l'accès au financement.

1) La réduction des coûts des transactions et l'approfondissement de l'intégration commerciale : cet objectif s'inscrit dans le cadre d'une exploitation judicieuse des opportunités qu'offre le marché mondial et de la consécration d'une intégration soutenue au sein de la sphère économique mondiale. Les actions envisagées dans ce cadre porteront notamment sur la poursuite du rapprochement des régimes tarifaires des biens en vue de les simplifier et de réduire les risques de détournement des échanges ainsi que sur la convergence au niveau des normes et des réglementations avec les principaux marchés visés.

Elles concerneront également le développement des services d'exportation au vu de la dynamique grandissante que connaît le secteur, du potentiel important qu'il recèle ainsi que de sa contribution à la croissance du PIB et à la création d'emploi. Une attention particulière devra également être accordée dans le cadre de ce programme au renforcement de l'efficacité des services logistiques compte tenu de leur rôle dans le raffermissement de la compétitivité de l'économie et la facilitation des procédures du commerce extérieur.

Plus concrètement, les mesures de réformes commerciales porteront sur trois axes fondamentaux:

- Approfondissement des réformes relatives aux échanges de biens à travers la réduction du nombre des tarifs douaniers de 9 à 6 en 2009 et de 6 à 5 à fin 2010 permettant de réduire le tarif moyen à 17 % en 2010, la clarification du système de contrôle des importations, la facilitation des procédures et transactions commerciales, le renforcement des standards et des normes de qualité et la consolidation des mécanismes de lutte contre la contrefaçon.

- Poursuite des réformes relatives aux échanges de services par le renforcement des prérogatives du Conseil National des Services à travers la création d'une unité de gestion par objectif dotée de moyens budgétaires et humains adéquats, ainsi que l'adoption d'un plan d'action pour la réforme et la promotion des secteurs de services à fort potentiel commercial sur la base d'un diagnostic du cadre réglementaire à établir. Les axes de réforme à ce niveau devront, également, porter sur l'amélioration de l'outil statistique relatif aux activités et au commerce des services à travers l'adoption d'une nomenclature commune des services et la création d'un système d'information et de statistique sur les activités et le commerce international des services, outre l'adoption d'un plan d'action pour mettre à niveau les secteurs de services en vue d'encourager et de faciliter leur exportation.

- Renforcement de l'efficacité des services logistiques par la réduction des coûts et des délais du passage portuaire et la facilitation des opérations logistiques internationales pour les exportateurs et les prestataires de services grâce aux nouvelles dispositions du code des douanes.

2) L'amélioration de l'environnement des affaires : l'environnement des affaires a bénéficié d'une attention particulière et a constitué au cours des dernières années une constante de l'œuvre de développement axée sur la dynamique privée et l'intégration à l'économie mondialisée. L'amélioration de l'environnement des affaires se poursuivra au cours de la période à venir en vue de renforcer davantage la compétitivité de l'économie, d'impulser l'initiative privée et attirer davantage les investissements directs étrangers.

Les axes du programme se focaliseront à ce niveau sur :

- La poursuite de l'amélioration des dispositifs administratifs régissant les activités des entreprises à travers la réduction effective à 7 jours de la période de remboursement de la TVA sur les produits d'exportations, le remplacement par des cahiers des charges de la moitié des autorisations restantes, l'instauration et la mise en ligne du nouveau système du registre du commerce et la réduction des délais de mise à disposition du foncier industriel.

- L'amélioration de l'information et du cadre réglementaire pour une meilleure convergence de l'offre et la demande de travail par l'élaboration d'un guide sur la législation du travail pour les entreprises, la réalisation des modules de formation sur la réglementation du travail et l'étude de certains aspects du marché du travail.

- Le renforcement de la protection des investisseurs dans la société et de la transparence des sociétés de capitaux et ce par l'amendement du code des sociétés pour permettre aux actionnaires minoritaires d'accéder aux informations sur la situation de la société, d'ester en justice et d'encadrer les opérations à risque, comportant un conflit entre les intérêts personnels des dirigeants et ceux de la société qu'ils gèrent.

L'environnement législatif et réglementaire de la concurrence a bénéficié, de son côté, d'une attention particulière à travers le renforcement des attributions du conseil de la concurrence, la consécration de son autonomie administrative et financière et l'instauration de l'obligation de solliciter son avis sur certains textes juridiques. Les actions se poursuivront, dans le cadre de ce programme en vue de renforcer son implication dans la révision des cahiers des charges et de renforcer les moyens humains dont il dispose.

3) L'amélioration de l'accès au financement : le développement du financement non bancaire des entreprises constitue le pilier de la réforme de la politique financière pour la prochaine période et ce, dans le but de consolider l'assise financière des banques, réduire le surendettement des entreprises et renforcer leurs fonds propres et prémunir l'économie contre les vulnérabilités aux chocs dans un contexte d'intégration croissante.

Dans cette perspective, la logique de financement devrait reposer sur une meilleure gestion des risques par les banques et une bonne appréciation de la rentabilité des projets d'investissement, outre la mise en place des principes de Bâle II en matière de réglementation prudentielle, la réforme du cadre législatif et réglementaire du capital investissement, le renforcement de la profondeur et de la liquidité du marché financier en vue de dynamiser davantage la bourse de Tunis et d'accroitre son rôle dans le financement de l'investissement privé et le développement des activités de la micro finance.

Les réformes retenues par le programme à ce titre concerneront :

- L'amélioration de l'efficacité et de la compétitivité du secteur bancaire à travers la réduction du poids des créances classées dans le portefeuille des banques en le ramenant à 15% en 2010, l'augmentation du taux de provisionnement des banques à 70% en 2010 et la mise en place d'un plan d'action pour Bâle II ainsi que le renforcement du système de garantie à travers l'aménagement du système d'indemnisation et de la politique de tarification de la Société Tunisienne de Garantie.

- La réforme du cadre législatif et réglementaire du capital investissement, notamment à travers l'amélioration des conditions de sortie du capital des projets sur la base des performances de l'entreprise et l'adoption d'un cadre comptable spécifique aux activités de capital risque à partir des mesures comptables internationales relatives au capital risque.

- Le renforcement de la profondeur et de la liquidité du marché financier notamment par l'accroissement des privatisations à travers la Bourse, le renforcement de la liquidité du marché des actions et du marché obligataire à travers le relèvement de la part autorisée d'acquisition des BTA par les étrangers de 20% à 30% et l'autorisation des institutions internationales à émettre des emprunts obligataires sur le marché financier tunisien dans les mêmes conditions que les opérateurs locaux.

- Le développement des activités de la micro finance par l'amélioration de la performance de la Banque Tunisienne de Solidarité.

En conclusion, le Gouvernement tunisien est d'avis que le programme de réformes esquissé dans la présente lettre permettra à la Tunisie de raffermir son processus d'intégration à l'économie mondiale, d'accroitre sa compétitivité et de relever les défis futurs auxquels elle se trouve confrontée. D'autant que la Tunisie devra subir au cours des prochaines années les répercussions de la crise économique mondiale qui secoue actuellement les économies de tous les pays du monde. La mise en œuvre de ce programme serait largement facilitée si la demande en vue d'une opération à décaissement rapide de l'ordre de 250 millions de dollars US était acceptée par la Banque Mondiale.

République Tunisienne
Ministère du Développement et de la Coopération Internationale

Mohamed Nouri Jouini

ANNEX II. INTEGRATION AND COMPETITIVENESS PROGRAM MATRIX

Objectives	**Actions**	***Conditions for Tranche Releases***		**Expected Outcome/Output**
		First tranche (2009)	***Second tranche (2010)***	
A. REDUCE TRADE TRANSACTION COSTS AND DEEPEN TRADE INTEGRATION				
1-A) DEEPEN INTERNATIONAL INTEGRATION FOR TRADE IN GOODS	Simplify and reduce customs tariffs.	**The Borrower's budget law for 2009 which revised the Customs tariff regime by reducing the number of Customs tariff rates from 9 to 6, including the tariff rate "zero", has been enacted**	***The Borrower's budget law for 2010 which shall revise the Customs tariff regime by reducing the number of Customs tariff rates from 6 to 5, including the tariff rate "zero", shall be enacted.***	Reduction of the average level of protection and diversification of trade Simple mean of MFN import duties at the HS 6 digits level drops from 21.7% in 2008 to 17% in 2010 Tunisia's standards and quality norms converge to international best practices The number of norms that are not identical to international standards (109 in 2008) falls by more than one third by the end of 2010
	Foster convergence of product standards and quality norms to EU and international norms	**The Inter-Ministerial Council has adopted a draft law related to standards and quality norms applicable to all products imported or utilized in the Borrower's territory, consistent with international best practices.**		
			Convert half of the existing 940 obligatory product quality and safety standards into voluntary standards.	
		Adopt: • a law on food safety • a law on safety for industrial products	Establish an agency in charge of food safety and quality control	

Objectives	Actions	*Conditions for Tranche Releases*		Expected Outcome/Output
		First tranche (2009)	***Second tranche (2010)***	
1-B) STRENGTHEN THE EFFECTIVENESS OF TRADE FACILITATION AND LOGISTICS SERVICES	Facilitate trade procedures	Establish a list of non-tariff measures, including technical regulations according to the classification of ITC.	***The Ministry of Commerce shall put in place a system of selective management of imports control based on the risks presented by the imported products and the importers in order to allow speedier controls for non-risks products and importers.*** Connect all trade control agencies to Tunisia Trade Net. Update the list of non-tariff measures.	Reduction of cost and delays due to technical controls. The share of import transactions subjected to technical controls is reduced from 100% in 2008 to 90% in 2010.
		Publish import tariffs and all required import documentation on the Customs website for online use.		
		Adopt an amendment to import control modalities (decree nr° 94-1744 of 29 August 1994) to: - specify the modalities of sampling and analyses, as well as factors justifying recourse for products on lists A, B and C and; - introduce the possibility of contesting laboratory decisions of nonconformity by having other laboratories (including private ones) undertake the tests according to international standards.		
	Reduce costs and time of border crossing		***The Customs Authorities and the Rades Port Authorities shall make the first one-stop trade control procedures office (guichet unique) at Rades Port operational and the Ministry of Transport shall make the electronic platform (liasse transport) which shall connect all operators in the transport chain operational.***	Reduction of delays between cargo entry and exit in the port of Radès The mean time of port clearance falls from 5.6 days in 2008 to 3 days in 2010
			Review the scale of port storage fees	

Objectives	Actions	*Conditions for Tranche Releases*		Expected Outcome/Output
		First tranche (2009)	***Second tranche (2010)***	
	Facilitate international logistics operations for exporters and transport service providers	Define criteria for access to the professions of trade intermediaries, especially freight forwarders.		
			Put in place a legal framework for the establishment and operation of logistic activities zones.	
			Improve the transparency and reduce delays by suppressing the manual tracking of goods and putting a GPS-based tracking system in place.	
1-C) FOSTER TRADE IN SERVICES	Establish a coherent institutional and coordinated framework for services sectors.	***The Inter-Ministerial Council has adopted a draft Decree amending the Decree No. 2006-1826 dated June 26, 2006 regarding NCS, in order to: (i) mandate NCS to prepare a strategy for services development; (ii) formalize the creation of thematic commissions within NCS; and (iii) strengthen the role of the Permanent Secretariat of NCS through the establishment of a performance-based budgeting unit.***	Adopt a national strategy for trade integration in services formulated by the NCS.	<u>Improving coordination among Ministries and stakeholders</u> Number of meetings organized annually, including sessions of thematic working groups, has doubled between 2008 and 2010.
	Implement the development strategy for services	*Establish diagnostics of the regulatory framework in the form of sector notes for services sectors with strong export potential.*	***The Inter-Ministerial Council shall adopt an action plan to reform the regulatory framework of the services sectors, to be prepared on the basis of a regulatory assessment to be carried out by NCS.***	<u>Support services sectors on their strategy</u> At least 3 activities proposed in the action plan are reflected in official documents
			Prepare an orientation document for the upgrading of firms in the services sector	
			Establish a common nomenclature for services.	
			Consolidate, and publish online for the sectors with strong export potential : • statistics on trade and FDI flows • the legislation and regulation relative to FDI and trade	

Objectives	Actions	*Conditions for Tranche Releases*		Expected Outcome/Output
		First tranche (2009)	*Second tranche (2010)*	
B. Further Improve the Business Climate				
2-A. Ease business entry and operations	Reduce administrative burden for creating and operating business	Launch an impact study on suppressions of authorizations and revisions of cahier des charges in regards to the impact on companies and job creation.	***The Prime Minister shall sign an executive order (arrêté) reducing by half the number of activities where operators are required to obtain a prior authorization in order to start their businesses.*** Get the observations from the Competition Council on the rules and regulations governing business conduct (*cahier des charges*) established before 2005.	The growth rate of the number of companies created in those sectors exceed the national average between 2008-2010. Number of "cahier des charges" on which the Competition Council gave his observations increase
		The Inter-Ministerial Council has adopted a draft law amending the Urban and Regional Development Code (Code de l'aménagement du territoire et de l'urbanisme), in order to reduce the time necessary for businesses to acquire industrial land.		Reduce delays to obtain access to industrial land Average delay for approving an industrial zone outside of the areas with an existing urban development plan will be reduced from three year and half in 2008 to 6 months in 2010 Average delay for allotting land within an approved industrial zone would be cut by 6 months
	Enhance business information systems	**The Inter-Ministerial Council has adopted a draft Law amending the Law No. 95-44 dated May 2, 1995 regarding the Registry of Commerce, in order to ensure an effective updating of the information contained in such Registry.**	Make the Registry of Commerce available online for a significant number of companies, with updated data.	Improving the functioning of the registry of commerce The number of companies recorded with updated data increases to more than 300 0000 (baseline: 268 330 in 2008) Number of consultation of the registry of commerce (monitoring of web site consultations will start in 2009)
			The Inter-Ministerial Council shall adopt an action plan for the establishment of a unique common identification number for businesses to be used by the National Statistics Institute, the tax authorities and the social security authorities, based on a feasibility study to be conducted with the	The action plan is adopted by end of 2010 and the institution in charge of putting in place the unique identifier is selected

Objectives	Actions	*Conditions for Tranche Releases*		Expected Outcome/Output
		First tranche (2009)	***Second tranche (2010)***	
			support of the Bank.	
2-B. STRENGTHEN THE APPLICATION OF THE COMPETITION LAW	Enhance the role of the Competition Council and the Directorate of the Concurrence	*The Competition Council shall be requested by the relevant sector Ministries to conduct a regulatory and competition assessment of businesses in two new sectors within the services sector.*	***The Competition Council shall be requested by the relevant sector Ministries to conduct a regulatory and competition assessment of businesses in two new sectors within the services sector.***	Reduction of anti competitive practices The 4 sectoral competition assessments contain concrete actionable recommendations on pro competitive policy or regulatory changes
		Increase the personnel of the Competition Council and Directorate of Concurrence, and increase the budget in order to reinforce the actions of promotion of the culture of competition.		
	Strengthen the instruments for fighting counterfeiting	Initiate the creation of a National Council of Anti-Counterfeit composed of Customs, Competition Directorate General, the Ministries of Health and Industry and other relevant agencies	Adopt and make operational the program of fight against the counterfeit established by the National Council on Counterfeit of statistics on counterfeiting for the institutions concerned (Customs, Health and Industry Ministries, Competition), including requests from operators, investigations, and fines.	
	Enhance the protection of investors and transparency and corporate governance	The Council of Minister adopts a draft law amending the business code ("code des societes") to enhance the protection of investors	*The Conseil du Marche Financier's regulation regarding on public information on the dealing among shareholders is adopted for companies raising public saving*	Access to information by minority investors is enhanced through improved disclosure A higher level of transparency of corporate operations, including potential conflict of interest situations
2-C IMPROVE REGULATION AND INFORMATION ON LABOR	Improve the knowledge of existing labor regulations.	Elaborate a guide on the labor regulation and collecting jurisprudence for the companies in order to mitigate the ignorance of the texts.	Undertake a study on selected aspects of the labor market, including i) the effective application of the labor code, in particular termination procedures, ii) a benchmarking of existing regulations..	A guide on the main features of Tunisia's labor regulation is elaborated and disseminated and a discussion with stakeholders on the rigidity of firing laws in the labor code engaged
	Improve intermediation between supply and		Revise articles 28, 29 and 30 and add articles 31 and 32 in the Labor Code	

Objectives	Actions	*Conditions for Tranche Releases*		Expected Outcome/Output
		First tranche (2009)	*Second tranche (2010)*	
	demand for labor		regarding regulations of interim agencies and submit this revision to the stakeholders	
C. ENHANCE THE CAPACITY OF THE FINANCIAL SECTOR TO FINANCE INVESTMENT				
3-A IMPROVE PERFORMANCE AND RISK MANAGEMENT IN THE FINANCIAL SECTOR	Improve financial stability by cleaning up banks' balance sheets.		***The Central Bank of Tunisia shall publish statistics for 2010 that shall show a decrease in the rate of non-performing loans to fifteen percent (15%), and an increase in provisioning of non-performing loans to seventy percent (70%).***	<u>Improving banking finance</u> The credit deposit margins falls from its baseline level (2007)
	Further enhance prudential regulations.		Assess the impact of the circular number 2006/19 on internal control.	
	Make the *Société Tunisienne de Garantie* (SOTUGAR) more effective	Carry out a study on the *Société Tunisienne de Garantie's* (SOTUGAR) regarding compensation schemes and tariff policy by June 200.9	Adopt an action plan based on the study's recommendations to improve the role of the SOTUGAR by the end of 2010.	
3-B ENHANCE THE DEVELOPMENT OF VENTURE CAPITAL AND REGULATED MUTUAL FUNDS	Modify the legal and institutional framework of venture capital firms (SICARs) and mutual funds (FCPR)	**The Law No. 2008-78 dated December 22, 2008 has been enacted. Such Law amends the Law No. 88-92 dated August 2, 1988 regarding venture capital companies (<u>Sociétés d'Investissement à Capital Risque</u>), and mutual venture funds (<u>Fonds Communs de Placement à risque</u>), in order to: (i) encourage venture capital companies' risk taking by eliminating pre-determined exit conditions and basing exit from financed projects on the performance of the venture capital company at the time of the exit; (ii) simplify taxation of venture capital**		<u>The new legal and accounting framework for SICAR encourage risk taking development.</u> The volume of project investment increases from (baseline in 2008: tbd)

Objectives	Actions	*Conditions for Tranche Releases*		Expected Outcome/Output
		First tranche (2009)	***Second tranche (2010)***	
		companies; (iii) encourage venture capital companies to invest in regional development areas; and (iv) eliminate the requirement that mutual venture funds must liberate the totality of the subscribed funds in order to benefit from tax exemption..		
	Adopt an accounting framework specific to venture capital based on international standards	A preliminary report and a set of draft accounting norms are working out. Adopt a new accounting framework for SICAR and FCPR.		
3-C STRENGTHEN THE TUNIS STOCK EXCHANGE 'S DEPTH AND LIQUIDITY	Increase the depth of the stock market.		***The Stock Market shall publish its annual reports that shall show an increase of the stock market capitalization to at least twenty percent (20%) of the Borrower's Gross Domestic Product, due in particular to the increased number of privatizations implemented through the stock market.***	Depth and liquidity of financial market is reinforced The capitalization of the stock market increases from 16.3% at the end of 2008 to at least 20% at the end of 2010.
			Undertake a mid-term assessment of the impact of the law 2005-96 on financial security.	
	Strengthen the liquidity of the stock market.	Increase the authorized percentage of acquisition of the Assimilated Treasury Bonds (BTA) by foreign investors from 20 to 25%.	Increase the authorized percentage of acquisition of the BTA by foreign investors to 30%. Fiscal incentives are only granted for capital increase through the stock exchange.	
			Authorize the international institutions financial organizations to issue bonds on the Tunisian financial market under the same conditions as the local operator.	

Objectives	**Actions**	***Conditions for Tranche Releases***		**Expected Outcome/Output**
		First tranche (2009)	***Second tranche (2010)***	
3-D DEVELOP THE MICROFINANCE MARKET IN TUNISIA	Carry out reforms in Tunisia's microfinance sector.	Carry out a study microfinance to identify the key reforms needed for the development of the sector, including the regulatory framework.	***The Borrower shall adopt institutional and regulatory provisions in order to improve the performance of the Borrower's micro-finance market, to be adopted on the basis of a study to be carried out by the Ministry of Finance.***	
	Identify reforms needed to improve the efficiency of the Banque Tunisienne de Solidarité (BTS).	Carry out a study on the performance and the impact of the BTS, in collaboration with development partners supporting this program.	Publish a progress report on the implementation of the action plan for the improvement of the operation of the BTS established in the light of the results of the study	

ANNEX III: FUND RELATIONS NOTE

IMF Executive Board Concludes 2008 Article IV Consultation with Tunisia

Public Information Notice (PIN) No. 08/136
October 15, 2008

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

On August 6, 2008, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Tunisia.[1]

Background

Tunisia's sound economic policies and pragmatic approach to structural reforms continue to bear fruit, as evidenced by strong growth and improved social indicators. Real GDP growth averaged 5 percent a year while the macroeconomic and financial position strengthened substantially during the past decade.

Tunisia has so far weathered relatively well the difficult international environment. Real GDP growth increased from 5.5 percent in 2006 to 6.3 percent in 2007—a record over the last decade—underpinned by strong performance of agriculture, energy, manufacturing and the services sectors. On the demand side, vigorous exports and investment powered the growth acceleration. Inflation has picked up, due mainly to rising international fuel and food prices and, to a lesser extent, growing liquidity in the banking system reflecting increasing foreign direct investment (FDI). Year-on-year inflation reached 6 percent in April 2008 before pulling back to 4.9 percent in June 2008. The Central Bank of Tunisia (BCT) responded by tightening monetary policy starting in the second half of 2007.

The fiscal deficit was kept within the 2007 budget target of 3 percent of GDP. Revenue exceeded expectations owing mainly to stronger oil revenue—notably from oil companies' higher profits due to surging oil prices and increased domestic production. The additional revenue offset expenditure overruns mainly caused by rising direct food and fuel subsidies. Continued fiscal consolidation and privatization receipts further reduced public debt-to-GDP ratio to about 51 percent at end-2007.

The current account deficit widened due to declining terms of trade, but the significant increase in FDI inflows increased reserves to over US$8½ billion, largely sufficient to cover short-term liabilities.

Bank performance improved significantly in 2007, including banking activity, profitability, and prudential indicators. The ratio of nonperforming loans (NPLs) to total loans declined from 24 percent in 2003 to 17.3 percent in 2007, largely accounted for by the proactive management of such claims, while the provisions-to-NPLs ratio increased from 43.1 percent to 53.8 percent.

The short-term outlook is encouraging despite the challenging international environment. In 2008, real GDP growth is projected to decelerate moderately to 5.5 percent. Inflation would remain around 5 percent if international prices taper off and monetary policy continues to be restrictive. High fuel and food prices are expected to widen the current account deficit to 3.5 percent of GDP. The fiscal deficit is projected to remain at 3 percent of GDP, owing to buoyant revenue, notably from the hydrocarbon sector. The medium-term outlook remains favorable with growth projected at above 6 percent sustained by strong FDI. Risks to the outlook are essentially related to the international environment.

Executive Board Assessment

Executive Directors commended the authorities for the notable resilience and continued strong performance of the Tunisian economy, which has been founded on prudent and forward-looking economic policies and market-oriented structural reforms. The outlook remains favorable, with buoyant FDI supporting growth, although there are downside risks related mostly to the global economic turbulence. Directors considered that the key immediate challenge confronting the authorities will be to address the pressures arising from the global food and fuel price increases while maintaining macroeconomic sustainability. Over the medium term, employment creation and income growth will be key to improving economic welfare in Tunisia.

Directors commended the authorities' commitment to fiscal prudence, which will remain essential for lowering the public debt. They endorsed the authorities' decision to contain the fiscal deficit within the 2008 budget target, which will require tight control over current spending and likely additional adjustments to domestic petroleum prices. They noted that buoyant fiscal revenues, particularly from the hydrocarbon sector, have accommodated the gradual pass-through of international oil and food price increases to domestic prices under the current subsidy system. Directors noted, however, that the current subsidy system is not sustainable, and suggested its replacement with a targeted safety net for the most vulnerable groups that would better support medium-term fiscal sustainability, reduce the country's vulnerability to shocks, and create the fiscal space for additional social and infrastructure expenditures. In this context, they welcomed the authorities' intention in the XI^{th} Plan to phase out subsidies for petroleum products by 2011 and to ensure better control of expenditures for food subsidies.

Directors supported the restrictive monetary stance of the BCT. They recommended that the authorities stand ready to increase the BCT's key policy interest rate if inflationary pressures intensify, given that growth still has significant momentum. They supported the BCT's efforts to manage persistent excess liquidity in the financial system, and to continue to build an inflation-targeting framework for monetary policy.

Directors considered that the exchange rate of the Tunisian dinar is broadly aligned with fundamentals and that the authorities' policies are consistent with external stability. Some Directors saw merit in an accelerated transition toward the authorities' commendable objectives of a floating exchange rate and an inflation-targeting framework.

Directors welcomed the continued strengthening of the banking sector's performance, with greater profitability, a decline in nonperforming loans, and improved loan-loss provisioning. Further strengthening of the banking sector should remain a high priority as the authorities continue to gradually open up the capital account. They welcomed the potential growth and employment benefits of the large FDI-financed projects, but counseled prudence with respect to real estate projects in particular, which may create a credit risk for the banking sector and contingent liabilities for the government. Directors supported the authorities' objective of implementing the Basel II system by end-2009 and achieving full compliance with international Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) standards over the medium term.

Directors welcomed the steps being taken by the authorities to deepen the global and regional integration of the Tunisian economy. They praised the authorities for their pragmatic approach to trade and financial integration, and noted the recent important milestone of achieving bilateral free trade in industrial goods with the European Union. They looked forward to further simplification and reduction of tariffs on a most-favored-nation basis.

Directors welcomed the steps aimed at further improving the business climate. They looked forward to further progress in liberalizing the services sector and reforming the tax and customs administration, in order to promote domestic and foreign investment.

Tunisia: Selected Economic Indicators, 2003-08
(Population: 10.2 million; 2007)
(Per capita GDP: $3,594; 2007)
(Poverty rate: 3.8 percent; 2005)
(Main export: textiles, electronic and mechanical goods, energy, tourism; 2007)

	2003	2004	2005	2006	2007	2008
					Prel.	Proj.
Output and Prices	(Annual percentage change)					
Real GDP (market price)	5.6	6.0	4.0	5.5	6.3	5.5
Consumer prices (end of period)	4.5	1.2	3.7	3.3	5.3	4.7
Consumer prices (period average)	2.7	3.6	2.0	4.5	3.1	5.1
Investment and Saving	(In percent of GDP)					
Gross capital formation	25.0	24.5	22.0	24.1	25.1	25.1
Of which: Nongovernment 1/	17.8	17.5	15.6	17.9	19.1	18.8
Gross national savings	22.1	22.5	20.8	22.1	22.4	21.6
Of which: Nongovernment 1/	18.0	18.0	17.5	18.9	19.5	18.1
Public Finances 2/	(In percent of GDP)					
Revenue, excluding grants and privatization	23.7	23.8	23.6	23.8	24.2	24.6
Expenditure and net lending	27.1	26.6	26.9	26.6	27.2	27.6
Budget balance, excluding grants and privatization	-3.4	-2.8	-3.2	-2.9	-3.0	-3.0
Primary balance, excluding grants and privatization	-0.6	0.0	-0.4	-0.1	-0.3	-0.5
Total government debt	60.5	59.4	58.3	53.9	50.9	47.0
Monetary Sector	(Annual percentage change, unless otherwise indicated)					
Credit to the economy	4.6	5.3	6.3	6.6	9.6	8.5
Base money	5.5	12.2	21.9	17.6	15.3	19.7
Broad money	6.3	10.3	11.0	11.4	12.5	10.5
Velocity of broad money	1.7	1.6	1.6	1.6	1.5	1.5
Three-month treasury bill rate (period average, in percent) 3/	5.5	5.1	5.1	5.1	5.1	5.1
External Sector	(In percent of GDP, unless otherwise indicated)					
Exports of goods (in $, percentage change)	17.1	20.7	8.3	9.7	30.4	29.9

Imports of goods (in $, percentage change)	14.7	17.6	2.9	12.7	28.0	29.1
Merchandise trade balance	-9.1	-8.6	-6.8	-8.2	-8.4	-9.4
Current account excluding official transfers	-2.9	-1.9	-1.1	-2.0	-2.6	-3.5
Current account including official transfers	-2.7	-1.6	-0.7	-1.5	-2.2	-3.3
Foreign direct investment 4/	2.1	2.1	2.6	3.1	4.2	4.6
Total external debt	66.8	66.5	65.4	58.3	54.9	51.8
Gross reserves (in billions of dollars) 5/	3.0	4.0	4.4	6.8	7.9	8.9
In months of next year imports of goods and services	2.5	3.1	3.3	4.0	3.5	3.6
In percent of short-term external debt (on remaining	61.8	82.2	88.3	137.1	137.7	133.9
• maturity basis)						
Memorandum Items:						
Nominal GDP (in $ billions)	26.6	29.3	27.6	31.8	36.7	40.2
Unemployment rate (in percent)	14.3	13.9	14.2	14.3	14.1	14.0
Net imports of petroleum products (in millions of dollars)	328.8	399.0	393.4	632.1	-106.3	108.9
Local currency per dollar (period average)	1.3	1.2	1.3	1.3	1.3	...
Real effective exchange rate (annual average, percentage change)	-5.0	-3.5	-4.6	-0.8	-2.9	...
Stock market index 6/	1,250.2	1,331.8	1,615.1	2,331.1	2,614.1	3,075.4

Sources: Tunisian authorities and Fund staff estimates.
1/Includes public enterprises.
2/the fiscal year is the calendar year.
3/In 2008, average for the first four months.
4/in 2006, excludes receipts from the privatization of Tunisie Télécom, of about $2.2 billions.
5/in 2006 includes receipts from the privatization of Tunisie Télécom.
6/TUNINDEX (1000=4/1/1998). The 2008 data as of August 8, 2008.

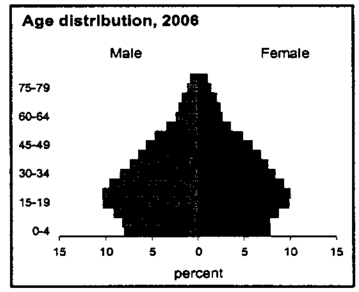
[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

ANNEX IV: COUNTRY AT A GLANCE (INCLUDES COUNTRY MAP)

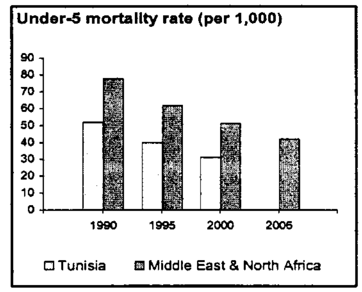
Tunisia at a glance

12/29/08

Key Development Indicators	Tunisia	M. East & North Africa	Lower middle income
(2007)			
Population, mid-year (millions)	10,2	313	3.437
Surface area (thousand sq. km)	*164*	8.778	35.510
Population growth (%)	1,0	1,7	1,0
Urban population (% of total population)	*66*	57	42
GNI (Atlas method, US$ billions)	32,8	876	6.485
GNI per capita (Atlas method, US$)	3.210	2.794	1.887
GNI per capita (PPP, international $)	7.130	7.413	4.544
GDP growth (%)	6,3	5,8	9,7
GDP per capita growth (%)	5,2	4,0	8,6
(most recent estimate, 2000–2007)			
Poverty headcount ratio at $1.25 a day (PPP, %)	..	5	..
Poverty headcount ratio at $2.00 a day (PPP, %)	..	19	..
Life expectancy at birth (years)	73	70	69
Infant mortality (per 1,000 live births)	20	34	41
Child malnutrition (% of children under 5)	4	..	25
Adult literacy, male (% of ages 15 and older)	83	83	93
Adult literacy, female (% of ages 15 and older)	65	63	85
Gross primary enrollment, male (% of age group)	111	108	112
Gross primary enrollment, female (% of age group)	108	103	109
Access to an improved water source (% of population)	93	89	88
Access to improved sanitation facilities (% of population)	85	75	54

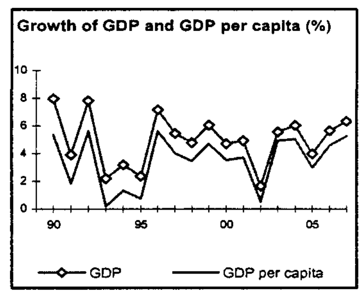


Age distribution, 2006



Under-5 mortality rate (per 1,000)

Net Aid Flows	1980	1990	2000	2007 [a]
(US$ millions)				
Net ODA and official aid	240	391	222	432
Top 3 donors (in 2006):				
France	79	76	93	176
European Commission	1	25	71	149
Germany	26	-8	2	40
Aid (% of GNI)	2,8	3,3	1,2	1,5
Aid per capita (US$)	38	48	23	43



Growth of GDP and GDP per capita (%)

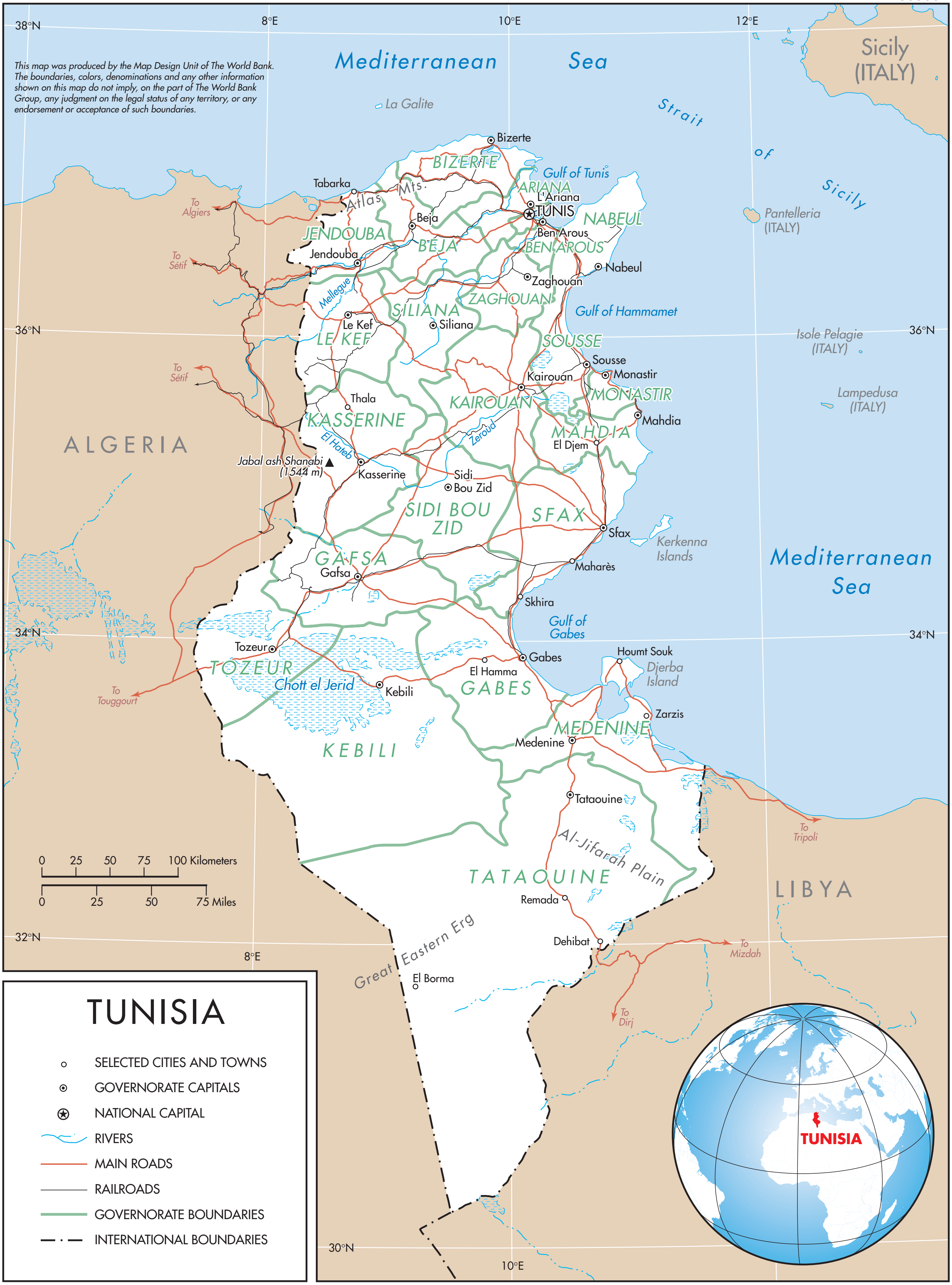
Long-Term Economic Trends	1980	1990	2000	2007	1980–90	1990–2000	2000–07
Consumer prices (annual % change)	..	6,5	3,0	3,1			
GDP implicit deflator (annual % change)	12,8	4,5	3,2	2,4			
Exchange rate (annual average, local per US$)	0,4	0,9	1,4	1,3			
Terms of trade index (2000 = 100)	..	64	100	100			
					(average annual growth %)		
Population, mid-year (millions)	6,4	8,2	9,6	10,2	2,4	1,6	1,0
GDP (US$ millions)	8.743	12.314	19.443	35.009	3,3	4,7	4,8
		(% of GDP)					
Agriculture	14,1	15,7	12,3	10,3	2,8	2,3	2,9
Industry	31,1	29,8	28,6	29,6	3,1	4,6	3,3
Manufacturing	11,8	16,9	18,2	17,2	3,7	5,5	3,2
Services	54,8	54,5	59,1	60,0	3,5	5,3	6,0
Household final consumption expenditure	61,5	63,6	60,7	63,2	2,9	4,3	5,1
General gov't final consumption expenditure	14,5	16,4	15,6	14,4	3,8	4,1	4,3
Gross capital formation	29,4	27,1	27,3	24,8	-1,8	3,6	1,3
Exports of goods and services	40,2	43,6	44,5	54,1	5,6	5,1	4,1
Imports of goods and services	45,6	50,6	48,2	56,5	1,7	3,8	2,4
Gross savings	25,1	22,2	23,1	22,6			

Note: Figures in italics are for years other than those specified. 2007 data are preliminary. .. indicates data are not available.
a. Aid data are for 2006.

Development Economics, Development Data Group (DECDG).

MAP SECTION

IBRD 33500R



TUNISIA

- SELECTED CITIES AND TOWNS
- GOVERNORATE CAPITALS
- NATIONAL CAPITAL
- RIVERS
- MAIN ROADS
- RAILROADS
- GOVERNORATE BOUNDARIES
- INTERNATIONAL BOUNDARIES

JANUARY 2007

ANNEX 1: LETTER OF DEVELOPMENT POLICY

Unofficial Translation

REPUBLIC OF TUNISIA
MINISTRY OF DEVELOPMENT AND
INTERNATIONAL COOPERATION
1 Place Ali Zouaoui – 1069 Tunis

The Minister

February 17, 2009

Mr. Robert B. Zoellick
President
The World Bank Group
Washington, D.C.

Letter of Development Policy

Dear Mr. Zoellick:

Tunisia's development process has been marked by the enormous progress made in the areas of economic liberalization and modernization, human resource development, the consolidation of social well-being, and the steps made toward laying the groundwork for sustainable development. All these achievements have helped our country move up the ranks in the group of emerging countries.

These performances have been possible because of the efforts made and the determination shown to persevere on the path of reforms in various economic and social areas. This has ensured continuity and efficiency in development work and helped improve the country's ability to take up challenges and withstand exogenous shocks.

Having started as of 2007 to implement the XIth Development Plan (for the period 2007–11), Tunisia is now facing a harsh international environment marked by the exacerbation of competition at the global level, especially with the dismantling of the Multi Fibre Arrangement as of 2005, the huge rise in hydrocarbon and commodity prices as of 2007, and, more recently, the outbreak of the international financial crisis, which quickly triggered an economic recession, primarily in developed countries.

Tunisia's real economy has been subjected to the repercussions of this crisis because of the decline in a number of export activities linked to the contraction of international demand, especially in Europe. In light of this and to support enterprises affected by the crisis, shore up economic activity, and enhance the competitiveness of the economy, the Tunisian Government has decided to implement a specific program consisting of cyclical and other structural measures.

Achieving the established objectives and strengthening the adaptability of the national economy require further efforts to accelerate the GDP growth rate, promote the innovative high value-added sectors, and instill a culture of quality in all areas. This calls for a new generation of structural reforms that can help the country meet these challenges and make the most of new opportunities.

These reforms represent the continuation of past development policies and programs and are based on the achievements of previous years at the same time as they draw on goals for the future, namely, consolidating the competitive positioning of the national economy, preparing the services sector for the era of openness, strengthening direct finance, and promoting private sector vibrancy. These actions are expected to help increase the global integration of the national economy.

Based on these considerations, the Tunisian Government hereby requests assistance from the World Bank to launch a new Integration Support Program (PAI), the purpose of which is to build on the results of previous reforms and measures—especially in the context of four programs to improve economic competitiveness (PACE I to PACE IV) supported by the World Bank, the African Development Bank, and the European Union—and to sustain the reforms initiated within the framework of the XI^{th} Development Plan, aimed at firmly anchoring the national economy in the global sphere.

I. Experience and achievements of past years

Tunisia has managed for more than a decade to achieve appreciable performances despite the pressures generated by harsh economic circumstances marked, at the domestic level, by adverse climatic conditions and increasing labor market pressures and, at the global level, by political and security events, the exacerbation of competition, the upward spiral of hydrocarbon and commodity prices, and the outbreak of three financial crises, the scope of which has affected the entire global economy.

These performances can be attributed to the soundness acquired by the national economy. They also attest to the economy's capacity to withstand the hazards of the national and global economic circumstances and highlight the effectiveness of the strategies, programs, and policies adopted in the economic and financial areas and with respect to human resource development, employment incentives, and social sector promotion.

More particularly, the performance of the Tunisian economy is evidenced by the achievement of an average growth rate of 5.2 percent since 1996, when the Association Agreement with the European Union became effective, as well as by the diversification of the production base, with an increase in the share of the services sectors (58.2 percent in 2008, compared with 47.2 percent in 1996). Such an outcome can be attributed, in particular, to the emergence of new, buoyant, innovative sectors, characterized by a strong knowledge content, the GDP share of which has incessantly improved, rising from 12.8 percent in 1997 to 23.4 percent in 2008.

These performances have also been accompanied by an improvement in the contribution of the global productivity of factors (GPF), which rose to about 41 percent over the past five years, compared with 36 percent on average for the period of the IXth Development Plan (1997–2001). This can be attributed to the boost generated by the reforms launched to improve the business climate and ensure optimal allocation of available resources.

Investment has developed considerably, representing 25.1 percent of GDP in 2008, compared with 23.2 percent in 1996. This was accompanied by an increasing private sector contribution (61.5 percent in 2008, compared with 53.4 percent in 1996), attesting to the growing interest in the enhancement of private initiative.

There was also fresh momentum in foreign direct investment (FDI) as a result of the efforts made to improve the business climate generally and develop mechanisms likely to attract more investors of a new type and steer them toward areas that are promising and of priority for the national economy, such as manufacturing industries, communications, the financial sector, and infrastructure projects in the context of concessions. In this regard, FDI increased by 65.4 percent in 2006, 35.1 percent in 2007, and 50 percent in 2008, excluding privatization operations. Their share in GDP thus grew, reaching 5.6 percent in 2008, compared with 1.6 percent in 1996, and their share in global investment was 20.8 percent, compared with 6.2 percent in 1996.

Job creation intensified, totaling 79,800 in 2008; 90 percent of the additional demand was thus met. Nonetheless, the rate of unemployment remains high, at about 14 percent, although it has started to fall by comparison with its 1997 level (16.8 percent).

Moreover, the domestic and external financial balances have been preserved. The current account deficit and the budget deficit have been contained, respectively, at about 2.6 percent and 2.9 percent of GDP during the period 1997–2007, compared with 5.9 percent and 3.7 percent during the period 1992–96, and inflation has been controlled, holding at 3.1 percent in 2007, compared with 3.7 percent in 1996.

These performances resulted from the efforts made to enhance the competitiveness of the Tunisian economy and increase its integration into the global economy. Market share in the EU grew from 0.59 percent during the period 1997–2001 to 0.62 percent currently, and the indicator of catch-up with EU countries reached 30.2 percent for the period 1997–2007, compared with 25.1 percent during the period 1993–96. In this context, the rate of openness stood at 102.6 percent in 2008, compared with 86 percent in 1996, because of the buoyancy that has characterized foreign trade, especially in the area of exports, whose share in GDP grew to about 47 percent during the period 1997–2007, compared with 42.4 percent during the period 1992–96.

In addition, the productivity gaps by comparison with EU countries seem relatively low at about 27 percent in the sectors most open to competition, such as mechanical and electrical industries and the textiles sector, whereas these gaps reach 55 percent in the case of other sectors. The program to upgrade the industrial sector that accompanied the process of liberalization and integration into the global economy has helped improve the competitive capacity of Tunisia's industrial base. The Tunisian economy thus has large margins for improving its competitiveness and, therefore, for accelerating the rate of growth.

At end-2008, 4,145 industrial enterprises had joined the upgrading program, including 474 during the period 2007–08, compared with 500 projected by the XIth Plan for that period. The number of approved applications totaled nearly 2,843, for an overall investment amount of TD 4,670 million, and the grants made totaled TD 652 million.

An assessment of the program revealed that it contributed greatly to modernizing the productive apparatus, establishing quality and IT systems, and organizing management methods. The program also helped raise the management to staff ratio from 9 percent to 17 percent.

In addition, for further improvement of the corporate environment, a major industrial modernization program was established. Its main objective is to support the ongoing efforts to restructure the industrial sector and modernize the private sector through development by innovation and creativity, the consolidation of quality, metrology, and standardization, the promotion of industrial ownership, and the improvement and facilitation of access to financing for small and medium-sized enterprises.

At end-October 2008, the industrial modernization program had initiated 570 actions, 417 of which were completed for investments totaling some €27.4 million, or 86 percent of the program's operational budget of €32 million. It is noteworthy that nearly one-third of the investments relate to quality improvement programs.

Meanwhile, major social gains were recorded during this period, as can be seen from the improvement in the indicators related to education, higher education, vocational training, health, and living conditions generally. For instance, life expectancy at birth was 74.8 years in 2008, compared with 71.6 years in 1996; the enrollment ratio of the six to fourteen yearold cohort climbed from 86.2 percent in 1996 to 94.8 percent in 2008; and the real social coverage rate rose from 77 percent in 1996 to 93.3 percent in 2008.

These economically and socially convincing results represent the crowning of a sustained effort to implement wide-ranging reforms in a gradual, clear-sighted way. This reform drive was geared especially to continuing to open up the Tunisian economy through the completion, since January 2008, of the program to remove customs tariffs for industrial products, initiated in the context of the Association Agreement with the European Union. This action was accompanied by a gradual lowering of customs duties with Tunisia's other partner countries with a view to reducing trade diversion. These assorted measures paved the way for a harmonization of the various rules and procedures and for a reduction of corporate transaction costs. In this regard, real protection was reduced to 16 percent in 2007, compared with 73 percent in 1997.

This integration within the global economy was also pursued through the signing of partnership agreements with other regional groupings, such as the European Free Trade Association and the Arabic-Mediterranean Free Trade Agreement (Agadir Agreement), and at the bilateral level with Morocco, Egypt, Jordan, Syria, Libya, and Turkey.

The reform drive also concerned export promotion through the building of export promotion institutions and mechanisms, the adoption of a new customs code, and the pursuit of the reforms launched within the framework of two consecutive export development programs supported by the World Bank and seeking to build the export capacity of enterprises, including the use of the proposed single-bundle procedures for imports and exports and a transport-related bundle. The thrust of the reforms also concerned the simplification of customs clearance and goods removal procedures, as well as the facilitation and development of trade logistics. Efforts in this context were also geared toward helping exporters gain access to new markets and strengthening the export financing pre-shipment guarantee mechanisms.

Particular attention was also paid to encouraging private initiative and enterprise creation through the intensification of support and advice for new promoters, the development and modernization of support bodies, the simplification and reduction of administrative red tape, and the creation of one-stop shops and a network of enterprise nurseries and business centers, technological hubs, and support structures at the regional level.

In this regard, the December 2007 promulgation of the law on economic initiative was a decisive step forward on the path to investment liberalization and simplification of the procedures for enterprise creation, the protection of investors, the facilitation of access to financing, and the encouragement of micro-enterprises opening up new horizons to promoters.

The laying of the groundwork for a knowledge-based economy is one of the principal characteristics of the work done to develop Tunisia. The efforts ongoing in this area were intensified to ensure better use of the available sources of intelligence and knowledge through modernization of the systems of education, training, and higher education, and their inclusion in the knowledge-based economy, the promotion of scientific research and technological innovation, and the facilitation of access to the various components of the knowledge-based economy, in addition to the development and intensification of remote services in various areas.

The reforms also concerned improving the yield of the tax system and modernizing the financial sector. Indeed, a high point of the tax reform was the promulgation of the tax procedures and duties code, revision of the direct and indirect taxation rates, and modernization of the tax administration, especially as regards collection and control.

The financial sector, for its part, was the subject of sweeping reforms that affected all of its components. In the area of banking, the actions taken involved establishing rules for prudential management in conformity with international standards, restructuring the sector through the establishment of multipurpose banking and the privatization of a number of banks, and consolidating the banks' financial resources by purging their portfolios of problem loans and provisioning loans. Efforts were also geared toward modernizing the services provided by expanding electronic payment systems, introducing remote clearing, developing data centers, and diversifying financial products. The organizational framework of the Central Bank of Tunisia was also restructured with a view to increasing the control of monetary policy and modernizing its mechanisms, in particular by moving toward a policy of inflation targeting.

The financial market expanded because of the measures adopted throughout recent years to diversify securities, modernize mutual funds, encourage companies to become listed on the securities exchange, develop financial security, improve the market in debt instruments, develop risk capital, and establish an alternative market.

The insurance sector, for its part, is experiencing real momentum in its progress and development as a result of the overhauling of its legislative and institutional framework, related to strengthening the prudential regulations, the automobile insurance reform, the development of life insurance and other vibrant subsectors, such as export insurance and agricultural insurance, in addition to improving the services provided by reducing compensation time limits and procedures, boosting the internal management of insurance companies, and giving administrative autonomy to the general insurance committee to ensure proper functioning of the sector.

As regards human development, for the purposes of better meeting the economic growth and development needs and of encouraging the laying of the groundwork for a knowledge-based economy, steps were taken to improve the yield of the education, vocational training, and higher education systems. In this context, the education and schooling policy law was promulgated, and the university diploma system was revised through the gradual adoption of the LMD system in conformity with the pertinent international rules and standards and an increase of hiring capacity in the buoyant, labor-intensive subsectors. The arrangements made also relate to diversifying the vocational training subsectors, increasing the capacities of training centers, supporting scientific research, and opening up corporations to education and research structures so as to improve their yield and effectiveness.

Employment received particular attention and was hoisted to the highest level of national priorities. This position of choice can be explained by the interest shown in the human factor in triggering growth and achieving development objectives. It can also be explained by the increase over the past decade in the additional demand for work and the evolution of its structure.

The recommended employment policy was based, in particular, on accelerating the growth rate, promoting investment, and encouraging private initiative, as well as implementing and strengthening programs and mechanisms designed to improve the employability of those seeking work and to facilitate their inclusion in the world of work. These mechanisms, relating especially to the creation of the Tunisian Solidarity Bank and the National Employment Fund and to the introduction of a microcredit system, have, from their inception to end-2008, benefited 528,000 persons.

Meanwhile, various measures were decreed to encourage enterprises to recruit higher education graduates and foster private initiative, as well as to consolidate the actions of programs to promote the employment of young people.

Regional development has also received particular attention through the promotion of private investment in the priority regions and the strengthening of infrastructure and community facilities, as well as consolidation of the projects and programs designed to preserve the environment, protect natural resources, and improve living conditions.

The reform drive is continuing more vigorously within the framework of the XIth Plan, first in light of the objectives set for meeting national aspirations, especially in the area of growth and job creation, and secondly in light of the unfavorable economic developments, which began in 2007 with the upsurge in hydrocarbon and commodity prices and which continue with the outbreak of the financial crisis that has shaken financial markets and affected numerous international banks.

II. Outlook for development for the period 2009–11

Tunisia is approaching a new key phase in its development process, buoyed by its experiences and performances in all areas and aspiring to move forward and make progress toward a better future.

On this basis, the development objectives adopted for the XI^{th} Development Plan (2007–11) were formulated in conformity with the priorities identified as a result of national aspirations and bearing the imprint of far-reaching changes, both domestic and international.

At the domestic level, it is worth highlighting the importance of the demographic changes that have occurred and the resulting challenges in the areas of job creation, the health system, and maintenance of financial balances, as well as the pressures on natural resources. At the international level, the economic environment is marked by the acceleration of changes in light of the expansion of globalization, the exacerbation of competition, and the adverse trends characterizing the international economic scene, as well as commodity price fluctuations and exchange rate volatility.

The main objectives recorded in the XI^{th} Development Plan relate essentially to:

- Acceleration of GDP growth to an average rate of 6.1 percent. Achieving this objective in a context that has become more difficult requires the contribution of all the productive sectors. It will depend on the performances of the modern services sector and on the consolidation of the share of high value-added knowledge-based activities, which is expected to represent 27.5 percent of GDP in 2011, compared with 20.4 percent in 2006.

  The targeted growth rate also assumes continued improvement of the GPF, whose contribution to growth will be some 48 percent, compared with 41 percent over the past five years. This requires, in particular, the pursuit of human resource development, the more widespread use of new information and communication technologies, the development of research, and innovation for diversifying products and improving their competitiveness; and

- Pursuit of an income redistribution policy aimed at improving the human development indicator, consolidating the middle class, and reducing poverty.

Given the deep changes characterizing the domestic and international scenes as well as national aspirations and choices, the achievement of the above-mentioned objectives requires:

- Further integration of the national economy into the global economy through export promotion, inclusion in the international networks of production and distribution, the garnering of foreign direct investment, the development of partnership relationships with strategic investors, the facilitation of investment abroad by nationals, and access by national enterprises to external sources of financing;

- Optimization of the allocation of available financial and natural resources as well as human resource development to ensure the efficient use of available resources and so improve GPF and ensure the sustainability of economic growth;

- Preservation of the financial balances conducive to ensuring the soundness of the economy, improving its adaptability to exogenous shocks, limiting the impacts of the current economic reversals, and as far as possible meeting economic globalization needs. Achieving this objective depends on controlling the current account deficit, reducing indebtedness, preserving the budget balances, and containing inflation; and

- Consolidation of social progress and optimization of income policy in the direction of equity and poverty reduction, as well as establishing a positive social climate and strengthening the programs designed to preserve purchasing power and support people with special needs.

Accordingly, the fundamental pillars of the development approach for the current development plan (2007–11) are accelerating the economic growth rate, guaranteeing its sustainability, and intensifying its employment content, while safeguarding the stability of the financial balances and optimizing the allocation of available resources.

However, although the transition period for implementation of the Free Trade Agreement between Tunisia and the European Union ended in January 2008 and the economy is becoming more integrated into the Euro-Mediterranean space, new challenges are arising because of the volatility of commodity and raw material prices and the financial crisis that has created turmoil in the financial markets, with severe consequences for global economic activity.

This crisis has not affected the Tunisian financial market for several reasons: the securitization system is still extremely small and concerns only two well-managed operations totaling less than US$300 million. Real estate loans are granted at fixed interest rates based on the recipient's ability to repay and represent only 10 percent of all banking liabilities. Market capitalization accounts for only one-fifth of GDP. The investment of Tunisia's foreign currency reserves, for their part, is governed by strict prudential rules; these reserves are maintained in the form of sovereign securities denominated in dollars and in euros and within the limit of 30 percent of deposits with first-tier banks.

As regards the real economy, negative credit terms and considerably diminished household and enterprise confidence are weighing heavily on demand in Tunisia's main partner countries. As a result, Tunisia's main export sectors—namely, automobile components, textiles, and tourism—are affected.

As soon as the precursory signs of this crisis appeared, Tunisia remained constantly vigilant so as to forestall its consequences and perceive its effects on the national economy by creating a committee to monitor international economic and financial developments and propose adequate remedial measures.

In this context, major decisions on actions to be taken were made by the President of the Tunisian Republic on November 7, 2008 and a program was adopted with short-term measures to support enterprises in difficulty, in particular those involved in exporting, as well as structural measures linked to five key areas, namely: improving public sector services, streamlining foreign trade procedures, accelerating public investment programs essentially in the area of infrastructure and community facilities, strengthening vocational training, and consolidating the economic and financial fundamentals.

As a result of these measures and despite the economic recession, especially in the Euro Area (-2 percent in 2009 and 1 percent expected for 2010), GDP growth is projected at 4.5 percent in 2009 and will accelerate to 5.5 percent in 2010 and 6 percent in 2011. These levels remain, however, below the objective of 6.1 percent a year adopted in the XIth Plan and result from the slowdown in export growth, estimated at 1 percent in 2009.

Efforts will continue to control inflation and contain it at 3 percent a year for the next three years.

Preservation of the domestic and external financial balances will be pursued; the goal is to contain the current account deficit and the government budget deficit at reasonable levels compatible with the national economy's means of financing. The amounts saved by lowering the food and oil product subsidies are expected to allow for an increase in capital expenditure and support to economic enterprises in 2009.

Special attention will be paid to private investment through the pursuit and deepening of the reforms to improve the investment climate. In this regard, the Tunisian Government is firmly committed to further intensifying and accelerating the economic and financial reforms as part of the thrust toward extensive integration into the global economy, so as to seize the opportunities afforded by a greatly changing environment.

To that end, and to achieve the assigned objectives and build the capacity to withstand shocks, the Tunisian Government, in close consultation with its donors and lenders, has prepared a new integration support program and wishes to obtain substantial support from the World Bank, in the form of a quick-disbursing operation.

III. The Integration Support Program

The economic integration support program, designed in collaboration with the World Bank, the African Development Bank, and the European Union, seeks to support the Tunisian economy further on the path toward integration into the global economy. This follows the major steps Tunisia has made to improve competitiveness through a series of reforms introduced in four consecutive programs in support of economic competitiveness.

The program is of key importance, given its conformity with a number of milestones for the Tunisian economy, such as the effective establishment of the Free Trade Area with the European Union as of 2008 and the preparation of negotiations on the liberalization of the services and agriculture sectors, as well as the steps taken toward Tunisia's establishment as a regional business and services market.

This program falls within a particular context, marked by the advent of the global financial crisis, the effects of which are being felt by the national economy as a result of the contraction in external demand. The reform measures and actions planned under the program support the objectives set in the XI^{th} Development Plan and relate to improving the corporate environment, facilitating the entry of Tunisian enterprises into foreign markets, modernizing their management methods, and consolidating the vibrant sectors that generate employment for skilled persons.

On this basis, the program has three key components:

1. Reducing transaction costs and deepening commercial integration;
2. Improving the business climate; and
3. Improving access to financing.

1. Reducing transaction costs and deepening commercial integration. This objective falls within the framework of a discerning use of the opportunities afforded by the global market and the achievement of sustained integration within the global economy. The actions envisaged in this context will relate especially to the continued reconciliation of the merchandise tariff systems, so as to simplify them and reduce the risks of trade diversion, as well as to the convergence of standards and regulations with the main markets targeted.

They will also concern the development of export services in light of the sector's growing vibrancy, its huge potential, and its contribution to GDP growth and job creation. Particular attention will also have to be paid, in the context of this program, to streamlining the logistic services, given their role in increasing the competitiveness of the economy and facilitating foreign trade procedures.

More concretely, the commercial reform measures will relate to three key areas:

- Deepening the reforms related to merchandise trade by reducing the number of customs tariffs from nine to six in 2009 and from six to five at end-2010 and thus paving the way for a reduction in the average tariff to 17 percent in 2010, clarifying the import control system, facilitating commercial procedures and transactions, strengthening the standards and rules on quality, and consolidating the mechanisms to combat counterfeiting;

- Pursuing the reforms related to trade in services by increasing the prerogatives of the National Services Council through the creation of a management unit for each objective, endowed with adequate budgetary and human resources, as well as adopting an action plan for the reform and promotion of those services sectors with high commercial potential, based on an analysis of the regulatory framework to be established. The key areas of reform in this regard should also concern improving the statistics apparatus related to services activities and trade, by adopting a common classification of services, and creating an information and statistics system on international services activities and trade, as well as adopting an action plan for upgrading the services sectors so as to encourage and facilitate exports; and

- Streamlining logistic services by reducing port transit costs and time limits and facilitating international logistic operations for exporters and service providers on the basis of the new customs code arrangements.

2. Improving the business climate. The business climate has received special attention and, over the past few years, has established a record of development work structured around private sector vibrancy and integration into the globalized economy. Improvement of the business climate will continue in the coming period with a view to increasing the competitiveness of the economy further, encouraging private initiative, and attracting more foreign direct investment.

The key areas of the program will be geared, at this level, toward:

- Continuing to improve the administrative arrangements governing corporate activities by effectively reducing to seven days the time limit for VAT refunds on export products, replacing one-half of the remaining approvals with specifications, establishing and putting online the new trade register system, and reducing the time limits for making industrial land available;

- Improving reporting and the regulatory framework for better convergence of labor supply and demand by compiling a guide on labor legislation for enterprises, preparing training modules on labor regulations, and studying some aspects of the labor market; and

- Increasing the protection of investors in the society and the transparency of market corporations by amending the companies code to enable minority shareholders to gain access to information on a company's position, go to court, and manage risky operations involving conflicts between the personal interests of executives and those of the corporation they manage.

The legislative and regulatory environment of competition, for its part, has received special attention, in that the attributions of the competition council have been strengthened, its administrative and financial autonomy has been established, and a requirement has been introduced to seek its opinion on certain legal documents. Actions will continue in the context of this program to strengthen its involvement in specification reviews and increase the human resources available to it.

3. Improving access to financing. The development of nonbank financing for enterprises represents the pillar of the financial policy reform for the coming period. The aim is to consolidate the banks' financial resources, reduce the over-indebtedness of enterprises and increase their capital, and shore up the economy against vulnerabilities to shocks in a context of growing integration.

With this in mind, the logic of financing should be based on better risk management by the banks and proper assessment of the profitability of investment projects, in addition to implementing the Basel II principles on prudential regulation, reforming the investment capital legislative and regulatory framework, increasing the depth and liquidity of the financial market with a view to giving a further boost to the Tunis securities exchange and enhancing its role in the financing of private investment, and developing microfinance activities.

The reforms adopted by the program in this area will relate to:

- Improving the effectiveness and competitiveness of the banking sector by reducing the weight of classified claims in bank portfolios to 15 percent in 2010, increasing the rate of provisioning by the banks to 70 percent in 2010, and establishing a Basel II action plan, as well as strengthening the guarantee system by developing the indemnification arrangements and pricing policy of the Tunisian Guarantee Company;

- Reforming the legislative and regulatory framework of investment capital, in particular by improving conditions for the outflow of project capital on the basis of corporate performances and adopting an accounting framework specific to risk capital activities, based on international accounting measures regarding risk capital;

- Building the depth and liquidity of the financial market, in particular by increasing privatizations through the securities exchange, enhancing the liquidity of the share and bond markets by raising the share of treasury bills for auction that foreigners are allowed to acquire from 20 percent to 30 percent, and authorizing international institutions to issue debenture debt on the Tunisian financial market on the same conditions as local operators; and

- Developing microfinance activities by improving the performance of the Tunisian Solidarity Bank.

In conclusion, the Tunisian Government believes the program of reforms outlined in this letter will enable Tunisia to consolidate its process of integration into the global economy, increase its competitiveness, and take up the challenges it will face in the future, especially as Tunisia will have, in coming years, to bear the impact of the global economic crisis that is currently rocking the economies of all the countries in the world. The implementation of this program would be largely facilitated if the request for a quick-disbursing operation in the amount of US$250 million were to be accepted by the World Bank.

/s/

Mohamed Nouri Jouini
[Seal of the Ministry of Development
and International Cooperation]