REPUBLIC OF TUNISIA

Social and Structural Review 2000

Integrating into the World Economy and Sustaining Economic and Social Progress

FOREWORD

Tunisia has sustained a very good economic and social performance since the late 1980s by maintaining a stable macroeconomic framework, placing strong emphasis on social achievements, and implementing — although very gradually — a number of key structural reform measures. Today, Tunisia's ambition is to build on its past economic and social successes to integrate into the global economy and achieve higher living standards.

It is a challenging goal — considering that the conditions that made Tunisia's success possible in the past decades are being fundamentally altered by developments in the international markets. The elimination of the Multi-Fiber Arrangements scheduled to be completed by the end of 2004 will bring about stronger competition for Tunisian producers in their export markets. Also, the implementation (over the period 1996-2007) of the free trade provisions of the Association Agreement signed with the EU in 1995, and free trade agreements recently signed with Arab partners, will intensify competition in the local market.

While trying to manage its integration in the global economy and realize its long-term development goal, Tunisia faces social tensions. For example, pressures are emerging in the labor market as some firms facing foreign competition try to reduce their employment and as young graduates are not finding jobs easily. As a result, unemployment is expected to remain high for the next five years or so.

Faster economic growth is required to achieve the dual goal of increasing rapidly living standards and reducing unemployment. However, the achievement of faster growth critically depends on the economy's ability to realize higher and more efficient private investments. This in turn will require that government reduce its involvement not only in producing goods and commercial services but also in decision-making processes in the private sector.

This report — one of a few pilot Social and Structural Reviews initiated in 1998-99 by the World Bank to enhance its knowledge-base and better contribute to policy dialogue with client countries — takes stock of Tunisia's development achievements both on historical grounds and in comparison with other countries in the MENA region and the middle-income group. The report offers options for adapting Tunisia's development model to its new environment. Through this report, the World Bank hopes to contribute — along side its Tunisian partners — to securing a prosperous future for the Tunisian people.

Jean-Louis Sarbib
Vice-President
Middle East and North Africa Region

June 19, 2000

ACKNOWLEDGEMENTS

This report was prepared by a core team comprising Daniela Gressani (Task Team Leader), Auguste T. Kouamé, François Lacasse and Nadir Mohammed (World Bank), Patrick Grady and Michel Paquin (Consultants). The core team benefited from helpful comments from a high-level task force organized by the Tunisian government. Essential contributions were made by Reçai Cecen, Giulio De Tommaso, Fatma Felah, Afef Haddad, Ingrid Ivins, Elena Morachiello, and Bertin Thériault. Invaluable inputs were provided by the teams preparing the Private Sector Update, led by Hamid Alavi, and the Social Conditions Update, led by Setareh Razmara. Helpful comments were received from Pedro Alba, Milan Brahmbhatt, Hassan Fazel, Edward Gardner (IMF), Malcom Holmes, Brendan Horton, Ali Khadr, Homi Kharas, Dorsati Madani, Sandeep Mahajan, Manuel Schiffler, Helcio Tokeshi, Zafiris Tzannatos, Willem Van Eegen, and Sona Varma. Khalid Alouane, Ilonka Csekey, Mary Lou Gomez and Marie-Huguette Osselyn contributed to the production of the document. The report was edited by Joost Polak. The team gratefully acknowledges the support and encouragement of Messrs. Kemal Dervis (Regional Vice-President), Christian Delvoie (Country Director, Maghreb), John Page and Mustapha Nabli (Chief Economists and Sector Directors).

Table of Contents

List of Figures

List of Tables

List of Boxes

List of Annexes

List of Annex Tables

CURRENCY AND EXCHANGE RATE

(Unit of Currency = Tunisian Dinar)

	1993	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**
TD per US$, period average	1.004	1.012	0.946	0.973	1.106	1.139	1.184
TD per US$, end-of-year	1.047	0.991	0.951	0.999	1.146	1.101	1.260

FISCAL YEAR OF BORROWER

January 1 - December 31

ABBREVIATIONS AND ACRONYMS

AMG	*Assistance Médicale Gratuite*
CNRPS	*Caisse Nationale de Retraite et de Prévoyance Sociale*
CNSS	*Caisse Nationale de Sécurité Sociale*
COPIL	*Comité de Pilotage*
CPI	Consumer Price Index
EU	European Union
FODEC	*Fonds de Développement de la Compétitivité*
GDP	Gross Domestic Product
GNFS	Goods and Non-Factor Services
GNP	Gross National Product
IACE	*Institut Arabe des Chefs d'Entreprises*
IMF	International Monetary Fund
INS	*Institut National de la Statistique*
MENA	Middle East and North Africa
MFA	Multi-fiber Arrangements
NGO	Non-Governmental Organization
OECD	Organization for Economic Cooperation and Development
REER	Real Effective Exchange Rate
SME	Small and Medium Enterprises
SICAR	*Société d'Investissement à Capital Risque*
SITC	Standard International Trade Classification
TD	Tunisian Dinar
VAT	Value Added Tax
WTO	World Trade Organization

EXECUTIVE SUMMARY

A Strong Record

Tunisia has sustained the best economic performance in the MENA region since the late 1980s by maintaining a stable macroeconomic framework and placing strong emphasis on social achievements. Today, Tunisians have a per capita GDP of about $2,200—more than two-and-a-half times the real income their parents had 30 years ago—and all indicators of their social and economic wellbeing have significantly improved. Poverty incidence has been reduced from 40% in the 1960s to about 7% in the mid-1990s, almost all children attend school, life expectancy has reached 70 years, and women make up one third of the labor force.

Behind Tunisia's successful economic performance lies a solid record of macroeconomic management and a persistent, although very gradual, approach to structural reform. Starting in 1986—when a sharp fall in oil prices nearly precipitated a balance of payments crisis—Tunisia has maintained a prudent macroeconomic framework, reduced the fiscal deficit, improved control over monetary aggregates, and managed the exchange rate flexibly. As a result, inflation has been reduced, while the real exchange rate has remained stable. During the same period, Tunisia introduced—though it has not yet fully implemented—many of the reforms necessary for sustained economic growth. These reforms have led to a significant increase in the private sector's contribution to investment, exports, and job creation.

The Case for Rethinking Tunisia's Development Strategy

Tunisia's ambition is to build on these economic and social achievements to join the ranks of the developed countries in the early decades of the 21^{st} century. Reaching this goal would require significantly higher GDP growth. One growth scenario that would allow Tunisia to catch up with the lower income OECD countries such as Korea and Portugal by 2025 requires average annual GDP growth of 6.6% in the next five years and 8.6% over 2005-25, compared to an average of 5% during the 1990s. Sustaining such high growth—which has been achieved historically by only a few countries, such as the fastest growing countries in East Asia—would be a formidable challenge even for an economy performing as well as Tunisia.

Joining the ranks of developed countries will require quantitative and qualitative leaps forward on many fronts. A Tunisia with a per capita income of $10,000 to $12,000 —the current level of Slovenia, Portugal, or Korea—would look very different from today. The number of Tunisians living in poverty would be far below today's 690,000. The education system would produce a larger number of graduates trained for higher-skill jobs. The manufacturing and services sectors would be much larger, and agriculture correspondingly smaller. The private sector would make up much more than 60% of investment, and enterprise output. Exports would have a broader base and higher value added. Infrastructure and financial services would have reached OECD standards, and be largely provided by the private sector in a competitive framework. Public sector efficiency would be greater, and its contribution to overall economic performance correspondingly larger. A broad-based civil society would actively promote transparency and greater efficiency in the public sector through open scrutiny.

Does Tunisia need to rethink its development strategy—a strategy that has served it well thus far, and that is likely to continue to support economic growth at historical levels in the near future—to achieve its ambition? There are six main reasons to propose an affirmative answer:

- Poverty incidence was not reduced between 1990 and 1995 (the most recent year for which poverty data are available), in contrast to the steady decline achieved since 1960. The lack of progress in poverty reduction between 1990 and 1995 was partially caused by bad agricultural performance following the 1993-95 droughts. Yet, it remains disturbing, as it occurred during a time of sustained overall economic growth and continuous attention to social development through investment in health, education, and basic infrastructure.

- Unemployment remains high, especially for first-job seekers, despite a decade of robust growth and job creation and fairly stable participation rates. Prospects for reducing unemployment are not good because of rapid growth of working age population and likely increases in female participation rates in the near future.

- The conditions that made Tunisia's success possible in the recent past are being fundamentally altered by developments in the international markets. Tunisian producers will face much stronger competition in their export markets after the elimination of the Multi-Fiber Arrangements (MFA) scheduled to be completed by 2005, and in the local market with the full implementation in 2007 of the free trade provisions of the Association Agreement signed with the EU in 1995.[1] The current approach to private sector development—based on picking winners—has been successful because it has been implemented by a competent administration, in a predictable environment, and with relatively few players. Itis unlikely to continue to be successful in a more competitive environment where past performance will not be a good indicator of future success. In the new era, a predictable and transparent policy environment will be much more important to facilitate enterprise adjustment—entry of new and competitive firms, and disappearance of non-competitive ones—than finely targeted incentives and discretionary interventions.

- The competitiveness of Tunisian enterprises will increasingly depend on the cost and quality of infrastructure and financial services. The agreement with the EU is expanding access to inputs at world prices to the on-shore sector of the economy, and thus differences in competitiveness between Tunisian producers and their competitors will be largely determined by cost and quality of non-tradables. Yet infrastructure services, especially in transport and telecoms, are largely provided by the public sector in markets that are neither competitive nor contested; and they remain behind those available to competitors in many other emerging market economies. The financial sector is dominated by public banks, suffers from operating inefficiencies, and is not responsive to the needs of small and medium enterprises. Despite recent steps to eliminate past losses and establish a sound regulatory framework, banks could again accumulate non-performing loans if enterprise adjustment is not successful.

- To join the ranks of the developing countries within the next two to three decades, Tunisia will need to develop more efficient public institutions. Public sector performance is a key element in overall economic competitiveness. It

[1] Even though in the short-term, some domestic firms will benefit from an increase in the effective rate of protection because of tariff reductions on imports of semi-finished manufactured inputs while tariffs on imports of competing manufactured products are maintained for a while or only gradually reduced.

affects the quality of the regulatory framework supporting the private sector, and the quality of public services used by households and investors, and thus the skills of the labor force. An efficient public sector also reduces the costs – in terms of time and effort – directly borne by citizens and businesses to gain access to public services or comply with public sector regulations, and raises the attractiveness of Tunisia to foreign investors.

- A more open and diverse civil society could greatly contribute to meeting the challenges posed by the changing external environment, the stagnation of poverty, and the aspirations of Tunisia's middle class and its younger generations entering the labor force. Tunisia has developed a system of social consensus that has ensured social stability and continuity in decision making—but has also contributed to the slow implementation of structural reforms and has limited the development of a broad-based civil society.

Toward a New Strategy

The reasons for rethinking Tunisia's development strategy also provide a guide as to what elements are necessary to make progress toward realizing the country's development ambition:

➢ **Build better information and closer community involvement for more effective anti-poverty interventions**. More effective anti-poverty interventions will require more timely and more widely shared information, as well as closer involvement of the affected communities in their design and management. The stagnation of poverty incidence despite rapid growth is disappointing, but not surprising, as targeting anti-poverty interventions becomes harder as poverty incidence falls. Yet information on the characteristics of the poor, the causes of poverty, and the relationship between skills and opportunities is not widely available in Tunisia, despite efforts to collect household-level data. As a result, interventions have not evolved to address emerging trends, such as peri-urban poverty or the persistence of unemployment—which is suspected to be on the rise for heads of poor households. In addition, the strong participation at the community level needed to tailor interventions to beneficiary needs, and to monitor results—especially in a rapidly evolving economic and social environment—has not yet developed.

➢ **Improve labor market flexibility**. As the economy moves closer to international integration, the competitiveness of firms—and their ability to create jobs in the longer run—will depend on their ability to restructure, including by shedding labor and changing the skill mixes of their labor forces. For this reason, labor market flexibility is critical in the adjustment period. The government will need to reshape its role in the labor market as a regulator, while at the same time consolidating Tunisia's positive record in labor relations and working conditions. Interventions in this area should include policies to deal with redundancies in the public and private sectors, encourage firms to invest in on-the-job training, and promote entrepreneurship. Emerging tensions in the labor market—resulting from uncertainty about job tenure and deterioration in relative wages for lower-skill workers—will need to be closely followed through comprehensive monitoring of unemployment, including its duration, and skill composition and location. In addition, education reform will be critical to improving the responsiveness of the education system to emerging labor market demands.

➢ **Focus on the enabling environment for private sector development**.

Ultimately, it is investment by private enterprises that will generate growth, exports, and jobs. Tunisian authorities should go beyond providing support to those existing enterprises participating in the *mise à niveau* program, and focus on the environment creating and expanding private businesses—especially small and medium firms.[2] These firms represent indeed the largest and most dynamic group in the industrial sector, and have the potential to respond flexibly to rising competition in domestic and international markets. Fiscal and financial incentives are too finely targeted and should be consolidated, and the overall incentives framework should be thoroughly reviewed with the objective of leveling the playing field within the private sector and avoiding the sprawling of footloose industries that take advantage of short-term opportunities. This approach would not only benefit small and medium firms; it would improve the prospects for success of the sizeable investments being undertaken in the context of the *mise à niveau* program.

- **Deepen the restructuring of the banking sector**. A number of problems recently identified in the Tunisian banking sector are being addressed. The regulatory framework is being strengthened to reduce future risks of non-performing loans and contingent liabilities for the government. However, to increase access to finance and reduce the cost of borrowing—especially for small and medium firms—and improve the overall efficiency of the credit market, it will be necessary to implement more forcefully the outstanding reform agenda, including opening the sector to competition and diversifying financial services.

- **Introduce competition or at least contestability in the service sector**. Improving the cost/quality mix of infrastructure and non-tradable services could be the most important source of greater competitiveness for Tunisian enterprises in the near term. In this area, detailed measures have already been elaborated in Tunisia, focused on increasing competition and/or contestability through deregulation, privatization, and private provision, especially in transport and telecoms. These measures should be rapidly implemented and expanded on the basis of new knowledge to eliminate the disadvantage of Tunisian businesses vis-à-vis their foreign competitors.

- **Introduce result-based governance systems for a more efficient public sector**. Progress on all fronts—from private sector development to poverty reduction—will require a more efficient public administration, and Tunisia's substantial success in modernizing its public sector suggests that further significant gains are within reach. The record of countries that have experimented with reforming public sector governance during the last 20 years indicates that supporting continuous productivity growth in the public sector requires moving away from a system based on controlling inputs toward a result-based system focused on the actual achievement of public objectives.

- **Strengthen the basis for consensus through broader participation**. The social compact that has ensured social stability and continuity of economic policy making in Tunisia was founded on widely shared economic prosperity. This foundation is, however, likely to erode as competitive pressures brought about by increasing integration in the world economy generate uneven opportunities for different social groups—the younger generations and

[2] The *mise à niveau* program was introduced in 1996 to raise the competitiveness of Tunisian enterprises in the more competitive environment brought about by trade liberalization.

the established middle class, higher and lower-skilled workers, workers in emerging manufacturing and services sectors and workers in traditional occupations, women entering the labor force, and laid off workers. To ensure the sustainability of Tunisia's international opening, a new social compact needs to emerge through participation—transparency, openness, and voice—in public institution decision making processes. Participation can be consistent with different institutional arrangements, but "*must entail open dialogue and broadly active civic engagement, and […] that individuals have a voice in the decisions that affect them*".[3]

The quality of macroeconomic management and the structure of its economy strongly suggest that Tunisia can maintain its performance at recent levels. In particular, neither fiscal nor external sustainability is under threat in the near future. Closer integration in the world economy will, however, make macroeconomic stability even more important for success, and will thus require further consolidation of Tunisia's macroeconomic management.

Fiscal aggregates—and in particular to the dynamics of public debt—will continue to require close monitoring. The stock of public debt is high at about 55% of GDP, and recent episodes involving the assumption of public enterprise debt by the budget indicate that it may still grow. This points to three areas of concern. First, there remains a need to establish a single focal point for the early identification of contingent liabilities, which remain the most likely source of a negative shock to fiscal balances in the medium term. Second, a deterioration in the primary balance—which could result from larger than expected losses of trade tax revenues, or an acceleration of public investment—should be avoided. Third, a negative shock on external balances would likely generate a need for fiscal adjustment. This would be difficult under the current budget structure, which is characterized by increasingly rigid expenditures because of the dominant weight of obligatory expenditure items such as civil service wages, interest payments on public debt, and key social protection expenditures.

Maintaining a prudent borrowing strategy and flexible management of the exchange rate will also continue to be important to maintaining external sustainability. The free trade component of the association agreement with the EU amounts to a unilateral reduction in protection; this is already leading to an increase in imports and is likely to give rise to downward pressures on the exchange rate. These pressures will need to be managed decisively to maintain a positive external outlook for Tunisia—which would help ensure adequate access to private capital markets and sustained inflows of foreign investment.

In sum, Tunisia has reached a threshold, by continuously—and gradually— adapting its development strategy to ensure sustained economic growth. Now, to fully realize its ambitions of economic prosperity and social development beyond the current threshold—and especially to meet the new challenges brought by opening to international competition—Tunisia needs a new strategy. This report seeks to highlight possible directions for this new strategy, building on the strengths that have brought Tunisia to its current level of economic and social development.

---

[3] Stiglitz, J. (1999), *Participation and Development: Perspectives from the Comprehensive Development Paradigm*, speech delivered at the Political Leaders' Symposium on Leadership, Governance and Development, held in Seoul, Korea, February 1999.

Social and Structural Policy Matrix

Objective	Social and structural policy recommendations	Beginning of the implementation period: Short term: 1 to 2 years Medium term: 2 to 5 years
1. Improve the effectiveness of anti-poverty interventions	Conduct more frequent analyses of social conditions and make public the results of surveys on living standards	Short term
	Establish a closer involvement of the affected communities in the design and management of anti-poverty interventions	Short term
	Target more effectively microfinance programs in support of entrepreneurship	Short term
2. Improve labor market outcomes and prevent social tensions		
2a. Improve labor market flexibility and strengthen the monitoring of the evolution of employment	Simplify hiring and lay-off procedures and decrease government direct intervention in the labor market, while at the same time maintaining Tunisia's positive record in labor relations and workers conditions, and introducing measures to deal with redundancies in the public and private sectors	Short term
	Conduct more frequent analyses to improve monitoring of unemployment – including its duration – for different types of workers, industries and regions	Short term
	Establish mechanisms to ensure timely circulation of information on demand and supply of jobs among potential employers and employees	Short term
	Implement policies designed to encourage firms to invest in on-the-job training for their workers	Short term
2b. Improve the education system's capacity to adjust and meet the new demands of the labor market	Introduce an evaluation and remediation system to improve performance at all levels of education (teachers, schools, student achievements, and learning materials)	Short term
	Upgrade the quality of teaching by intensifying efforts to recruit qualified teachers, by improving teacher training and conditions of service, and by supporting research on the education system	Short term
	Introduce new methods of teaching, and adapt the learning environment and curricula to changing economic conditions	Medium term
	Involve private employers in the design and implementation of vocational training strategies	Short term

Objective	Social and structural policy recommendations	Beginning of the implementation period: Short term: 1 to 2 years Medium term: 2 to 5 years
2c. Continue improving the quality, efficiency and equity of the health care system, in order to consolidate social achievements	Better apply the criteria for access to the AMG II passbook so as to limit its use only by vulnerable persons, while ensuring that the really needy have access to free health care (through the AMG I passbook)	Short term
	Improve the regulation of the private health system, and improve its integration in the health sector	Medium term
	Introduce a health information system to monitor and evaluate the resources, activities, costs, quality, results and performance record of both the public and private health sectors	Medium term
2d. Strengthen the social security system	Improve the current system of social security by strengthening the financial position of social security funds	Short term
	Reform the social security system by creating a multi-pillar scheme with, on the one hand, a public scheme operating on a pay-as-you-go basis and offering basic pension benefits, and, on the other hand, a mandatory savings scheme based on individual capitalization accounts	Medium term
	Generate political consensus by consulting and informing the public on the details of the reform of the social security system	Medium term
3. Focus on improving the enabling environment for private sector development, especially for the SMEs		
3a. Go beyond the *mise à niveau* of existing firms and focus on creating an enabling environment for the creation of new firms	Consolidate fiscal and financial incentives, which at present are too finely targeted; and harmonize the various incentives available to enterprises	Short term
	Move ahead with privatization in all economic sectors, which will help strengthen the viability of external balances (see recommendation No. 8 below)	Short term

Objective	Social and structural policy recommendations	Beginning of the implementation period: Short term: 1 to 2 years Medium term: 2 to 5 years
3b. Increase access to finance and reduce the cost of borrowing – especially for SMEs	Strengthen credit analysis and management capacity in venture capital firms (SICAR) and banks	Short term
	Target more effectively microfinance programs in support of entrepreneurship, which will contribute in turn to employment creation (see recommendation No. 2)	Short term
3c. Introduce more competition in the production of services	See recommendation No. 5 below	
4. Deepen the restructuring of the banking sector	Move ahead with the privatization of public banks	Short term
	Accelerate the liberalization of the banking sector including by allowing the entry of foreign banks	Medium term
5. Introduce competition or at least contestability in the service sector, in order to improve the cost/quality mix, the availability and reliability of the services used by industries and the private sector in general	Strengthen the regulatory framework for telecommunications in order to ensure competition among private actors (whose number is bound to grow)	Short term
	Increase private sector participation in telecommunications and information technology	Short term
	Accelerate the privatization of the traditional telephone services, while ensuring that rural areas have adequate access	Medium term
	Increase competition in internet service provision	Short term
	Liberalize other sectors that provide essential services for economic activity, such as electricity and shipping (e.g. finalize the restructuring and privatization of the state maritime company, and the state port handling company)	Short term
	Improve information services on export markets, available technologies, international norms and standards -- especially for SMEs and export firms	Short term
	Strengthen the capacity of public institutions that deliver services to the private sector, including judicial services, enforcement of patent laws, metrology services, contracts and property rights, conflict resolution and arbitration	Medium term

Objective	Social and structural policy recommendations	Beginning of the implementation period: Short term: 1 to 2 years Medium term: 2 to 5 years
6. Introduce a result-based governance system for a more efficient public sector		
6a. Facilitate the use of existing measures in order to improve productivity	Expand the information collected, to include broad measures of users' satisfaction with public services, and use rigorous methods to assess the performance of public administrations	Short term
	Make public the information on the results achieved with respect to the relations between citizens and the administration	Short term
6b. Make those public enterprises that are not to be privatized truly independent and accountable for the fulfillment of clearly defined objectives	Avoid non-transparent or discriminatory business practices among public enterprises, including arrears accumulation or special discounts	Short term
	Clarify the dividend policy of the State as shareholder	Short term
	Quantify and reimburse the cost of fulfilling public policy mandates, by extending to all public enterprises the budget treatment that currently applies only to enterprises that receive transfers from the government budget	Medium term
	Allow full discretion to public enterprise managers on the choice of productive inputs	Medium term
	Take fully into account the productivity gains expected from firms in setting administered prices	Medium term
	Use a limited number of economic indicators -- for example, return on capital -- to measure performance; and assess performance on the basis of external audits and evaluations (to be made public)	Medium term
	Clarify the incentive framework for public enterprises, for example by establishing clean and predictable treatments of profits and transfers to the budget, and by modernizing the pricing policies	Medium term
	Introduce prior ministerial approval of business plans in a multi-year framework, and ex-post controls on an annual rolling basis to establish consistency with agreed objectives	Medium term

Objective	Social and structural policy recommendations	Beginning of the implementation period: Short term: 1 to 2 years Medium term: 2 to 5 years
6c. Adopt result-based management in public administration	Introduce a system of budget allocations centered on results and based on a functional classification of expenditures and linking budgetary outlays with results achieved	Medium term
	Devolve financial management authority to public managers, in order to enable them to make full use of the superior knowledge they have by virtue of being close to users and to the point of production and delivery of public services	Medium term
	Modify the functions of the Ministry of Finance, toward increased emphasis on policy analysis and monitoring of results	Medium term
6d. Launch a productivity drive, in order to mobilize existing energy for modernization and innovation	Establish benchmarks and targets for productivity in a multi-year framework, integrated with the budget process, supported by adequate technical resources, and monitored for progress	Medium term
7. Strengthen the foundations of the social compact by broadening public participation	Broaden public debate on the challenges of economic integration and globalization so as to reduce tensions that might be generated by uneven opportunities for different social groups – the younger generations and the established middle class, higher-skill and lower-skill workers, workers in emerging manufacturing and services sectors and workers in traditional occupations, women entering the labor force and laid off workers	Short term
	Ensure the participation of a greater number of people in the decisions taken within public institutions, through grater transparency, openness and voice	Short term

Objective	Social and structural policy recommendations	Beginning of the implementation period: Short term: 1 to 2 years Medium term: 2 to 5 years
8. Maintain a prudent macro-economic stance		
8a. Maintain flexible management of fiscal aggregates	Monitor closely the primary balance of government budget	Short term
	Strengthen the management of contingent liabilities by establishing a focal point within the Tunisian administration for the early identification of possible liabilities	Short term
8b. Safeguard the viability of external balances and maintain access to international financial markets	Maintain a flexible management of the exchange rate; monitor the level, term structure, and currency composition of external debt; manage the repayment cycles of external debt with caution; develop national financial markets.	Short term
	Attract foreign investment through large-scale privatizations	Short term

Chapter 1. Growth Performance and Macroeconomic Management

A. Introduction

1. Tunisia has been one of the fastest growing economies in North Africa and the Middle East (MENA) since the mid-1980s. Today, with a per capita GDP of about $2,200, Tunisians have more than two-and-a-half times the real income their parents had 30 years ago, and all indicators of their social and economic wellbeing have improved significantly. Almost all Tunisian children attend school, compared to only 80 per cent for the MENA region as a whole, and female labor force participation is high in a regional context (Table 1.1). In Tunisia, more children survive their first few years, and life expectancy is higher than the average for both lower-middle-income and MENA countries. As of the early 1990s, less than 10 percent of the population lived in poverty, and inequality had not worsened since the 1960s—with a Gini coefficient hovering around 0.4.[1] As a result of these social and economic achievements, the Tunisian middle class has expanded and includes some 80% of the population. This broad middle class has contributed to Tunisia's stability.

2. The Tunisian authorities emphasize in the IXth economic development plan (1997-2001) that it is Tunisia's ambition to join the ranks of developed countries during the first few decades of the 21st century.[2] This poses a formidable challenge, as Tunisia remains well below even the lower-income OECD countries in economic and social terms (Figure 1.1). Tunisia's per capita income is one fifth of that of Korea or Portugal. And at its current growth rate it will take Tunisia more than half a century to be where Korea and Portugal are today. .Tunisia's infant mortality is three times higher than that of Korea and six times higher than Spain's. Moreover, average years of schooling—a key indicator of the skills of the workforce—remains significantly lower than in OECD countries.

[1] Bruno, Ravallion and Squire (1996).

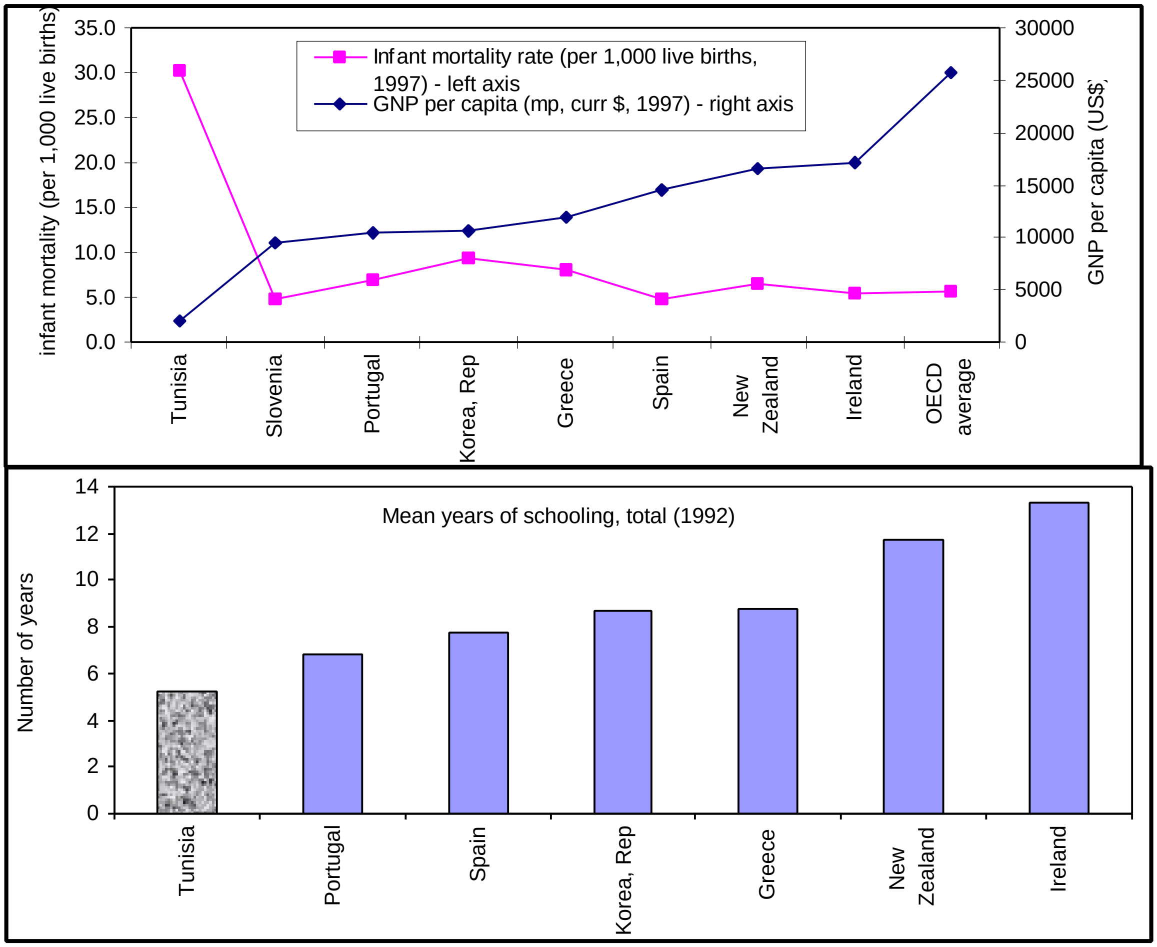
[2] The objective of transforming Tunisia into a developed country early in the 21st century is stated in several official documents and speeches. See for example Ministère du Développement Economique (1996 and 1997)

Table 1.1: Tunisia and Comparators: Selected Economic and Social Indicators

Indicators	Tunisia		Lower-middle income countries		Middle East and North Africa Region	
	Mid 1980s*	**Late 1990s****	**Mid 1980s***	**Late 1990s****	**Mid 1980s***	**Late 1990s****
GDP per capita ($, current)	1,158	2,137	1,422	1,665	2,852	2,512
GNP per capita ($, current)	1,160	2,060	1,250	1,740	1,990	2,000
Life Expectancy at Birth (total, years)	63.7	72.00	64.9	68.4	59.7	67.6
Infant mortality **[per 1,000?]**	59.4	28.1	52.8	35.3	86.5	45.8
School enrollment (primary, net)	93.1	97.6	83	87.8	78.9	86.6
Labor force (% female)	29	31.2	39.9	40.1	23.9	26.9
Public Expenditure on Health (% of GDP)				3.4		3.4
Public Expenditure on Education (% of GNP, UNESCO)	5.8	7.7	3.75	4.9	6.3	5.2
Fertility Rate (total, births per woman)	4.8	2.2	3.6	2.5	6.1	3.5
Safe Water (% of population with access)	89	99	60.3	71	67.8	87.5
Sanitation (% of population with access)	52	96	55.8	62	67.8	81
CO2 Emissions (kg per 1995 US$ of GDP)	0.93	0.84	1.3	2.66	1.74	2.09

* refers to data from 1982 to 1987.
** refers to data from 1994 to 1998.
Source: World Bank, *World Development Indicators*

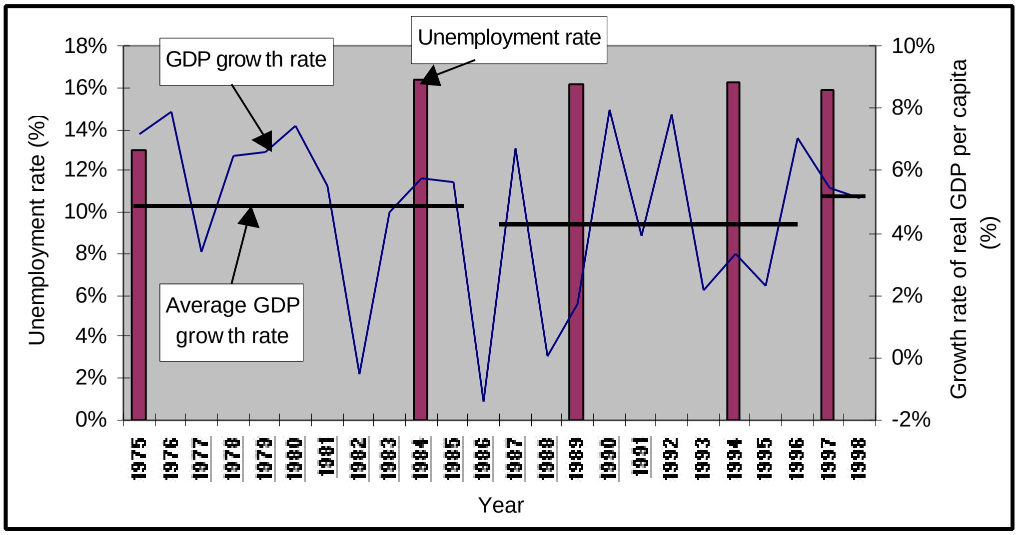
Figure 1.1: Tunisia and Lower-Income OECD Countries: Gaps in Socio-Economic Achievements



Source: World Bank, *World Development Indicators*, 1998 and INS, *Population Census*, 1994

3. As Tunisia attempts to close these gaps, it is already beginning to face some of the social and economic problems that prevail in more developed countries, such as persistent unemployment and rising urbanization. The unemployment rate has risen from 13% in 1975 to an average of over 16% over 1984-94, reflecting the slowdown in economic growth from an average of 4.9% over 1974-86 to 4.3% over 1987-96 (Figure 1.2). Although economic growth has recently recovered (to 5.3% on average for 1997-98), this has not yet resulted in declining unemployment, which has remained close to the 16% mark. In addition, there are indications that social tensions may be increasing, owing to reduced job security, growing cost of services, and widening income disparities. The urbanization rate—the ratio of urban to total population, now at 64%—and the speed of urbanization are higher than in most lower-middle-income countries (Figure 1.3). In fact, at 3.3% on average between 1980 and 1998, growth of the Tunisian urban population is twice that of the population as a whole.

Figure 1.2: Tunisia: Growth and Unemployment



Source: World Bank, *World Development Indicators*, INS Population Census, 1994

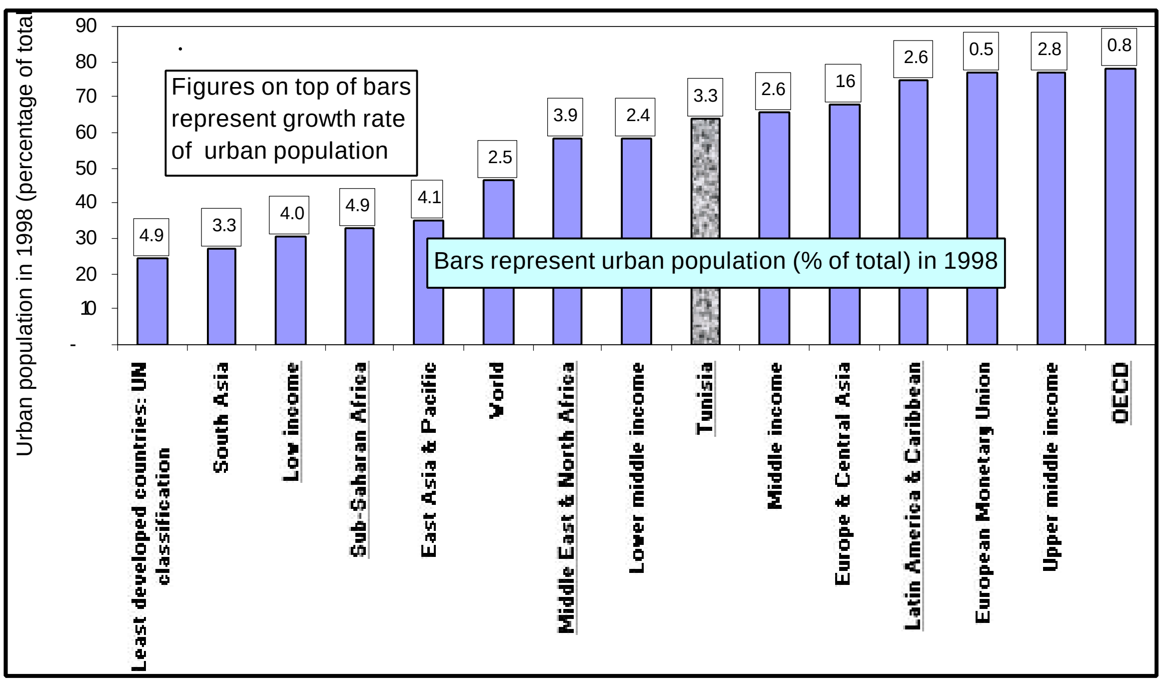


Figure 1.3: Tunisia and Comparators: Urbanization, 1998
Source: World Bank, *World Development Indicators*

4. This chapter reviews recent economic developments and the policies that contributed to them, and identifies sources of risks for future macroeconomic performance. It reaches the conclusions that Tunisia has achieved a significant economic progress, and that the development model followed so far—combining prudent macroeconomic management with direct government involvement in productive decisions through a complex system of incentives and *ad hoc* interventions—may well allow Tunisia to maintain, in the near term, economic performance similar to that achieved in the recent past. However, this model will be challenged by the consequences of deeper integration in the world market, and is unlikely to support the realization of Tunisia's ambition to catch up with OECD countries early in the 21st century.

5. Tunisia's economic adjustment efforts started in 1986 when a decline in oil export earnings and excessive public investment brought the country close to a balance of payments crisis. Since then, prudent macroeconomic management and cautious structural reforms have helped sustain positive per capita income growth, declining inflation, and a stable real exchange rate (Figure 1.4 and Table 1.2). Tunisia reduced the ratio of foreign debt to GDP, and consolidated its foreign reserve position until 1998, when the authorities had to draw on foreign exchange reserves to satisfy part of the demand for foreign currency, given the high cost of borrowing in the international financial markets that year. Foreign exchange reserves fell from 3.1 to 2.6 months of imports between 1997 and 1998. Subsequently, the authorities managed to improve the foreign reserve position to 2.7 months of imports.

B. Economic Performance

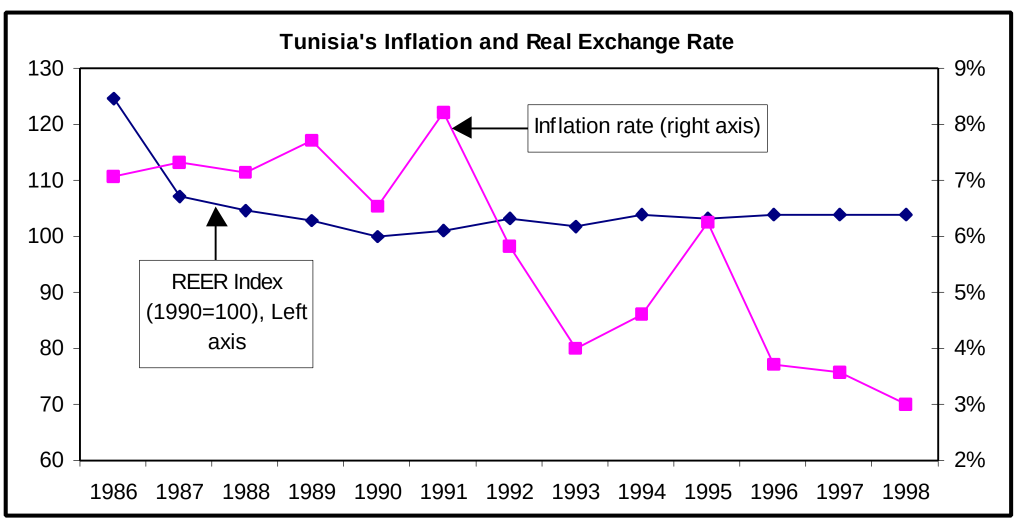


Figure 1.4: Tunisia: Inflation and Real Exchange Rate
Note: A decline of the real effective exchange rate index corresponds to a depreciation.
Source: World Bank, *World Development Indicators*, 1998.

Table 1.2: Tunisia: Key Macroeconomic Indicators

Indicators	1981-86	1987-90	1991-95	1996	1997	1998
GDP growth (%, real GDP at market price)	2.8	3.2	3.9	7.1	5.4	5.0
Inflation (%, CPI Index)	9.2	7.1	5.2	3.7	3.7	3.1
REER Index (1990=100)	144.0	103.7	102.6	104.1	103.9	103.9
Budget Deficit (% GDP)		4.8	3.7	3.9	3.9	2.9
Current Account Deficit (% GDP)	12.0	2.4	6.1	2.7	2.8	3.0
Foreign Direct Investment (% GDP)	4.8	1.4	2.6	1.3	1.7	3.1
Domestic Public Debt (% GDP)				26.9	27.9	15.7
Foreign Debt (% GDP)	75.5	76.8	63.0	60.1	54.2	48.8
Gross Foreign Reserves (months of imports)	1.67	2.29	1.93	2.78	2.81	2.60

Source: World Bank, *MENA LDB*, and *World Development Indicators*

Economic Growth, Factor Accumulation, and Productivity

6. Between 1961 and 1998, the Tunisian economy grew at an average rate of 5.1%, quite a reasonable rate by lower-middle-income country and regional standards. Factor accumulation and a significant total factor productivity growth have jointly driven Tunisia's growth performance. Capital and labor generated respectively one half and one quarter of economic growth during 1961-98, with total factor productivity growth amounting to the remaining quarter (Table 1.3).[3] Over 1973-86, productivity growth slowed to zero. Accumulation of capital and labor (especially in the public sector) resulting from large public investments in low-efficiency sectors was partly responsible for the productivity slowdown. Since 1986, productivity growth has recovered, while—owing to cuts in public investment during economic stabilization and adjustment programs—capital growth has slowed markedly, going from an average of 3.3% over 1973-86 to an average of 1.6% for 1986-96. Overall, Tunisia's total factor productivity growth compares well with other countries in the MENA region, and even with fast-growing countries such as Korea and Chile (Table 1.4).

[3] These findings are consistent with the results of a study by the Tunisian government covering the period 1961-96 which are as follows: contribution of capital accumulation to economic growth: 47%; contribution of labor: 29%; contribution of total factor productivity: 24%. Ministère du Développement Economique (1996).

Table 1.3: Tunisia: Factor contribution to GDP and total factor productivity growth

	GDP Growth (average)	Labor			Capital			Total Factor Productivity Growth	
		Growth	Contribution to GDP growth	% share in GDP growth	Growth	Contribution to GDP growth	% share in GDP growth	Contribution to GDP growth	% share in GDP growth
1960-73	5.8	1.6	0.8	14	5.8	2.9	49	2.2	37
1973-86	5.0	3.4	1.7	34	6.7	3.3	67	0.0	-1
1986-96	4.2	2.8	1.4	33	3.2	1.6	38	1.2	28
1996-98	5.2	2.8	1.4	27	3.9	2.0	37	1.9	36
1960-98	*5.1*	*2.6*	*1.3*	*25*	*5.4*	*2.7*	*52*	*1.1*	*22*

Source: Staff calculations based on data from World Bank, *World Development Indicators*, and Ministère du Développement Economique, Tunis

Table 1.4: Tunisia and Comparators: Total Factor Productivity

	Staff Estimate	Bosworth, Collins and Chen (1996)							
	Tunisia	Tunisia	Korea	Taiwan	Chile	Singapore	Ireland	Morocco	Jordan
1960-70	1.5	1.7	0.6	1.4	1.4	0.1	2.5	4.6	-1.1
1970-80	2.0	1.8	0.8	1.1	0.0	0.4	1.7	-0.2	3.0
1980-86	-1.2	-1.6	2.5	1.8	-1.9	-0.8	1.2	-0.3	-2.6
1986-92	1.8	1.4	1.9	2.5	3.8	4.0	3.4	-1.2	-4.3

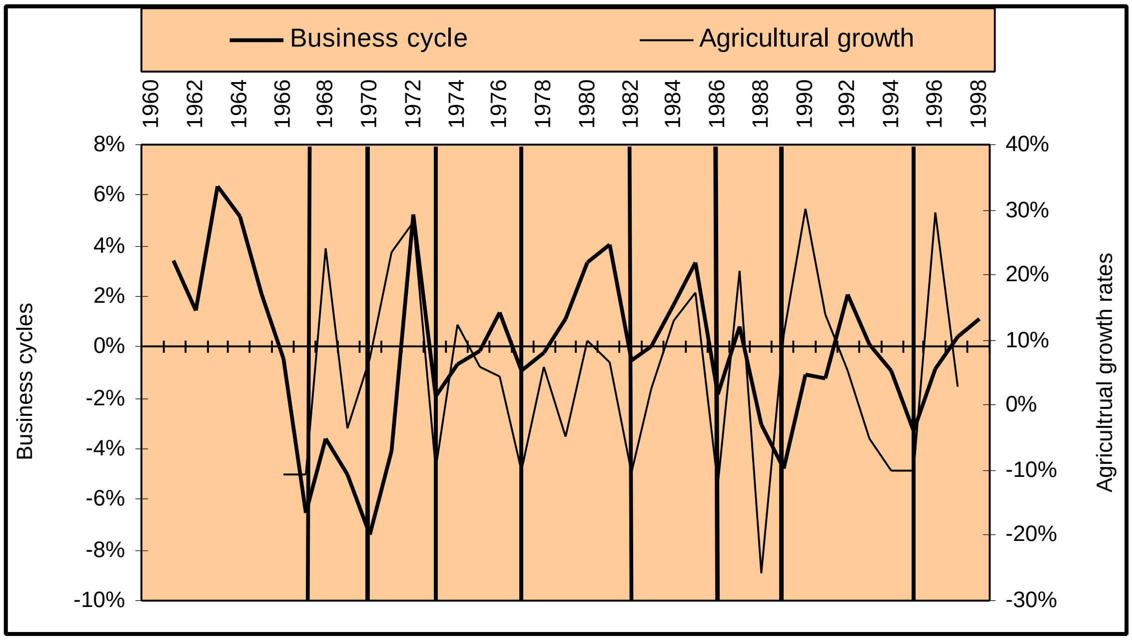
Source: Staff calculations, and Bosworth, Collins and Chen (1995).

Growth Performance and the Business Cycle

7. Tunisia's economic growth pattern has been marked by a strong cyclical pattern linked to agriculture. Between 1962 and 1998 there were eight full business cycles, with a stable average length of about four years and decreasing amplitudes (Figure 1.5).[4] Expansion phases lasted three years on average, and contractions one year. Agriculture appears to have been a determining factor in ending expansions: the troughs of the cycles generally corresponded to years of falling agricultural output (1967, 1969/70, 1973, 1977, 1982, 1986, 1988/89, 1995). The impact of fluctuations of agricultural production on overall GDP remains strong, even though the average share of the agricultural sector in GDP has been declining and the dependence of agriculture on rainfall has eased, in part owing to increased reliance on irrigation.

[4] See Kouamé (1999) for more details.

Figure 1.5: Tunisia: Agricultural Cycles and Aggregate Economic Activity



Source: Staff calculations

8. The impact of the agricultural sector on GDP has been asymmetric: it is stronger during years of agricultural contractions than during years of agricultural expansions. A 1 percentage point decrease in agriculture causes a 0.25 percent decline in overall GDP, while a 1 percentage point increase in agriculture generates an additional GDP growth of only 0.17 percent. This asymmetry originates from significant indirect effects produced by fluctuations of agricultural output on manufacturing and service activities linked to agriculture. On the supply side, a decrease in agricultural output tends to translate fully into decreases in agricultural related activities—transport, agro-processing—irrespective of capacity in these sectors. On the other hand, an increase in agricultural output can stimulate productive activity in related sectors only if spare capacity is available. On the demand side, the asymmetry results from liquidity constraints faced by households. A decrease in household incomes in the agricultural sector has a larger impact on their consumption than an increase in their incomes, because rural households do not have sufficient savings or borrowing opportunities to smooth out shocks and maintain their consumption levels.

9. The asymmetric effect of agriculture on GDP is also due to the fact that economic agents adjust their agriculture-related activities differently depending on whether they face drought or good rains. When they expect drought economic agents anticipate bad agricultural production and a weak level of activities in agriculture-related industries and services; they lower investment in these activities accordingly and, thus, cause a large effect on GDP growth. By contrast, when they expect good rains, economic agents are unable to anticipate with certainty the extent to which this will translate into higher future agricultural production and agriculture-related activities. As a result, they do not increase their investments in these activities sufficiently, thus generating only a limited effect on GDP.

10. Tunisia's business cycle has also shown a weak link with business cycles in major EU trading partners (Germany,

France, and Italy).[5] In the near future, the business cycle in Tunisia is likely to be influenced more strongly by business cycles in the EU because of the expected increase in trade and investment with the progressive implementation of the 1995 Association Agreement. Tourism may, however, provide a counter-cyclical link: because Tunisia is a low budget tourist destination, during periods of slow economic growth in Europe European tourists (90 percent of total tourist arrivals in Tunisia) tend to switch away from higher budget destinations and toward Tunisia.[6]

Sectoral Contributions to Growth

11. The decomposition of GDP growth by sectoral origin reveals four major trends. First, the services sector—with about 50% of GDP—has provided the largest contribution. Second, the contribution of manufacturing to growth has also been consistently larger than its share of GDP (as a result of higher than average growth in the sector)—although the share of manufacturing in Tunisia's GDP remains smaller than in fast-growing economies. Third, the growth contribution of the most export-oriented sectors is limited by their low value added, which is due to a weak integration with the rest of the economy (this is notably the case in the textile and electromechanical equipment industries). The fourth major trend is the large fluctuations in agriculture's contribution to growth discussed above.

12. The services sector—including public administration and other non-market services—has maintained a fairly stable share in total GDP, amounting to 51.5% in 1998 (Annex Table A1). Within the services sector, public administration is the largest component, with about 15% of GDP, followed by commerce, with 10%. Communications has been the most dynamic component—growing at an average 17% a year over 1995-98—although it still represents only a small share of GDP (3%).

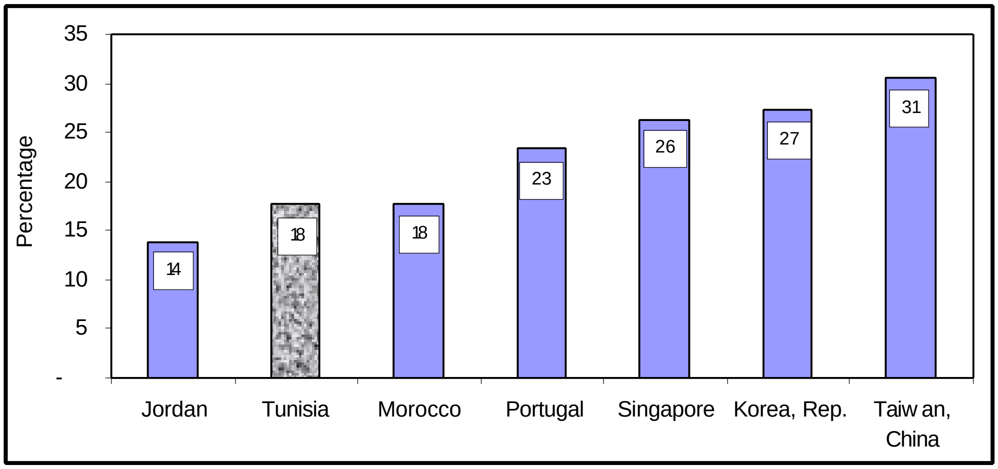
13. The manufacturing sector is the second largest, with about 20% of GDP, and has been fairly dynamic. Tunisia's manufacturing sector remains, however, fairly small, particularly when compared to countries that have achieved fast economic growth (Figure 1.6). This is cause for concern. Even though in the new era, services may play a more important role in small open economies such as Tunisia's, it is well documented that in the process of development the manufacturing sector usually increases its share in GDP, and often represents the main engine of growth.[7]

5 Baccouche, Bouazizet and Goaied (1997).

6 Jbili and Enders (1996).

7 Robinson and Syrquin (1986).

Figure 1.6: Tunisia and Comparators: Share of manufacturing, 1998



Source: World Bank, *World Development Indicators*

Demand Decomposition of Growth

14. Domestic demand made a large contribution to GDP growth, except during 1986-96 due to a slowdown in demand growth (from an average of 4.8% per year in 1973-86 to 2.7% per year in 1986-96) following the post-1986 economic stabilization program (Table 1.5). Domestic consumption has consistently been the largest component of domestic demand. The growth of foreign demand has been sustained at 5 to 6%, and its contribution to GDP growth has been maintained in the 2 to 3% range. With a stronger growth than domestic demand, foreign demand increasingly represents an important component of GDP (44% in 1996-98 from 27% in 1961-73).

Table 1.5: Tunisia: Contributions of Demand Components to GDP Growth

Period	Shares		Growth rates		Contribution to GDP growth		
	Domestic Demand	Foreign demand	Domestic Demand	Foreign demand	Domestic Demand	Foreign demand	GDP growth
1961-73	72.5%	27.5%	5.6%	7.6%	4.0%	2.1%	6.2%
1973-86	65.6%	34.4%	4.8%	5.7%	3.1%	2.0%	5.1%
1986-96	58.0%	42.0%	2.7%	6.7%	1.6%	2.8%	4.3%
1996-98	56.3%	43.7%	4.5%	6.3%	2.5%	2.8%	5.3%

Source: Staff calculations

15. Despite growing foreign demand pushing up exports, the net contribution of trade to GDP growth has been low because of growing imports—as expected in a growing developing country. In fact, it is expected that in the near term imports of manufactured goods—both equipment and finished goods—will rise rapidly as a result of the implementation of the Association Agreement with EU, and that the net contribution of trade may deteriorate temporarily.

Future Growth Prospects

16. *Short-term growth outlook.* During 2000-01, under the current policies of maintaining a stable macroeconomic

framework and implementing structural reforms at a slow pace, economic growth is likely to remain close in real terms to the level achieved in the 1990s, namely around 5.1% for overall GDP and 3.4% for GDP per capita. Tariff reductions on manufacturing imports included in the Association Agreement with the European Union will shift domestic expenditures for both investment and consumption toward imports. Also, the growth of external demand for domestically produced goods is unlikely to be higher than recent levels. Although European recovery is stimulating EU imports, some of Tunisia's competitors, particularly those emerging market economies and East European countries that devalued their currency in 1997-98, could easily enjoy a greater comparative advantage on the EU market, thus limiting the growth of demand for Tunisian products.

17. *Long-term growth.* In the long term, for per capita GDP growth to increase to the level required to catch up with lower income OECD countries, Tunisia has to deepen structural reforms aimed at rapidly improving the competitiveness of its economy while continuing to maintain a stable macroeconomic framework. An exercise undertaken in a background paper for this report found that Tunisia could catch up with Korea or Portugal by the end of the first quarter of the 21st century if it achieves real GDP growth of 6.6% on average during 2000-05, and 8.6% over 2005-25. This would correspond to per capita income growth rates of about 5.3% and 7.3% respectively (Figure 1.7).

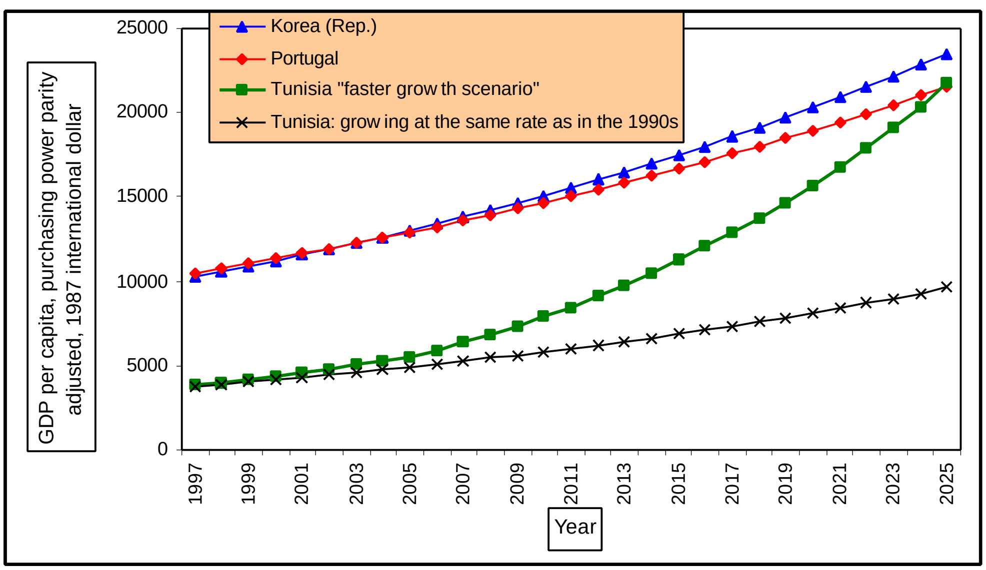


Figure 1.7: Tunisia: Convergence toward OECD countries
Source: Staff calculations

18. Convergence with OECD countries will require a substantial improvement in the factors that contribute to growth. The growth model on which the above projections are based suggests that moving to a faster growth track will imply at a minimum that Tunisia quickly curtails distortions in the policy environment and trade regime,[8] and minimizes distortions in the domestic competitive environment (Chapter 3).

[8] In particular the share of revenues derived from trade tax will need to be reduced dramatically from around 25% in the mid-1990s to close to 7% by 2005 and 3% by 2015 (in the EU all countries have a ratio of less than 1%),

19. The improvements in the policy environment will underpin and facilitate other improvements required to accelerate economic growth. For example, to realize the faster growth scenario, the investment to GDP ratio will need to increase to the 30-35% range (driven by private investment unlike in the 1970s and early 1980s). Education and human capital formation will need to improve and bring the average years of secondary education from the current estimate of 0.8, to 1.5 by 2005 and to 2.3 by 2015. Achievements in health will also need to be consolidated (Chapter 4). A stable macroeconomic framework will need to be maintained, with particular focus on reducing the budget deficit from current levels of 3 to 4% of GDP to about 1%.

20. Moving to a faster growth track would affect macroeconomic aggregates (Table 1.6). For instance, faster growth would bring higher fiscal revenues into government coffers and contribute to reducing the fiscal deficit as a share of GDP, compared to a situation in which Tunisia is assumed to grow at the average historical rates. The current account deficit would be larger in the faster growth than the historical growth scenario, as accelerating growth will require higher investment, which in turn will require an increase in imports (of equipment and intermediate goods). External debt does not decline as fast as in the "historical growth" scenario due to external borrowing needed to finance imports in support of faster growth.

---

and the highest ratio among OECD countries in the mid-1990s was 6 to 8% for Korea.

Table 1. 6 : Moving to a faster growth track: implications for macro-economic indicators

Indicators	Average 1995-99	Average 2000-05		Average 2006-08	
		"Historical growth" scenario[9]	Faster growth scenario	"Historical growth" scenario	Faster growth scenario
Growth of Real GDP	5.2	5.1	6.6	5.1	8.0
Budget Deficit (% of GDP)	-5.0	-2.8	-2.6	-2.0	-1.4
Gross Domestic Investment (% of GDP)	26.6	27.6	30.6	27.6	35.4
Gross Domestic Saving (% of GDP)	23.8	25.4	26.5	28.0	31.3
Growth of Merchandise Export (FOB) %	1.7	6.0	6.2	6.7	7.7
Growth of Merchandise Import (CIF) %	3.4	5.1	7.2	4.4	8.4
Current Account Balance (% of GDP)	-3.3	-2.2	-4.4	1.0	-4.7
Public Debt (% of GDP)	59.7	53.3	50.8	45.3	38.4
External Debt (% of GDP, public and private)	56.6	43.2	47.9	26.6	45.0
External Debt Service (% of exports)	16.6	13.7	14.5	7.9	12.5

Source: Staff calculations

21. Faster growth could be driven by capital accumulation and productivity gains. In the faster growth scenario, the contribution of capital to GDP growth is estimated to remain around 50% on average during 2000-25, as faster capital accumulation and faster economic growth would go hand in hand. The contribution of total factor productivity is estimated to increase to about 30% (compared to about 25% in the recent past), while the contribution of labor is estimated to decline to around 20% on average (from about 25%). The possibility of a high-growth scenario for Tunisia, thus, depends critically on strong total factor productivity growth. In particular, a strategy to sustain and increase total factor productivity growth should include improvements in the macroeconomic policy environment, as discussed above. Such a strategy should also encompass measures to increase the contribution of the public administration—which can improve its own productivity and also facilitate productivity growth in the private sector (Chapter 2). In turn, this

[9] This scenario corresponds to the situation where Tunisia is assumed to grow at historical growth rates on average

involves improving the environment for business development and cutting the costs of doing business, especially those costs of infrastructure and services that continue to be inefficiently provided in non-competitive and non-contested markets (Chapters 2 and 3).

International Trade

22. Since the mid-1980s Tunisia has successfully managed its transition from a resource-based to a manufactures-based export strategy. The most salient feature of this transition has been the shift from an export base dominated by oil and related products to one dominated by textile clothing and accessories (Figure 1.8). The heavy dependence of Tunisia's exports on oil and the attendant high exposure to commodity price fluctuations, as experienced in the mid-1980s, have thus markedly receded.

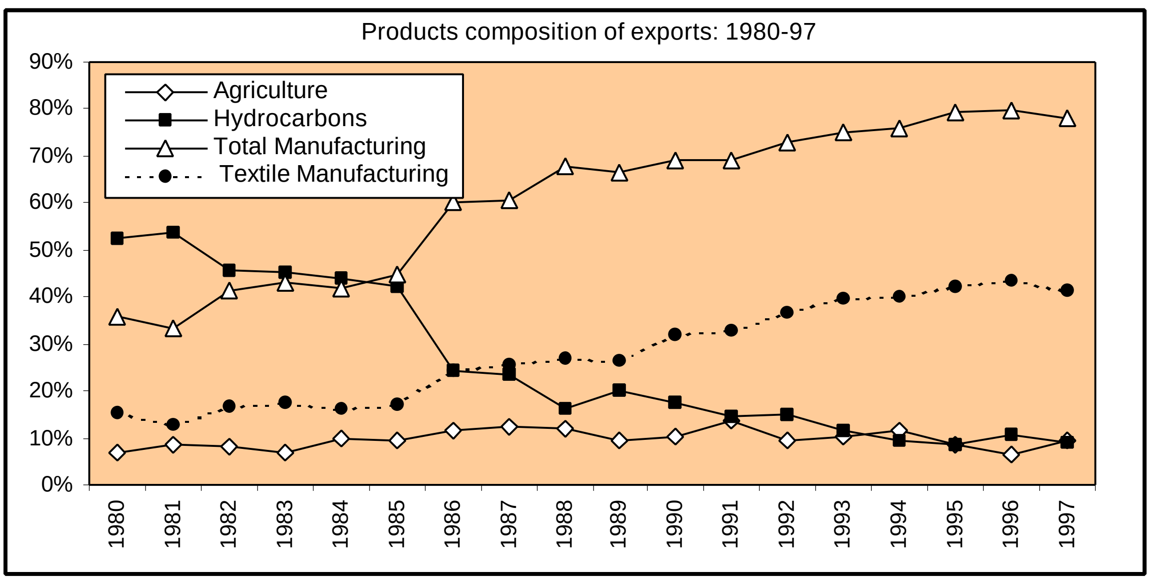


Figure 1.8: Tunisia: Sectoral Composition of Exports
Source: UN *Comtrade*

23. The current heavy concentration of exports on textile manufactures however encompasses new risks, resulting from the scheduled phasing-out of the Multi-Fiber Agreement (MFA) by 2005. Helped by the MFA, Tunisia expanded its share of the EU textile market from 1.5% in 1980 to 3.5% in 1997, and today the EU absorbs all but 4% of Tunisia's exports of textile garments. After the MFA is eliminated, Tunisia will face increased competition from countries with cheaper or more skilled labor, and which will no longer be limited by import quotas on textile products. This will make it difficult for Tunisia to maintain its market share in Europe or to penetrate other OECD markets.

24. Beyond the heavy concentration on textile manufactures that emerged from the transition away from oil and related exports, Tunisia has successfully diversified its exports toward new manufactured products (Table 1.7). Over 1980-97, at the two-digit SITC level, Tunisia gained comparative advantage in three manufacturing related product lines, while loosing comparative advantage in two agricultural product lines.

Table 1.7: Tunisia: Revealed Comparative Advantage[10] in Selected Products, 1980-97

SITC code and product name	1980	Average for 1980-89	Average for 1990-97	1997
Loss of comparative advantage				
29 Crude Animal, Vegetable Material	1.019	0.739	0.453	0.421
05 Vegetables And Fruit	1.494	1.769	1.197	0.966
Weakening of comparative advantage				
83 Travel Goods, Handbags	1.673	1.854	1.696	1.522
33 Petroleum And Products	3.786	3.978	2.072	1.998
27 Crude Fertilizer, Minerals	4.911	4.242	2.936	3.606
Strengthening of comparative advantage				
03 Fish And Preparations	1.830	2.645	2.050	1.986
61 Leather, Dressed Fur, Etc	2.193	2.682	4.850	6.196
52 Inorganic Chemicals	6.107	6.994	7.954	9.605
42 Fixed Vegetable Oil, Fat	6.278	8.529	13.509	11.717
84 Clothing and Accessories	7.549	7.788	11.739	12.836
56 Fertilizers, Manufactured	14.145	21.237	18.694	17.305
Gain of comparative advantage				
12 Tobacco And Manufactures	0.305	0.221	1.318	2.284
85 Footwear	0.617	0.511	1.964	2.965
57 Explosives, Pyrotechnic Products.	0.020	0.115	0.217	4.284
Areas of Potential Future Export Growth				
26 Textile Fibers and Waste	0.108	0.160	0.016	0.810
66 Nonmetal Mineral Manufacturing	0.057	0.606	1.020	0.872
77 Electric Machinery Etc	0.318	0.472	0.839	0.879
04 Cereals and Preparations	0.088	0.161	0.528	0.899
55 Perfume, Cleaning Etc Products	0.308	0.450	0.727	0.913
81 Plumbing, Heating, Lightning Equipment	0.048	0.137	0.499	0.930

Source: Staff calculations based on UN *Comtrade* data

[10] The Revealed Comparative Advantage of Tunisia in product i is obtained by computing {Tunisia's exports of product i divided by Tunisia's total exports} and dividing that quantity by {world export of product i divided by world total exports}.

25. Tunisia also managed to maintain, or even increase, its comparative advantage in key manufactured goods where it already had such an advantage in 1980. These include textile clothing and accessories, leather goods, and manufactured fertilizers. Tunisia is on the track to developing comparative advantage in a few other products. In particular, exports of electrical machinery boomed (their share in exports grew from just 1.2% in 1980 to 7.6% in 1997), and are poised to grow further in the near future in view of good investment intentions in the sector shown in a recent investors survey published by the Central Bank of Tunisia.[11] Electrical and mechanical machinery clearly constitutes a potential area for export expansion, particularly to the EU where Tunisia has already developed a comparative advantage.

26. Despite their high and growing contributions to exports, textiles and mechanical/electrical manufacturing have made relatively modest contributions to GDP growth. Production in these two subsectors is generally undertaken under offshore arrangements, which allow for duty-free access to imported inputs and benefit from an array of investment incentives. As a result, value added generation in these subsectors has remained very limited, as imported inputs undergo little transformation before being re-exported.

27. Tunisia's service sector has developed a strong capacity to export over the years.[12] Its comparative advantage in commercial services averaged 1.7 during 1995-97; and services represent nearly one third of exports of goods and services. Tourism has greatly contributed to the surplus on the service account in recent years, strengthening linkages with Europe—the source of more than 90% of Tunisia's tourists. In addition to tourism, new services are quickly emerging in Tunisia and can be expected to rise, in particular in international medical care, consulting services, data processing, and software design and translation.

28. The future of Tunisia's exports, thus, lies not only in further diversification toward new manufactured goods, such as electric machinery or footwear, but also in nurturing exports in new services related to information technology where the potential for booming exports is high. Tunisia's traditional exports of goods (textile garments) and services (tourism) mostly rely on unskilled labor. As diversification toward manufactured goods such as electrical and mechanical equipment, manufactured fertilizers, and information technology-related services takes root, the capacity of the export sector to absorb a larger share of Tunisia's growing pool of skilled labor will grow.

29. Tunisia trades increasingly with the EU (Table 1.8). The EU's share in Tunisia's exports grew from around 70% in the 1980s to 78% in 1997.[13] The EU now absorbs more than 80% of virtually every significant product exported by Tunisia. The EU's share in Tunisia's imports grew from 67% in the early 1980s to 71% in 1997. Although Tunisia's share of the EU market is still a very small 0.3% it is worth noting that this share has increased significantly since the late 1980s, particularly for non-oil and gas (Figure 1.9).

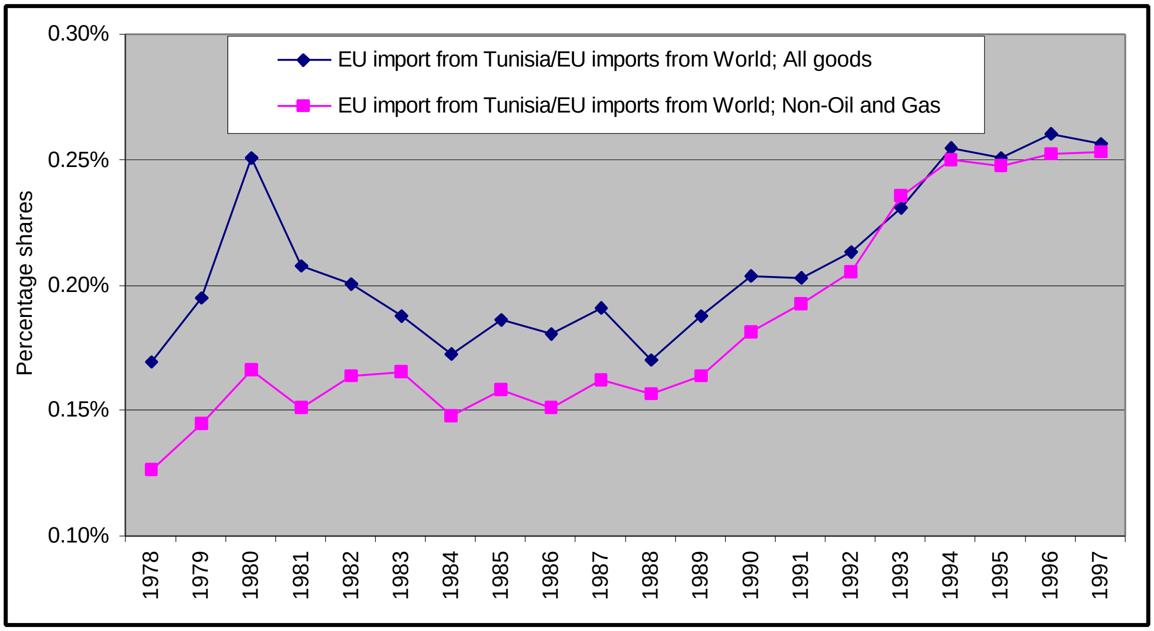
---

11 Banque Centrale de Tunisie (1998).

12 Haddad (1999).

13 The share of the EU in Tunisia's export of product i is computed as {export of product i from Tunisia to EU} divided by {export of product i from Tunisia to the world}.

Figure 1.9: Trend in Tunisia's Share of EU market: 1978-97



Source: UNComtrade

Table 1.8: Tunisia and EU: Trade Shares and Trade Intensity Indices, 1980-97

		1980	Average 1980-89	Average 1990-97	1997
Trade Shares					
Share of EU in Tunisia's Exports		0.72	0.69	0.78	0.78
Share of EU in Tunisia's Imports		0.67	0.67	0.71	0.71
Trade Intensity Indices					
Intensity of Tunisia's Exports to EU	All products	1.46	1.57	1.95	2.06
	Manufactured goods	1.77	1.82	1.99	2.15
Intensity of Tunisia's Imports from EU	All products	1.61	1.72	1.84	1.88
	Manufactured goods	1.44	1.69	1.92	1.96

Source: Staff calculations based on UN *Comtrade* data

30. Looking at trade shares is insufficient, however, to evaluate the intensification of trade with the EU, for the EU's share of Tunisia's exports or imports could have grown simply because the EU is expanding its trade faster than the rest of the world. However, this is not the case. Looking at trade intensity indices reveals not only that, in 1980, Tunisia traded more intensively with the EU than the rest of the world did, but also that Tunisia's trade with the EU has since intensified further.[14] Tunisia's trade intensity indices with the EU

[14] The intensity index of export of product i from Tunisia to EU is obtained by dividing the share of the EU in Tunisia export of product i by the following quantity: {export of product i from the world to EU} divided by {total world export of product i }. An intensity index higher than one suggests that the share of EU in Tunisian exports of product i is larger than the share of world exports of product i received by EU.

have increased from around 1.5 to about 2 both for exports and imports (Table 1.8 above). This reveals strong integration with the EU market, as it compares with intra-EU trade intensity indices between 1.5 and 2.5.[15]

31. Moreover, it appears that Tunisia trades even more intensively with the EU in manufactured goods than in the aggregate, and more so today than in the 1980s. Both economic theory and empirical observation suggest that such intensive trade in manufactured goods with the EU—a large and more advanced economic area—will lead to higher economic growth in Tunisia.[16] There are risks however. With more intensive trade with the EU, Tunisia's export performance—and economic growth performance—will be more vulnerable to economic slowdowns in Europe. An effort to expand exports to other regions such as Asia, North America, and other developing countries—while maintaining market shares in Europe—may, thus, be called for. The fact that Tunisia recently signed bilateral free trade agreements with Egypt, Morocco and Jordan – and plans to sign more bilateral agreements with Arab partners – constitutes a great opportunity to expand trade with other countries.

32. Beside the recently signed free trade agreements, the Tunisian authorities have taken additional measures to promote exports. These include research on strategic positioning on export markets, customs reform geared at simplifying procedures for economic agents, creation of institutions to monitor supply, prices, and international trade, and creation of an export promotion council (*Conseil supérieur de l'exportation*).[17]

C. <u>Macroeconomic Management</u>

33. Behind Tunisia's strong economic performance lies a good record of macroeconomic management. Starting in 1986, when a sharp fall in oil prices nearly precipitated a balance of payments crisis, the authorities have followed consistent stabilization policies and adopted gradual adjustment measures. The fiscal deficit has been reduced through a combination of expenditure restraint and revenue measures. Monetary aggregates have been better controlled. The exchange rate has been managed flexibly, while maintaining overall stability in real terms. As a result, inflation has been significantly reduced and now stands at around 3 percent. The external position (current account balance, foreign currency reserves, and external debt) has also improved considerably, and has given international financial markets confidence in the Tunisian economy.

Fiscal and Monetary Policies

34. Tunisia's fiscal policy during the 1990s was characterized by a moderate and stable tax burden, averaging about 20% of GDP (Table 1.9). Maintenance of the tax burden has been achieved by offsetting the loss of trade tax revenues—declining since 1996 under the Association Agreement with the EU—with rising VAT revenues, resulting both from broader coverage and higher rates. However, total revenues as a share of GDP have declined as a result of falling transfers from state enterprises, especially in the petroleum sector.

35. Similarly, current expenditures (including interest payments on public debt) have been moderate, and declined gradually from 22.5% to 20.6% of GDP between 1990 and 1998. This decline resulted from correspondingly modest reductions in subsidies and the civil service wage bill as a percentage of GDP, while the interest payments component has remained stationary around 3.6% of GDP as the impact of higher public debt has been moderated by falling interest rates. Capital expenditures other than repayment of principal of public debt have gradually

---

15 Freund, and McLaren (1999).

16 Vamvakidis (1998); and Pack and Saggi (1998).

17 For more detailed information, see World Bank (2000a).

declined, from about 10% to below 8% of GDP. As a result, the overall fiscal deficit fell from 5.9% in 1991 to 2.9% in 1998. The primary balance has also improved, going from a deficit of 2.4% of GDP to a surplus of 0.5% during the same period.

Table 1.9: Tunisia: Government Budget, 1991-98 (% of GDP at Current Prices)

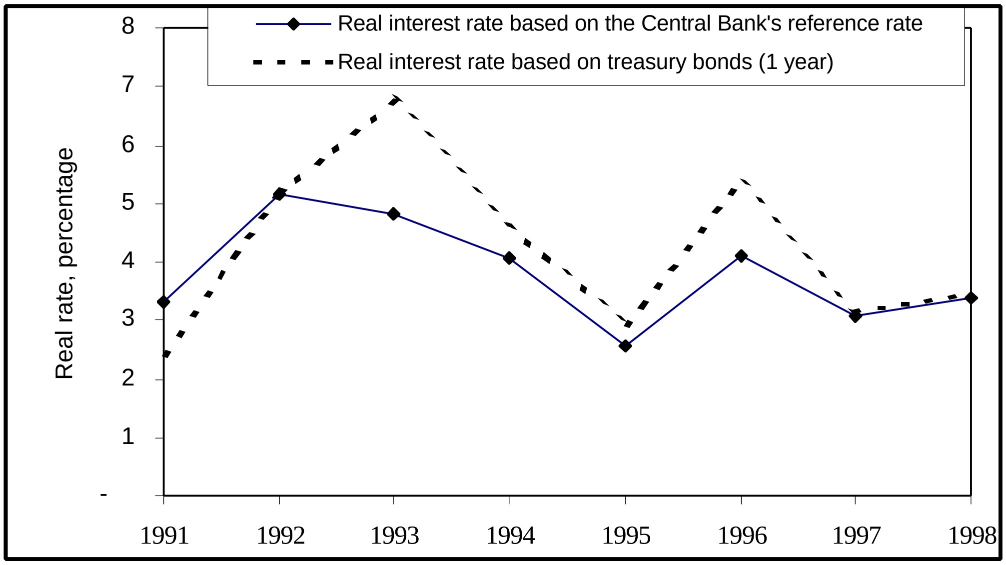
	1991	1992	1993	1994	1995	1996	1997	1998
Total Resources	38.4	34.8	37.4	38.3	37.6	39.7	37.8	34.7
Current Revenues	26.4	26.6	27.6	27.4	26.3	25.2	24.5	24.7
o/w Fiscal Revenues	20.5	20.5	21.0	20.8	20.5	19.9	20.2	20.9
Borrowings	12.0	8.2	9.8	10.9	11.3	14.5	13.3	10.0
Total Expenditures	38.2	35.1	37.8	39.9	38.8	39.2	38.5	37.2
Current Expenditures	22.5	21.6	22.1	22.0	22.17	21.1	21.1	20.6
(incl. Interest payments)								
o/w Interest Payments	3.45	3.31	3.62	3.53	3.78	3.98	3.76	3.41
Other Current Expenditures								
Capital Expenditures	15.7	13.5	15.7	17.9	16.7	18.1	17.4	16.6
o/w Reimbursement of the Principal of Debt	6.0	5.2	7.0	9.4	8.2	9.9	9.8	9.3
Other Capital Expenditures	9.7	8.2	8.8	8.6	8.6	8.2	7.6	7.3
Budget Balance	-5.87	-3.06	-3.21	-2.95	-4.04	-3.93	-3.85	-2.88
o/w Primary Balance	-2.42	0.25	0.41	0.57	-0.26	0.06	-0.09	0.53

Source: Staff calculations based on data obtained from the Ministry of Finance, March 1999

36. The monetary stance has also been prudent and consistent with fiscal policy in recent years. In 1998 growth in money and quasi-money (M2) was 7% (end of period), which represents a significant moderation compared to growth rates of 16.5 and 13.6%, respectively, for 1997 and 1996. Inflation was reduced from 6 to 3% between 1991 and 1998, while the real effective exchange rate appreciated moderately, by 5% cumulatively (Figure 1.4 above).[18] During the same period, real interest rates declined, as the central bank lowered the interest rate used to manage liquidity—which also serves as reference rate for commercial banks—from 11.5% in 1991 to 6.9% in 1998 (Figure 1.10), and to 5.9% in 1999.

[18] This slight appreciation is based on IMF data. Data from the Tunisian Central Bank, however, do not suggest an appreciation of the real exchange rate.

Figure 1.10: Tunisia: Evolution of Real Interest Rates, 1991-98



Source: *Banque Centrale de Tunise*, 1999

Fiscal Sustainability

37. Comparing Tunisia's public finance indicators with those of similar MENA countries shows a prudent fiscal policy, indicated by low primary and overall fiscal imbalances and moderate government debt.[19] It is, thus, not surprising that, if current levels of GDP growth and interest rates are assumed for the medium term, existing fiscal policies are found to be sustainable.

38. Fiscal policies are considered sustainable if they do not lead to a buildup of public debt in excess of the government's capacity to service debt over the medium and long terms.[20] The key variable is the level of public debt in relation to GDP. An ever-increasing debt-to-GDP ratio eventually makes it impossible to finance the budget deficit, by leading to a confidence crisis or inducing destabilizing money creation. However, it should be noted that in the presence of a high—even if not increasing—debt-to-GDP ratio, external events such as an increase in the cost of borrowing or adverse changes in the perception of country risk, can lead to unsustainability by increasing the cost of servicing debt.

39. In Tunisia maintaining the 1998 situation—a modest primary surplus of 0.5% of GDP, accompanied by yearly growth of 5%, an effective real interest rate of 3.3% on outstanding debt, and a stable real exchange rate—would result in a gradual decline in the government's outstanding debt from 54% of GDP in 1998 to 42% in 2008 (Annex Table 3).[21] But, this outcome is critically dependent on the level of real interest rates and GDP growth: *ceteris paribus* an increase in domestic interest rates by 1 percentage point would lead to an increase of one third of a percentage point in the effective real interest rate on government total debt. In turn, this would result in an

[19] Public finance indicators for Tunisia and selected comparators are presented in Annex Table 2.

[20] At the extreme, government debt becomes unsustainable either if it is projected to rise indefinitely as a share of GDP or if the cost of debt servicing absorbs an excessive amount of resources. See IMF (1995).

[21] The analysis presented here is based on the model described in World Bank (1997).

increase in the debt-to-GDP ratio of 2 percentage points by 2008, as compared with the baseline. Similarly, a decrease in GDP growth by 1 percentage point a year would increase the debt-to-GDP ratio by 5 percentage points – again as compared with the baseline.[22]

40. Thus, unless the very favorable conditions described earlier are maintained in the medium term there are risks to fiscal sustainability. Two sources of potential risk are particularly significant in the Tunisian context: first, a negative shock to external balances and an associated real devaluation; and, second, a negative shock to fiscal balances and an associated increase in the real domestic interest rate.

41. A negative shock to external balances could arise from the combination of the following factors: implementation of the final round of tariff reductions under the EU Association Agreement (leading to higher imports), elimination of the MFA (leading to lower exports), and a slowdown in the world economy (resulting in lower demand for Tunisian exports). Such a shock is likely to cause both a decline in GDP growth and a real devaluation. The combined effect of these two trends could radically change the outlook for fiscal sustainability.

42. A negative shock to fiscal balances could also arise from the emergence of contingent liabilities requiring significant budgetary expenditures. This scenario is not likely in the short term, but, in the light of recent experience, it is not implausible over the medium term. In 1996 contingent liabilities generated by the government's consumer subsidy policy led to the assumption of arrears amounting to TD969 million (5.2% of GDP); in 1998 the accumulation of significant non-performing loans in the banking sector led to the assumption of those incurred by state enterprises, about TD800 million (3.5% of GDP). In the latter case, the fiscal implications were significantly smaller than the stock of debt assumed by the budget—because of burden sharing with the banking system in the form of rescheduling at zero interest rates—nonetheless, the magnitudes involved are alarming. In the event of a large shock to budget balances—as could arise from the emergence of large contingent liabilities, fiscal sustainability could again be undermined by the impact on the stock of public debt itself, and the likely attendant increase in domestic real interest rates.

Fiscal Sustainability and Contingent Liabilities

43. Contingent liabilities reflect existing commitments, whose fiscal consequences are dependent on future events that may or may not materialize, and that are beyond the control of policy makers. The importance of contingent liabilities to fiscal sustainability stems from their potentially large effect on fiscal balances. Management of contingent liabilities is complicated by the fact that they do not only originate from legal obligations of the government—– e.g. from public ownership of enterprises and banks, or government guarantees—but also from the moral obligation to assume liabilities stemming from public policy mandates, such as social security and mandatory insurance. The fiduciary nature of financial activities may also generate a moral obligation to assume liabilities, for example to prevent banking failures that could destabilize the financial system or impoverish small depositors. Emerging market economies face particularly large risks because of opaque ownership structures, weak financial sectors, limited information disclosure, and weak regulatory and enforcement systems. For these reasons, contingent liabilities should be taken into account not only in the general formulation of policies that reduce their size and the likelihood of their occurrence, but also in fiscal decision making, for example, through budgeting and provisioning.

[22] In the accelerated growth scenario described before, the debt-to-GDP ratio would be 35% in 2008.

44. In Tunisia, the two recent episodes discussed above suggest that contingent liabilities may represent significant potential risks to fiscal sustainability and, thus, macroeconomic stability. Increasing integration into the world economy and competition from the EU further heighten these risks. In this context, five potential sources of contingent liabilities can be identified in Tunisia: the social security system; insurance funds; public enterprises; government guarantees, and the banking system.[23]

45. It should be noted that regulatory weaknesses that could lead to the occurrence of contingent liabilities have been greatly ameliorated in all five areas identified above. However, there still is no unified responsibility for monitoring and managing contingent liabilities that may arise in the future. It should also be noted that the exposure of the financial system to public enterprises has been at the center of recent episodes, and that this is probably the area where the most progress in reducing the underlying causes has been made.

46. *Insurance*. While no contingent liabilities stemming from the insurance sector are expected in the short term—owing to a series of gradual reforms that improved its financial performance during the 1990s—there remain risks for the medium and long term. These risks are largely associated with the predominance in the sector of compulsory insurance lines (such as automobile insurance) where the public sector exercises significant control on premiums. An additional but smaller source of risk is constituted by the poor financial performance of the remaining two state-owned insurance companies.

47. *Banking system*. The risks of contingent liabilities in the banking sector originate from three different sources. First, there remains extensive state ownership or control of banks: four of the five largest commercial banks are public, and so are the two largest development banks (the other development banks are joint ventures between the Tunisian government and Arab countries). Despite significant efforts to improve loan provisioning and capital adequacy since 1992, these banks still suffer from poor asset quality, and many have weak capital bases. Second, and again despite progress in regulation and supervision, non-performing loans in the banking system reached an alarming level in recent years – some 8.4% of GDP as of end-1999. This problem is being addressed by the assumption of non-performing loans of public enterprises by the budget, as discussed above, while market-based recovery mechanisms have been instituted for non-performing loans of private enterprises. In this regard, the government has granted authorization to a number of private debt collection agencies, and one such agency has collected 90 million dinars worth of debt in the first quarter of 2000. Nonetheless, pressure for the budget to assume at least in part the non-performing loans of private enterprises may arise if these recovery mechanisms fail. Third, the banking system is financing—with the government's seal of approval—a significant portion of the *mise à niveau* program (Chapter 3). If some of the firms in the program were to find it difficult to face external competitors and meet their financial obligations, this may again result in pressure for the government to bail out banks overexposed to this program.

48. *Public enterprises*. To date, public enterprises have caused the two largest episodes of assumption of liabilities on the part of the budget, as discussed above. The gradual privatization of public enterprises in the competitive sectors and the introduction of safeguards limiting the borrowing of non self-financing public enterprises have over time limited the exposure of the banking sector to public enterprises. Specific high-risk cases may exist—public enterprises with large arrears—but they cannot be identified because of unavailable data.

[23] See Mohammed (1999) for more details.

49. *Government guarantees*. In Tunisia, the government grants guarantees mostly to facilitate borrowing by entities undertaking projects of a public nature. The overall envelope for providing financial guarantees is approved in the budget, and charges are imposed on entities using government guarantees.[24] In recent years the government has begun to provide guarantees for purposes other than to facilitate borrowing, such as concession contracts and privatization of enterprises. This type of guarantee—*garantie de marché*—is granted on an ad hoc basis by the ministry responsible for the oversight of the industry in question, and no monitoring or provision is undertaken at the level of the budget.

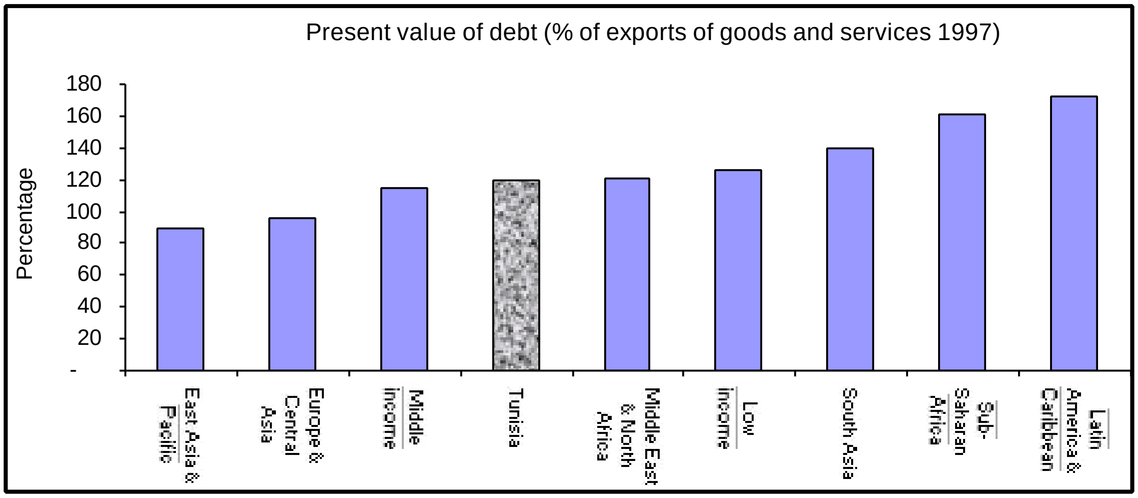
50. *Social Security*. The existing system combining old age and survivor benefits, basic health coverage, and family allowances has two large schemes (one for public sector workers and one for private sector workers). The system is characterized by broad coverage (all public sector workers and some 75% of private sector workers), relatively high mandatory contribution rates (17.2% for public sector wages, 23.75% for private sector wages, and 11% for self-employed earnings), and generous benefits relative to contributions. The old age component is a partially funded defined benefit system based on scaled premiums, which is gradually reaching maturity as rising dependency ratios lag declining fertility. Because of different expected dynamics in public and private employment and different contribution rates, the performance of the public sector scheme is weaker and is expected to deteriorate more rapidly than performance of the private sector scheme. Again, no crisis is imminent but the difficulties inherent in putting social security on a sustainable basis—especially through alliances between pensions and workers that would enable them to borrow from their children and grandchildren—are serious and should be addressed sooner rather than later.

External Sustainability

51. By various indicators, Tunisia is a moderately indebted country. Total external debt was estimated at $11 billion as of end-1999, equivalent to 51% of GDP and down from about 60% of GDP in the early 1990s. In present value terms, Tunisia's external debt outstanding at end-1997 was equivalent to slightly over 100% of exports of goods and services, which is comparable to the average for middle-income countries (Figure 1.11). The debt service ratio—payment of principal and interest as a share of exports of goods and services—is about 18%.

[24] In the 1999 budget, the total envelope authorized for financial guarantees was TD950 million. The charges for financial guarantees to financial institutions was 0.5%, and to non-financial institutions was 1.5%.

Figure 1.11: Tunisia and Comparators: Debt-to-Export Ratios, 1997

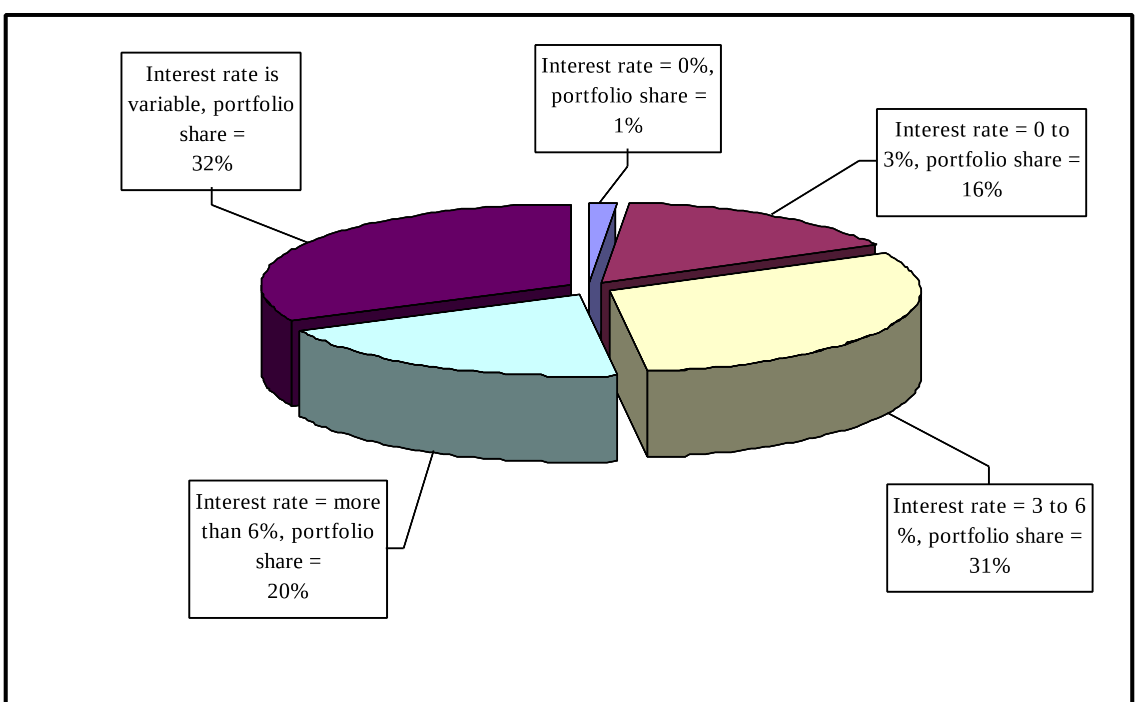


Source: World Bank, *World Development Indicators*

52. Tunisia's debt profile by rates and maturities is also positive. As of end-1997, two thirds of external debt was at fixed rates (Figure 1.12). The average maturity of medium- and long-term debt (essentially incurred by the public sector) was 13 years, with only 10% having a maturity of less than 5 years. Short-term debt, with a maturity of less than a year, is essentially incurred by the private sector. It is limited by controls on short-term capital inflows (for example, foreigners need authorization to purchase short-term assets). As a result, short-term external debt was estimated at $1.1 billion as of end-1999, corresponding to 1.3 months of imports—compared to foreign reserves of 2.7 months of imports.

Figure 1.12: Tunisia: Interest rate composition of external debt, 1997

Source: World Bank, *World Development Indicators*, 1998



53. The currency composition of external debt is less favorable. The share of dollar-denominated debt in total debt rose to 44% in 1997 (up from 34% in 1996) owing to the issuance of $400 million in Yankee bonds. The share of dollar denominated debt is high in consideration of the fact that nearly 80% of exports are denominated in European currencies. The issuance in July 1999 of Euro-denominated sovereign bonds (for a total of €225 million, with a 280 basis points spread over comparable German bonds) is a positive development toward rearranging Tunisia's debt composition. It should be noted that, as a result of issuing sovereign bonds in recent years, the debt service is expected to peak in 2000—owing to a payment of $(?)465 million on account of Samurai bonds issued in the mid-1990s, and $(?)88 million on account of syndicated loans.

54. To ensure that external balances remain sustainable in the future, Tunisia is pursuing a three-pronged strategy. It is encouraging export development (including through the *mise à niveau* program) and foreign direct investment (including through privatization). It is also trying to deepen the domestic financial markets to ensure adequate budgetary financing from domestic sources. Third, Tunisia is strategically managing its resort to international capital markets to consolidate its past record as a good credit risk able to borrow at the low end of emerging market spreads.[25]

55. In the medium term, the main risk to Tunisia's external outlook would come from a failure of this three-pronged strategy. Tunisia's financing requirements averaged about $1.6 billion a year during the 1990s, and are expected to continue to remain significant in the near future. A serious deterioration of external balances—as could be brought about by a concurrent surge in imports from the EU, a drop in exports because of weak international demand and domestic competitiveness, or a drop in foreign direct investment—would lead to significantly larger borrowing requirements. A large increase in borrowing requirements accompanied by worsening borrowing conditions for emerging economies, could then lead not only to an increase in external indebtedness, but also to a deterioration of the external debt profile by rates and terms structure.

[25] In meeting its external financing needs in 1998, Tunisia was able to avoid borrowing on private international capital markets when borrowing terms were not favorable. This was made possible by sizeable privatization receipts in foreign currencies, and by reducing foreign currency reserves.

Chapter 2. Strengthening the Public Sector's Contribution to Growth

A. Introduction and summary diagnosis

56. This chapter deals with public sector organizations and the governance systems that can improve their performance in a sustainable manner. The chapter focuses on two key public sector contributions to economic growth. First, the quality of services that the public sector provides to households and investors is a key element in the overall competitiveness of the economy, as it affects the capabilities of the labor force and the cost of doing business; it thus affects the attractiveness of Tunisia to foreign investors. Second, real national income is directly affected by the costs—in terms of time and effort —borne by citizens and businesses to gain access to public services or to comply with public sector regulations. A third important contribution of public institutions to economic performance—establishing and enforcing a regulatory framework to support the private sector—will be discussed in Chapter 3.

57. Tunisia has achieved substantial progress in modernizing its public sector and in strengthening its contribution to economic performance. The most important achievements include clarifying the role of the state by redirecting public enterprises away from competitive sectors, and a start at separating public mandates and commercial activities within their operations. It has also improved access to public services, through three structures: the *Médiateur administratif* (Ombudsman), the *Bureau des relations avec le citoyen* (Office of Relations with Citizens), and the *Equipe du citoyen superviseur* (Citizens acting as Supervisors). As well a number of administrative reforms were carried out, ranging from the modernization of the *Cour des Comptes* (Auditor General) to the streamlining of civil service compensation, and the introduction of elements of multi-year budgeting by integrating the capital and recurrent budgets.

58. The prevailing system of governance is based on centralized controls of, and budgeting for, inputs. These controls are inadequate in rapidly evolving and increasingly complex circumstances. International experience on the contribution of public organizations to economic performance points to two main directions of reform. First, the focus of reform needs to be on governance—the rules and incentives that shape the organization and the behavior of public organizations—because it is central to organizations' ability to manage and innovate to achieve higher productivity. Second, the governance system should be focused on the actual achievement of public objectives—with robust accountability systems and clear incentives for

achievements—to increase the productivity of public organizations in a sustainable and dynamic manner. Enriched by numerous innovations during the last two decades, these experiences have undergone sufficient testing in different national contexts to ensure that they would be beneficial to Tunisia.

59. Moving in these two directions requires that Tunisia effect profound changes in the governance of core public organizations and expand the scope of ongoing public enterprise reform. The leap forward that is needed for Tunisia to establish a governance system supportive of continuous productivity growth is indeed well within its reach. This view is supported by recent success in modernizing the Tunisian public sector, and reinforced by the tradition of professionalism that has long distinguished Tunisia's public organizations.

60. The transformation of the governance systems of public organizations will be complex and will require an extended period of implementation. An important aspect of international experience in this regard—budgeting—is summarized in Box 2.1.

61. To begin transforming the governance system of public organizations in the context of Tunisia, the following measures could and should be introduced rapidly:

- *For public enterprises*, ongoing reforms should be completed and the incentive framework should be strengthened to further clarify accountability, scope of managerial autonomy, treatment of profits, and public policy mandates. In addition, options will need to be explored to improve the cost/quality mix of the services produced by the public sector and offer private enterprises a greater choice of providers, as is being done in the EU and acceding countries, by establishing a clear framework for concessions and other forms of alliance between public and private enterprises.

- *For the core public administration*, functional classification of expenditures and results-based budgetary framing and reporting should be introduced as the first step in support of the devolution of adequate autonomy for achievement of public policy objectives to administrators as close as possible to the point of production and delivery of public services. This first step should be followed by the launch of a productivity drive, which could make a strong contribution to mobilizing existing energy for modernization and innovation.

Box 2.1: International Experience on the Evolution of Budgeting

The milestones noted below illustrate the experience of Singapore, with selected references to the experience of other countries.

- *Pre-1978: Line Item Budgeting.* The emphasis was on input controls. There was no explicit mechanism within the system to link resource allocations to goals and objectives. Decisions on resource allocation within ministries were centralized, as budget allocation was defined in detailed lists of inputs allocated to each administrative unit.
- *1978-89: Program Budgeting*. This approach emphasized, for each ministry and group of agencies with overlapping objectives (e.g. education and training), actions, objectives (e.g. number of persons helped in finding a job, number of students at each level, etc.), and choices and priorities of each organization, defined in terms of service delivery outputs instead of expenditures. In this vein, separate accounting and budgeting was established for public policy mandates given to state enterprises. The program approach provided more flexibility to move resources around within programs. Within a multiyear expenditure framework, the approach was used to deal with effective priorities; reporting on past years and forecasting for future periods facilitated monitoring beyond exclusively focusing on financial controls.
- *1989-96: Block Vote Budgeting*. Block vote budgeting provided greater flexibility in resource allocation. Under block voting, line agencies were given larger blocks of appropriations within which they had the flexibility to reallocate resources without seeking central approval. In Singapore, there remained constraints on the ability to shift funds across years, while most OECD countries relaxed them at this stage. As a result, in many OECD countries, from Australia to Finland to Canada, block voting was accompanied by multiyear agreements (some called them contracts, some memoranda) between ministries of finance and other ministries on core funding and corresponding ministerial commitments to outputs and some outcomes (e.g. number of miles of roads maintained to given standards). In addition, many OECD countries gave wide latitude to ministerial managers on the allocation of funds between office space, consultants, computers, etc.; fungibility between salaries and other expenditures was more constrained, and gave rise to a variety of different practices. Generally, ministries such as public works, transport, health and higher education were the first to use this approach.
- *1996-: Budgeting for Results*. This is the most recent development in the evolution of Singapore's budgeting system. The emphasis is now on outputs and deliverables, and the management philosophy is based on devolving more authority to public sector managers to improve performance and at the same time increase accountability. Resource agreements specify the outputs and performance targets that agencies—units that are much smaller than ministries—will deliver with their allocated resources, and hold top managers accountable for results. The resource agreement is used as an accountability tool for performance evaluation and resource allocation and its details are agreed between the individual agency, the parent ministry, the minister, and the budget division.

Source: Adapted from World Bank (1998a).

B. Recent Reforms of Public Organizations in the Economic Domain

62. The Tunisian public sector has made remarkable progress in the recent past, and has greatly increased its contribution to overall economic performance. At the same time, the size of the public administration has remained approximately stable, while the size of the public enterprise sector has declined (see Box 2.2). This section reviews the most important achievements in reforming the Tunisian public sector, especially those that can be used as a foundation for future reform, focusing on public enterprises and the core public administration.

Box 2.2: Tunisia – Size of the Public Sector

Core public administration—including central and local government, but excluding public financial and non-financial enterprises—accounted for approximately 15% of GDP in 1997-98. This share has remained stable in the last decade. Employment in the core public administration has been increasing in absolute numbers, but its share in total employment, about 16% according to the 1994 census, has remained stable. A discussion of the institutional and administrative framework of Tunisia is presented in Annex 2 along with international comparisons. The share of public enterprises in value added has declined, from 29% in 1990 to 22% in 1996; corresponding data on employment are not available. The decline of the share of public enterprises resulted from the expansion of private business; privatization had in fact not significantly reduced public assets in the productive sector until 1998, when two large cement companies were sold to private investors (Chapter 3).

Governance of Public Enterprises

63. The government's policy commitment on the role of the state in the economy is unambiguous: the growth strategy is to be market-based. This implies that public enterprises in competitive markets will be privatized or closed; enterprises with commercial character that operate in non-competitive markets—e.g. the major utilities—are expected to remain in the public sector in the near future.

64. The implementation of the government strategy has proceeded, albeit with an uneven record. On the one hand, the privatization program announced over a decade ago is being implemented very slowly (progress made in 1998 was, however, encouraging). On the other hand, public enterprises that are to remain in the public sector have been given a clear mandate, consistent with the government strategy, to provide public services in an efficient and profitable manner. However, important changes remain to be introduced for this governance strategy to be effectively implemented for all important firms still in the public sector.

65. The regulatory framework within which these public enterprises operate, and especially the system of budgetary controls to which they are subjected, have been deeply reformed in the course of the past decade. The definition of their objective as the efficient and profitable provision of public services within their mandate restricts their activities to well-defined areas—for example, it prevents Tunis Air, the public airline company, from investing in hotels. In some cases (e.g. for public enterprises that receive direct budgetary allocations), costs related to public policy objectives attributed to the enterprise are quantified and reimbursed. *Contrats de programme* have been refined, specifying targets in terms of quantity, quality and price of services provided, and returns on assets.

66. Despite these reforms, the transition from a system based on administrative controls to one based on achievement of results is not yet complete. The governance system remains very complex and is still characterized by a measure of arbitrariness and uncertainty. And adequate managerial autonomy has not been granted to make the profitability mandate fully credible and achievable.

67. The following aspects of the present regulatory framework clearly limit the autonomy of public enterprises to achieve their objectives and accountability:

- The rules and expectations directing the boards of public enterprises are not sufficiently clear to provide for effectively discharging their responsibilities for strategy determination and control. This problem is exacerbated by the existence of parallel rules and organizations that impact on the firms' controls and strategic choices. Chief among these are the *contrats de programme* negotiated with the Ministry of Economic Development, and the fiscal and budgetary controls exercised by the Ministry of Finance.

- The makeup of the boards of public enterprises is a source of confusion. Directors should concern themselves exclusively with strategic orientations and their implementation. But, apart from board chairmen, who are generally chosen by the highest level of the executive branch of government, most directors are selected from ministries with effective supervisory authority over the enterprise, including the Ministry of Economic Development, the Ministry of Finance and the relevant sectoral ministries. The confusion arises because these ministries can influence the enterprises both through administrative control instruments and instructions given to their representatives on the boards. In addition to this confusion about roles, board members are likely to have little time and resources to devote to their functions as "owners" of public enterprises, given their heavy responsibilities as senior government officials. Taken together these factors result in an unclear governance and accountability framework.

- *Contrats de programme* are negotiated between enterprises and the relevant ministries with the concurrence of the central agencies. Those reviewed by the mission were precise and comprehensive, but did not escape the limitations inherent to these instruments. First, they are not real contracts, as they include neither sanctions nor recourse in the event of breach of contract. Second, their very comprehensiveness prevents them from specifying priorities among multiple objectives: multiple unweighted indicators of performance thus arise, preventing their use as clear accountability guidelines. For instance, in urban transportation, the *contrat de programme* specifies the commitments of the firm in terms of levels of services, investments to be realized, prices, and clients. It, thus, could be an efficient way of specifying what the government expects from a supplier. As the main governance instrument for an enterprise for which a clear distinction is sought between its commercial and public service functions, the *contrat de programme* is both too little and too much. It includes a long string of objectives—unweighted—without even considering the likely tradeoffs between objectives and the rules that could then be used to decide priorities. But, at the same time, it confirms the primacy of economic efficiency in distinguishing public service functions while refraining from defining how these missions impede maximizing returns on assets. This is left to budgetary negotiations on the amount of compensation for these public service tasks.

- These problems with *contrats de programme*—which in Tunisia are state of the art documents within the genre—could indicate problems inherent in this governance instrument. It seems that it has not aged well and that it is poorly suited to present needs. This is not really surprising, given its original purposes. When it was designed, in France between 1965 and 1970, the *contrat* was to serve two objectives. Its main objective was to ensure that public enterprises were effectively used as instruments of public policy, in particular industrial policy. (On this score, the *contrat* has generated famous heirs: the agreements negotiated between ministries and central agencies in many countries where substantial financial and managerial autonomy has been granted in return for performance commitments.) Secondly, *contrats were designed* to insulate day-to-day management from political interference.

- All in all, the evolution in Tunisia's public enterprises has generated stronger alternative mechanisms to realize the original objectives of the *contrats de programme.* Public enterprises remain subject to an array of fiscal and quasi-fiscal controls. The Ministry of Finance approves annual budgets, investments, medium-term business plans, and staffing levels and allocations; in addition, it negotiates with each public enterprise its annual additional contribution to the budget over and above regular taxes.[26]

- The reimbursement for costs incurred in the fulfillment of public policy mandates attributed to the public enterprise—for example railroad tariff discounts to students and military personnel—is limited to enterprises with direct budgetary allocations. In general, self-financing public enterprises, e.g. gas and electricity utilities, do not receive such compensation. In other words, the self-financing public enterprises still operate under the old model, which allows for opaque cross-subsidies and low accountability given the effective confusion between their public policy and commercial activities and objectives.

Administrative Reform

68. Administrative reform efforts are a clear expression of high-level commitment to modernizing the public administration. However, these efforts have been limited by their focus on improving performance within the current structure. Structural changes are needed to generate a leap in the productivity of the public administration. Indeed, structural reforms were at the forefront of initiatives in all countries where solid results in administrative productivity increases have been obtained.

69. Administrative reform in Tunisia has been in progress for a long time. In 1972 the *Conseil supérieur de la Fonction publique et de la Réforme Administrative* was established; in 1979, the *Secrétariat d'État à la Fonction publique et à la Réforme Administrative* was created within the Prime Minister's Office. During the 1980s, administrative reform moved toward deconcentration and strengthening of local administrations. During the early 1990s, efforts were directed at improving relations between the administration and the citizens, with the creation of the ombudsman, the corps of the *Citoyen superviseur*, and the offices of relations with the citizen (placed in central and local administrative buildings and public enterprise offices). These efforts will be discussed in detail below.

70. Since the mid-1990s, the focus of reform efforts has been on rationalizing and consolidating legislation, codifying procedures, and informatization of processes. In addition, the capital and recurrent expenditure budgets have been integrated, thereby introducing an important element of multi-year budgeting. Finally, significant progress was achieved toward rationalizing compensation with the introduction in 1997 of legislation that consolidated the salaries and most indemnities and cash benefits of civil servants, facilitating mobility within the administration. Higher-end pay scales were also expanded, facilitating the retention of high-skill staff.[27]

***Mise à Niveau* of Ministries**

71. A number of pilot initiatives have been recently undertaken in the context of the *mise à niveau* of ministries, focusing on the definition of staffing plans, the introduction of cost accounting, management by objectives, and incentive pay. Progress to date has been limited, however, and there are questions as to the effectiveness of some of the measures being taken, such as the definition of staffing plans (Box 2.3).

[26] Taxation on public and private enterprises is identical.

[27] The salary differential in the Tunisian public administration remains however small, with a ratio of 1 to 5, in comparison with other countries (see Annex 2).

Box 2.3: Pilot Initiative for the Definition of Staffing Plans

The formulation of staffing plans is a pilot project for the administrative services in three ministries: health, agriculture, and commerce. The immediate objective is to define the staffing levels and composition needed to accomplish administrative functions; the ultimate objective is to facilitate reallocation of staff within the civil service. This is the only initiative currently in progress where an attempt is made at measuring productivity. Extension of this pilot to the rest of the core public administration is planned for the next two years.

The pilot is very limited with regard to its object (only administrative functions). It is not methodologically rigorous. Staffing plans are prepared by individual units and then negotiated in the same way as budgetary allocations. It is static in its approach, despite the dynamic nature of productivity growth, which rests upon, among other things, on increased innovative capability, reduced lags in adapting to evolving needs, control systems involving users, harnessing individual, and managerial initiatives and abilities.

Innovation at the *Cour des Comptes*

72. The limited results thus far achieved in the *mise à niveau* of ministries can be contrasted with the experience of the *Cour des Comptes*, which has successfully modernized its approach to ex-post control and audit on the basis of international standards. The emphasis on comprehensive auditing may well provide the needed guidance to an ex-post evaluation function, which is not yet deeply rooted in Tunisia. The most important institution of ex-post control is thus positioned to facilitate the transition to management by objectives and control of results rather than compliance.

Improving the Relation between Public Organizations and Citizens

73. The reforms implemented in recent years to improve the relation between citizens and public organizations are among the best observed in countries at Tunisia's level of development. They are important in two respects. First, from an economic perspective, they are a concrete effort to reduce access costs to public services for citizens (though not necessarily for enterprises); and second, from a public management perspective, they are an attempt at utilizing user feedback to improve the performance of public organizations.

74. In addition to the new structures discussed below, one major element of this effort has been a thorough rationalization of regulations and paper burden imposed on citizens. Regulations have been drastically reduced in numbers and harmonized across ministries. The reduction in administrative discretion has been a major target of the effort; to that end, what can be demanded from citizens has been clearly defined and published.

75. As introduced over the last few years, the present structures involve three organizations that report to the President's Office either directly (as is the case for the case of the Ombudsman), or through the Prime Minister's Office:

- *Médiateur administratif* (Ombudsman): receives complaints from citizens, evaluates them, instructs the appropriate agencies to follow up, and ensures that adequate follow-up is provided.

- *Bureau des relations avec le citoyen:* is a network of offices located in each ministry, region, and public enterprise, which receive citizens, direct their questions to the appropriate agency and explain procedures. The decentralized offices of the Bureau are also responsible for following up citizen complaints processed by the Ombudsman or brought directly to them. They report to a central office in the Prime Minister's Office, which is responsible for oversight and for identifying and resolving procedural and regulatory problems detected by the number and severity of problems encountered by citizens and the difficulties experienced by administrations in handling those under present regulations. For instance, long standing identity papers problems—dating back to naming procedures inherited from the Protectorate era—were solved by overhauling the regulatory framework at the initiative of the bureau. This central office has also recently been charged with relations with NGOs to facilitate achieving its objective of effectively reaching all regions and social strata in the area of relations between the citizens and the administrations and assist NGOs in expanding their actions in Tunisia.

- *Équipe du Citoyen Superviseur*: established in the Prime Minister's Office, it is responsible for active supervision of public agencies. This takes the form of staff posing as citizens, and making anonymous visits to public agencies to establish access to, and quality of, public services on the basis of well defined criteria.

76. To date, the experience with this system indicates very clearly that it is possible to design and rapidly implement a mechanism of prevention, control, and feedback to limit administrative arbitrariness and promote equal access to public services. However, the limits of the present system are also evident: the feedback mechanisms are not complemented by arrangements to promote continuous improvements in the quality of public services and productivity of the public administration.

77. In this respect, given their quality and comprehensiveness, the present mechanisms constitute a great forgone opportunity: indeed, international experience in the past two decades has shown that broad-based systems of control and feedback can be more efficient and more robust than centralized ones. To take full advantage of the existing systems, steps should be taken in two directions. First, information about the results achieved should be made public to improve the system of checks and balances between citizens and the administration. For example, data on the use of the services discussed above, and the extent of citizen knowledge and comprehension of them, have been collected through surveys, but are not available outside the public administration. Thus, the decline in the Ombudsman's case load from 4,000 cases in 1996 to 2,500 in 1998 could be interpreted as a measure of success— citizen complaints have led to administrative changes—or as a sign of failure—citizens stopped lodging complaints because they concluded this served no useful purpose. Second, to take advantage of the potential of existing mechanisms to improve productivity, it would be necessary to expand the information collected to include broad measures of user satisfaction with public services, and to use rigorous measurement methods to assess administrative performances.

C. Future Directions for Better Governance of Public Organizations

78. The remarkable evolution of the Tunisian public sector in recent years strongly supports the view that further reform of the governance system is achievable, and that public organizations can make a greater contribution to economic growth. In addition, further reform can be built on the strong foundation of the many important achievements reviewed in the previous section.

79. The most difficult challenge, as witnessed by difficulties encountered by administrative reforms everywhere, is to provide governance institutions capable of sustaining productivity growth over time. This objective is a long-term and structural one; it is not attainable via simple fiat, however energetic those commands may be. Only changes to governance institutions can provide for continuous productivity growth equivalent to those arising from the competitive forces that drive firms to improve managerial methods and techniques, to reposition themselves

constantly to meet evolving clienteles and opportunities. To ensure that productivity growth occurs as naturally and continuously in the public administration as in market situations, two elements are necessary: the involvement of citizens—the direct beneficiaries of the services provided by the public administration—and establishing a decentralized system of governance based on achieving public objectives and harnessing managerial innovative abilities instead of relying only on financial controls of inputs.

80. Experience from Costa Rica to Finland has shown that to sustain productivity growth it is critical to involve the citizens systematically. In this context, the role of citizens is equivalent to that played by customers in market situations, though obviously through different channels. This systematic involvement in turn requires both open scrutiny—through the press and citizens' organizations—and direct feedback from users to the level of management within the public administration and the levels at which the production or delivery of public services takes place.

81. Again, overwhelming international experience indicates that sustaining productivity growth in the public administration requires the establishment of a system of governance focused on achieving results. In Tunisia, overcoming the current approach based exclusively on centralized controls on inputs is the necessary first step in this direction. The current approach—based exclusively on centralized budgetary input allocations and controls on disbursements—is generally effective in controlling simple variables (disbursements) or to establish new organizations with simple objectives. But the evolution of the public sector over time has led to more complex objectives and structures. In this context, the current approach has laid the correct foundations for future reform, but is no longer sufficient.

82. Centralized control, together with greater complexity leads to rigidity, unresponsiveness, and inefficiency. Again because of complexity, the ability of a centralized control system to ensure compliance with regulations and the realization of public policy objectives is largely illusory and further increases the distance between the locus of decision making and the users of public services. Finally, the continuous growth of productivity within a complex structure with multiple objectives is a dynamic phenomenon, and promoting it in a continuous and sustainable manner requires deep knowledge usually unavailable at the center, far away from where public services are actually delivered to their users.

83. Moving from a system based on centralized control on inputs to one based on results does not need to reduce financial discipline, or increase risks of fraud or abuse of authority. In the first place, while existing ex-ante controls should be greatly reduced, technical progress has already rendered them largely obsolete. Second, necessary ex-post accounting controls on the use of resources should remain in place even in a result-based system, which in fact introduces an additional form of control—based on achievement of objectives. Third, the current system of controls functions very well and thus it should be possible to reform it without significant efficiency losses. Finally, it should be emphasized that on the international scene, the early initiatives leading to the introduction of results-based systems were motivated precisely by the need to reduce expenditures without reducing the level and quality of public services, and evidence from the past 20 years supports the view that these objectives can indeed be achieved.

Implications and Additional Challenges for Public Enterprises

84. Success in improving the incentives framework for those enterprises that will remain in the public sector in the medium term is necessary for economic success.

These enterprises provide services such as energy, water and sanitation, transport, and telecommunications that are critical for the productivity of private enterprises. Improving governance of these public enterprises has three other important benefits. First, it will contribute to maintaining and improving the competitive position of Tunisian enterprises vis-à-vis the EU, second, it will provide incentives and an example of reform in the rest of the public administration. Finally, it will allow those enterprises to face up to the direct competition arising from the worldwide breakdown of protected monopoly positions in such industries.

85. Improving the governance, and, thus the performance, of public utilities will be critical to increasing the competitiveness of Tunisia in the context of its partnership with the EU; both to improve the competitiveness of present firms and attract foreign investment. This will be discussed in Chapter 3, but here it is important to note that similar reforms are being undertaken inside the EU and by countries that are planning to accede to the EU in the near future. A critical objective of these countries is to improve the cost/quality mix of the services produced by the public sector, and to offer enterprises a greater choice of providers. Tunisia is beginning to move in this direction, for instance in rail transport—where management and ownership have been separated—but will need to increase its efforts rapidly if it is not to lag further behind the EU or the countries planning accession in the near future.

86. Historically, the modernization of public enterprise governance has been the leading force for administrative reform and especially for the introduction of result-based governance. In fact, it is much easier to measure results of public enterprises than of services delivered by ministries, and to attribute larger managerial autonomy to enterprises than to public administrations. This is also true in Tunisia, and in fact the modernization of public enterprises is ahead of that of the administration.[28]

87. In its current stage, the governance of public enterprises in Tunisia is typical of a sector in transition. On the one hand, there is clarity about day-to-day managerial autonomy; although there is less progress on clarification of enterprise objectives and results as provided in *contrats de programme*. On the other, there remains a ministerial control structure, dating from the past, that requires enterprises to seek approval for staffing plans, annual budgets, investment plans, and prices. Even more importantly, the incentive system is weak. Quasi-fiscal controls lead to uncertainty, especially about contributions to the budget and pricing policies; the weaknesses in the composition and mandate of the boards confuse governance structures; the design and implementation problems of the *contrats de programme*, as discussed above, remain and are unlikely to be remedied by further refinements, and mechanisms are not yet in place to compensate self-financing public enterprises for fulfilling public policy mandates.

88. Further progress in making public enterprises truly independent and accountable for the fulfillment of a complex but clearly defined set of objectives will require the completion of on-going reforms. To this end, it will be necessary to focus only on essential controls—taking into account their negative impact on the autonomy of enterprises—and providing clearer performance incentives. The following measures should be considered:

[28] However, some significant success has also been achieved within the administration: for instance, in the case of hospitals a framework essentially analogous to that of state enterprises has already been implemented. It would be useful to attribute to some unit in the administration the task to monitor the lessons from the experience of state enterprises that can already be applied to other institutional arrangements, including the administration.

- Accountability should be based on a limited number of economic indicators, e.g. return on capital.

- Performance should be confirmed by external audits and evaluations, and both should be made public.

- The incentive framework should be more certain, especially with regard to the treatment of profits, and including taxation, transfers to the budget, and pricing policies. For instance, public enterprises should be able to know their fiscal burden in advance and not negotiate it each year. Also, a clear dividend policy should be articulated by the state as shareholder to reduce uncertainty and increase accountability for public enterprises managers. On price controls, it could be beneficial for Tunisia to follow present British practices, where prices are set by taking fully into account all the productivity gains expected from firms, thereby providing a strong stimulus for performance improvement.

- Managers of public enterprises should be given full discretion on the choice of productive inputs.

- Business plans should be subject to prior ministerial approval in a multi-year framework, and to ex-post control on an annual rolling basis to establish consistency with agreed objectives.

- The cost of fulfilling public policy mandates should be quantified and reimbursed to all public enterprises.

- Non-transparent or discriminatory business practices should not be tolerated among public enterprises, including arrears accumulation or special discounts.

- Public enterprise procurement should not be used as a means of discretionary intervention, e.g. to provide non-tariff protection to private or public enterprises. At present, problems on this score seem to involve mostly cross-indebtedness between public enterprises. This—and the rather opaque reporting practices associated with it—involve serious risks, as demonstrated by the recent difficulties experienced by the banking sector.

- Recent measures to improve public banks' capital base should be complemented by increasing competition in the sector. The high effective protection granted to this sector can only slow Tunisia's industrial growth by raising the cost of borrowing and limiting the supply of new financial products.

89. These measures are critical to ensuring that remaining enterprises contribute substantially to economic growth, but are unlikely to be sufficient, given Tunisia's growth objectives and its ongoing economic integration with the EU markets. New challenges come from worldwide deregulation in sectors formerly accepted as "natural monopolies"— such as rail, telecommunications, gas and electricity—which have introduced elements of competition or at least contestability. Thus, for Tunisian firms served by utilities to compete with firms such as those in the EU and acceding countries served by utilities with governance structures geared to ensuring competitive outcomes, the bar has to be raised above efficient management and clearly defined objectives.

90. Facing, in the very near future, these second generation challenges means considering a wider array of measures to improve the governance structure of public enterprises. These are needed to empower Tunisian enterprises to export and to allow Tunisian public utilities to prosper in an environment where they themselves will have to compete. Probably the most pressing item in this realm is to establish a clear regulatory framework for concessions and other forms of alliance between public and private enterprises to avoid gray areas of

accountability and integrity where neither the state nor the market have control. This would also allow for a gradual adaptation of these public enterprises to these new challenges, in keeping with Tunisian traditions with reforms and incorporating the lessons from the few examples of such practices being experimented with at present in Tunisia.

Implications for core public administrations

91. The size of Tunisia's public sector (Box 2.2 above) is by itself a strong indication of the possible aggregate gains that can be achieved by increasing productivity in the public sector. In addition, the quality of the public administration is a very important determinant of the enabling environment for private sector development. There is, therefore, no doubt that the payoffs from improving productivity in the public sector can be very significant. And there is also no doubt that such improvement can be achieved in Tunisia.

92. The necessary elements for the successful implementation of a system of governance based on results are listed in Annex 1. It must be stressed that the reform of budgetary processes must be a priority, as this provides not only a key initial impetus, but also the framework for continuous incentives and follow-up measures. Efforts to create a result-based system with solid productivity growth attempted without changing the basic resource allocation framework and rules embedded in budgetary processes, have not fared well on the international scene in the past decades.

93. The starting points along this path of change include the following elements:

- *Introduction of result-based budget allocations.* As discussed above, this is indispensable to give public administrators adequate autonomy to manage with the full benefit of the superior knowledge that they have by virtue of being close to the users. The introduction of some form of functional classification of expenditures adapted to Tunisian preferences will be necessary to implement result-based budgeting.

- *Devolution of financial management authority to public managers*. This will be a necessary complement to the devolution of responsibility to achieve results, and should take place as close as possible to the point of production and delivery of public services.

- *Changes in the functions of the Ministry of Finance.* An important consequence of the shift from ex-ante controls on inputs to ex-post controls on results is the transformation of the activities of the Ministry of Finance toward increased emphasis on policy analysis and monitoring of results.

94. Following the introduction of these measures, it would be possible to launch a productivity drive. The establishment of benchmarks and targets for productivity in a multi-year framework, integrated with the budget process, supported by adequate technical resources, and openly monitored for progress, could make a strong contribution to mobilizing existing energy for modernization and innovation.

Chapter 3. Improving the Environment for Private Sector Development

A. Introduction

95. Like many countries in the region, Tunisia pursued a policy of state-led industrialization until the mid-1980s, when the fall in oil prices caused a severe deterioration in fiscal and external balances. The adjustment and structural reform program adopted in response to the crisis included measures to encourage private investment and redirect the role of the state away from commercial activities, including the announcement of a privatization program. These policies resulted in a significant expansion of the private sector, especially in export-oriented manufactures, a modest but sustained inflow of foreign direct investment, and a reduction in public investment. They did not however result in sizeable divestiture of public enterprises until 1998, when two large cement companies were privatized.

96. The external outlook for Tunisia changed dramatically in the mid-1990s with the Association Agreement with the EU and the phase out of the Multi-Fiber Arrangements. Their implementations—to be completed by 2007 and 2005 respectively—will result in a very large fall in effective protection for domestic industries and in increased competition on export markets. To date, the private sector has assumed a wait-and-see attitude, as indicated by a weak investment performance while sentiment remains positive. However, opportunistic investments have occurred to take advantage of temporary distortions in effective protection caused by the phased implementation of the EU agreement. The public sector response has been a large program of *mise à niveau*, which includes investment incentives for selected producers in sectors that either have had strong export performance in the recent past (textiles and garments, and mechanical and electrical products) or that are judged to have good potential (agro-processing). In addition, the government has expanded its export promotion efforts, introducing a broad set of ad hoc measures ranging from streamlining customs procedures to training.

97. Can Tunisia's private businesses continue to achieve high growth in the face of increased competition at home and abroad? We believe that the answer is affirmative, but the risks have increased:

- The increase in competition at home and abroad will lead to a deterioration of external balances in the short term. On the import side, this deterioration has already begun with the elimination of tariffs on capital and intermediate goods imported from the EU, and will continue as tariffs on imports of other manufactures from the EU will be phased out.[29] This deterioration is likely to be reinforced on the export side, as increased competition in EU markets for textiles and garments intensifies with the phasing out of the MFA.

- Again in the short term, this increase in competition will lead to some industrial restructuring and corresponding labor market tensions, as some workers are laid off in declining sectors and new jobs are created in emerging sectors. In addition, in the short as well as the longer terms, increased competition will need to be met with an overall increase in skill levels and changes in the skill composition of the workforce. The resulting tensions in the labor market are likely to be important, as the unemployment rate, especially among first-time job seekers, is high and the labor market is not flexible enough to facilitate inter-sectoral reallocation of labor.

- Since the EU Association Agreement is expanding access to inputs at world prices to the on-shore sector of the economy, the competitiveness of Tunisian enterprises will increasingly depend on the cost and availability of non-tradable goods and services. These remain to a large extent provided by the public sector in markets that are non-competitive and not yet contested, and their cost/quality mix lags that available to competitors in other emerging market economies.

- The public sector response also entails new risks. The public resources committed to the *mise à niveau* program—some 0.24% of GDP per annum for a period of five years—are very large and their return very uncertain. In addition, the program is generating a new kind of contingent liabilities for the government due to the fact that banks are assuming credit risks with government blessing when financing enterprises participating in the program.

98. These risks can be ameliorated, and the prospects for growth strengthened, by refocusing attention on the enabling environment for private sector development. Tunisia's manufacturing sector is still dominated by small and medium enterprises, which are less likely to benefit from existing programs than large firms. Thus, the *mise à niveau* of the rules of the game, the implementing institutions and the basic infrastructure, will be critical for success of the SME sector and the economy as a whole. The main policy recommendations that emerge from this chapter are:

- Review investment incentives, financing mechanisms, and ad hoc export promotion interventions to reduce variation in the level of support across firms and sectors, establish a more consistent and transparent set of supportive measures for investment and exports, and avoid encouraging footloose industries to take advantage of short-term opportunities.

- Focus on the constraints to the creation of new enterprises and the growth of SMEs. Existing successful enterprises may not be those that will generate the most growth, exports, and employment in the new environment, even if they continue to prosper. While administrative and regulatory constraints do not appear to be high, access to and cost of credit, prime industrial land, and telecoms, are among the most quoted difficulties faced by small and medium private enterprises according to a survey recently conducted by IACE.

[29] Although in the short term, some domestic firms may enjoy an increase in the effective rate of protection due to the fact that tariffs on imported intermediate inputs are reduced, while tariffs on imported competing final goods are maintained for a few more years or reduced gradually.

- Introduce competition or at least contestability in the service sector. This sector remains dominated by public enterprises—banks and utilities—and will not be exposed to increased international competition in the short term, as the EU Association Agreement does not yet include the liberalization of services. Yet services are an important component of overall competitiveness of the economy and especially of the manufacturing sector.

- Move ahead with privatization. Progress in 1998 was very encouraging, especially in terms of privatization revenues, but privatization was slow in 1999. To contribute to overall competitiveness and flexibility of the economy, and to help attract foreign investment, privatization needs to accelerate in 2000 and the years ahead.

- Maintain a prudent macroeconomic stance and a flexible exchange rate management. These have been critical ingredients of Tunisia's success during the past 15 years and will be even more important in the near future. The deterioration of external balances that is likely to follow full implementation of the EU Association Agreement will require prudent and flexible management of domestic demand, including moderating the rate of implementation of the *mise à niveau* program, and flexible management of the exchange rate.

B. The Tunisian Private Sector

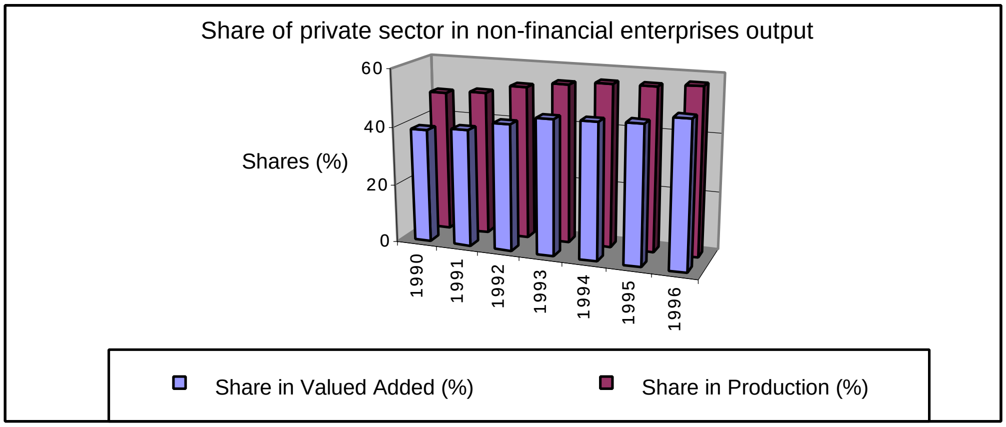
99. The distinction between public and private economic activity is not always clear in Tunisia. The definition of public enterprise has evolved over time. A government share ownership of 10% was sufficient for an enterprise to qualify as public up to 1985; this threshold was raised to 34% that year, and to 50% for non-financial enterprises in 1989. These changes in definition reduced the number of firms classified as publicly owned, but in aggregate, public assets have not decreased substantially. The public sector also permeates the private sector through a complex web of cross ownership and allegiance of private sector executives to public authorities.

100. In addition to the unclear demarcation of ownership and control, the relation between the public and private sectors remains characterized by a *dirigiste* attitude on the part of the former, and a compliance attitude on the part of the latter. On one hand, public programs in support of private sector development provide fiscal incentives or financial support by discriminating between enterprises on the basis of rather minute characterization such as size, sector of economic activity, location, and export orientation. This degree of detail is likely to be accompanied by a correspondingly high degree of arbitrariness, as public officials administering the programs determine what applies to whom. On the other hand, the private sector has often relied on risk-sharing mechanisms with the public sector, such as the *mise à niveau* program discussed below, and on the direction provided by the public sector, e.g. through funding and top appointments.

Performance of the Private Sector

101. *The size of the private sector*. The private sector—defined here as to exclude non-financial enterprises with majority public ownership and financial enterprises with public ownership exceeding 34%—represents about half of industry. In 1996 the non-financial private sector accounted for 57% of output and 50% of value added of non-financial enterprises (Figure 3.1).

Figure 3.1: Tunisia – Private enterprise share in output



Source: Ministère du Développement Economique, *Agrégats et Tableaux d'ensemble* 1990-1996, Vol. I, p.48.

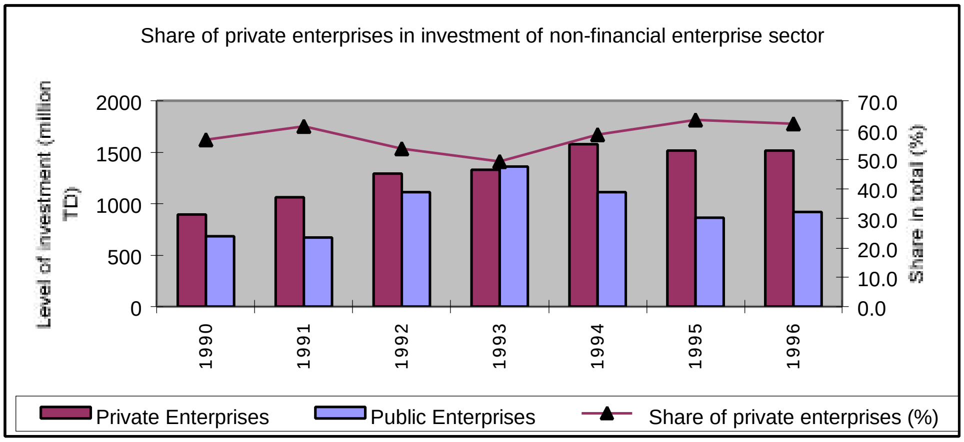
Box 3.1: Privatization in Tunisia

Between 1987 and 1997, 93 enterprises were privatized in full or in part, yielding total revenues of TD397 million. These enterprises were generally medium and small—averaging TD4.3 million—and predominantly in the tourism and handicraft sectors. In 1998 two large cement companies were privatized, yielding about TD400 million. The 1998 experience was particularly successful, not only because of the revenue raised but also because of the method—public offering—and the investors—foreign companies new to Tunisia. Following the slowdown of privatization in 1999, efforts are being intensified in 2000, and a third large cement company has been privatized.

102. *Private investment*. The share of private enterprises in total investment by non-financial enterprises remained more or less flat at about 60% in the 1990s (Figure 3.2). Similarly, total private investment has remained more or less flat as a share of either GDP or total investment in the economy—respectively at about 12% and 50% (Table 3.1).[30] Moreover, Table 3.1 shows that the share of private investment in total investment in Tunisia has, on average, remained lower than in most other developing countries. This performance is disappointing, especially in light of continuous efforts to promote private investment through financial and fiscal incentives as discussed in Section C of the chapter. As will be discussed below, this also suggests that the current policy focus on incentives has reached its limits, and that further increasing the share of private investment in the economy will require accelerating privatization efforts and improving the overall policy environment and incentive framework.

[30] Total private investment comprises private enterprises investment and household investment.

Figure 3.2: Tunisia: Private Enterprise Investment in Total Investment, 1990-96



Source: République Tunisienne, Ministère du Développement Economique,1983, Agrégats et Tableaux d'ensemble 1990-1996, Vol. I, p.48.

Table 3.1 : Private Investment in Tunisia, 1983-98

Period	Total Investment/GDP (%)	Private Investment/GDP (%)	Private investment/ Total investment (%)
1983-86	28.4	13.5	47.5
1987-91	21.6	10.6	48.9
1992-95	26.6	12.3	46.5
1995	24.2	11.7	48.4
1996	23.2	11.7	50.6
1997	24.6	12.4	50.4
1998	25.0	12.8	51.0
Other Countries (1990-95):			
All Developing Countries	23.3	16.5	70.8
- Europe, Middle East and North Africa	21.3	12.3	57.7
- East Asia	34.3	25.6	74.6
- Latin America and the Caribbean	19.1	14.6	76.4

Source: World Bank (2000a).

103. *The Private Sector's Contribution to GDP*. Despite flat private investment ratios (as a share of GDP and total investment) and limited privatization, the share of private enterprises in the output and value added of non-financial enterprises has increased steadily since the early 1990s (Figure 3.1 above). This attests to an increasing efficiency in the private sector, and points to the potentially beneficial effects of a policy of accelerating privatization efforts as a means of transferring ownership of existing assets and improving overall efficiency and value added in the Tunisian economy.

104. *Employment*. Because private sector enterprises are smaller and more labor intensive, their share of employment in the economy is larger than their share of production or value added. A breakdown of employment between the private and public sector based on the 1994 census shows that the private sector employed 83.4% of the labor force, compared to 16.6% in the public sector. These data are not comparable with those on production, value added, and investment, because in the former the government sector is narrowly defined as public administration and excludes public enterprises.

105. Even though data are not available to identify the contribution of the private and public sectors to job creation, the expansion of the private sector since the mid-1980s has been accompanied by strong employment generation, which has averaged 3% per annum since 1989. Aggregate labor market trends will be discussed in Chapter 4; it is however important to note here that trends in employment creation by sector have been very different between subperiods, and that manufacturing and tradable services—two sectors where private businesses dominate—have consistently been at, or above, average job creation in the economy since 1984 (Table 3.2). It should also be noted that the gradual decline in the share of agricultural employment in total employment appears to have stopped since 1994.

106. *Export Performance*. The expansion of the private sector since the mid-1980s has also been accompanied by the transformation of Tunisia from a resource-based (essentially petroleum) to a manufactures-based exporter (Chapter 1). During this period public sector exports, mostly in oil and related products, were gradually overtaken by private sector exports, mostly in textiles and garments. This transition—initiated by falling oil prices—was greatly facilitated by the creation of an offshore sector beyond customs and foreign currency regulations, and preferential access to European markets.[31] The offshore sector quickly became dominated by the textile industry, though more recently, electric and mechanical industries have become more visible.

107. The development of a successful manufactures export sector took place while the private sector producing for the domestic market remained shielded from foreign competition by high effective protection resulting from a combination of high tariff rates on finished imports and low tariff rates on equipment and raw material imports. As a result the onshore sector has been less efficient and has been virtually absent in manufactured exports. In addition, weak linkages between the on- and offshore segments limit the creation of value added and employment in both sectors.

The Environment for Private Sector Development

108. *Access to Funds*. The private sector has received an increasing share of the banking sector's credit to the economy (Table 3.3).[32] However, many small-scale enterprises report difficulties in accessing credit. Central Bank and API data show that, as of September 1999, SMEs (with sales under TD2 million) represented 77% of total enterprises but accounted for 42% of credit to enterprises.[33] This problem does not appear to stem from limited loanable funds but from unwillingness on the part of banks to lend to firms without track records or to accept intangible assets as collateral (which for example penalizes SMEs in the new information technologies sector). A recent survey reveals that, of the SMEs that did not receive bank loans during the preceding three years, 33% of the small enterprises and 15% of the medium enterprises did not obtain credit because of inadequate business plans or insufficient collateral.[34]

[31] The offshore sector exports 90% of its production and controls 40% of Tunisia's exports.

[32] The definition of public enterprise used by the *Centrale des Risques* does not appear to be consistent with the definition of at least 50% government ownership used in the rest of the chapter. In addition, credit to public enterprises excludes foreign borrowing (which are directly obtained by the enterprises) while credit to private enterprises includes foreign borrowing (which are obtained through the banking system). Therefore the share of credit to the private sector as indicated by the table may be overestimated. The trend however suggests that the private sector receives an increasing share of credit to the economy.

[33] The share of SMEs in total sales is not available.

[34] World Bank (2000a).

Table 3.2: Employment by Sector of Economic Activity(1984, 1989, 1994, 1997)

	Workers (thousand)				Growth rate per annum (%)			Share of T (%)	
	1984	1989	1994	1997	1984-89	1989-94	1994-97	1984	1989
Agriculture and fisheries	475.4	509.7	501	546.2	1.4	-0.3	2.9	26.6	25.8
Manufacturing	345.1	382.7	455.7	506.5	2.1	3.6	3.6	19.3	19.3
Food processing	28.2	42.2	48.6	51.3	8.4	2.9	1.8	1.6	2.1
Construction materials	27.4	33.6	33.5	35	4.2	-0.1	1.5	1.5	1.7
Mechanical and electrical	29.7	41.7	48.6	61.3	7.0	3.1	8.0	1.7	2.1
Chemicals	11.2	16.6	16.9	21.7	8.2	0.4	8.7	0.6	0.8
Textiles and leather	203.9	191.2	239.9	259.2	-1.3	4.6	2.6	11.4	9.7
Others	44.9	57.4	68.2	77.9	5.0	3.5	4.5	2.5	2.9
Non Manufacturing	275.5	282.8	342.5	337.7	0.5	3.9	-0.5	15.4	14.3
Construction and public works	237.5	247.6	305.8	304.8	0.8	4.3	-0.1	13.3	12.5
Market Services	253.6	374.7	509.7	579.1	8.1	6.3	4.3	14.2	18.9
Trade	118.3	168.9	217.9	260.5	7.4	5.2	6.1	6.6	8.5
Transport and communication	86.7	95.8	112	122.7	2.0	3.2	3.1	4.9	4.8
Hotels and restaurants	35.5	49.1	75.7	83.8	6.7	9.0	3.4	2.0	2.5
Financial Services	13.1	15.4	22	24.8	3.3	7.4	4.1	0.7	0.8
Other market services	36	45.5	82	87.4	4.8	12.5	2.1	2.0	2.3
Non Market Services	305.8	398.8	476.2	509.3	5.5	3.6	2.3	17.1	20.2
Education, health, administration	251	324.9	382.2	413.2	5.3	3.3	2.6	14.0	16.4
Other non market services	54.8	73.9	94	96	6.2	4.9	0.7	3.1	3.7
Not declared	95.1	30.7	35.5	24.8	-20.2	2.9	-11.3	5.3	1.6
Total	1786.4	1978.8	2320.6	2503.6	2.1	3.2	2.6	100.0	100.0

Note: Other Market Services include Real estate, Repairs and Consultant Services.
Note: In 1984 and 1989: other non-market services = other private plus other public services.
Note: In 1994 and 1997: other non-market services includes also foreign services.
Source: Recensement général de la population de l'habitat, 1984; Enquête nationale population-emploi, 1989; Recensemen population de l'habitat, 1994; Enquête nationale population-emploi, 1997 (tables processed for the World Bank);Institut n statistique, Tunis.

In addition, SMEs with access to bank borrowing face on average higher interest rates than large corporations, (with spreads as high as 7 percentage points over the money market rate) owing to the perception that credit to SMEs is riskier and less adequately collateralized. As a result, many SMEs are funded through personal savings, are undercapitalized, and cannot undertake sizable investments often required for being competitive on the domestic or export markets.

Table 3.3: Tunisia: Credit to the Economy, 1996-98

	1996		1997		1998	
	Amount	Share	Amount	Share	Amount	Share
Including Guarantees						
Public enterprises	1.4	9%	1.7	10%	1.5	8%
Private enterprises	13.4	91%	14.7	90%	16.6	92%
Excluding Guarantees						
Public enterprises	0.7	6%	0.7	5%	0.6	4%
Private enterprises	11.2	94%	12.4	95%	14.1	96%

Note: TD million, end of year.
Source: Central Bank of Tunisia, Centrale des risques.

109. In part to relax the constraints on the establishment and growth of SMEs, since the beginning of the 1990s the government has encouraged the creation of venture capital firms, by, among other things, granting them a complete profit tax exemption. Seventeen venture capital firms have been established but they remain small and are yet to be active in financing small projects, particularly in new sectors. More recently, in February 1999, the government established a fund for the promotion of small firms in information technologies.

110. *Transportation Services*. The bulk of Tunisia's external trade in goods (95%) is done through shipping. Therefore, high cost, slow port handling, and inefficient shipping services constrain the efficiency of economic activity and hamper export competitiveness. Progress has been made since 1994, including simplifying customs procedures through the introduction of a single document (*liasse unique)* as in the EU. However, dwelling time in port and the length of customs procedures are still very long in Tunisia, especially when compared to its ambition to be a successful exporter. For example, merchandise dwelling time in port and customs clearance time remain longer in Tunisia than in Morocco, Brazil, or Argentina (Table 3.4). Moreover, a recent survey of Tunisian private enterprises indicates that various steps involved in import procedures take on average 19 days for large enterprises, and about 33 days for SMEs.

Table 3.4 : Efficiency of port services and customs procedures: Tunisia andomparators

Country	Dwelling time in ports	Customs clearance time
Argentina	4/5 days	3 hours
Brazil	4/5 days	
Morocco	12 days	12-24 hours
Tunisia	Up to 18 days	48-72 hours

Source: World Bank (2000a).

111. Some progress has however been made toward liberalizing maritime transport. The government has approved a law abolishing the privileges granted to Tunisian ship-owners in chartering, and a law on commercial port handling. However, the authorities were soon reminded of the importance of market regulation in a liberalized environment, when some shipping companies formed a cartel, keeping shipping prices from declining as expected. The authorities have since dismantled the cartel.

112. International air transport is provided by several international companies and Tunis Air, the national company. As a result of competition among providers, the cost/quality of services compares well with international standards. However, Tunis Air faces higher costs than its international competitors, because of the small size of its operations and an excess workforce. The company sold 20% of its shares to the private sector in the mid-1990s, and is now restructuring to reduce costs and rationalize management and staffing.

113. Road and railways are the main means for in-country transport of goods. The road network is well developed for a country the size of Tunisia, but railway performance is below international standards. The restructuring of the railways now underway (including separation of ownership from management), and increased competition from road transport are expected to bring about the needed improvement in railways performance.

114. *Telecommunication and Information Services*. The cost and quality of telecoms and information services are critical for the success of private business in an era of global competition. Since 1997 Tunisia has made good progress in telecommunications development. Waiting time for a fixed telephone line connection has declined from several months in 1997 to 15 days in 1999 in urban areas. The disruption rate has been reduced from 0.7 to 0.4 during the same period. Digitization of the telephone network has increased from 10% in 1987 to 100% in 1999. And following international trends in tariffs, the Tunisian authorities have implemented a series of telephone tariffs reductions since 1997 (Table 3.5).

Table 3.5: Tunisia: Tariffs for International Telephone Calls, 1997-99

Country of call termination	Old tariffs (December 1997) Tunisian dinar per minute		New tariffs (December 1999) Tunisian dinar per minute		Percentage decline of regular tariff
	Regular tariff	Reduced rate	Regular tariff	Reduced rate	
Maghreb countries	0.63	0.567	0.54	0.486	14.3%
Arab countries	1.5	1.35	0.9	0.81	40.0%
Sub-Saharan African countries	1.5	1.35	1.08	0.972	28.0%
North America	1.5	1.35	1.08	0.972	28.0%
North and Western European countries	0.98	0.882	0.9	0.81	8.2%
Other European countries	1.5	1.35	1.08	0.972	28.0%
Rest of the world	1.75	1.575	1.08	0.972	38.3%

Source : Ministry of Communications, Tunisia.

115. Despite the important progress accomplished over the past two to three years in the area of telecommunications development, Tunisia still lags behind many middle-income countries in terms of fixed-line telephone density (Figure 3.3). In mobile phones, Tunisia had 5.3 subscribers per 1,000 people in early 1999. Although this represents a sizeable improvement over previous years, it still leaves Tunisia behind the rate achieved by Sri Lanka in 1997.[35] Moreover, telecommunications appear to have developed almost exclusively as an urban phenomenon in Tunisia. With 36% of total population, rural areas have only 1% of Tunisia's fixed telephone lines (Figure 3.4).

116. The main challenge for Tunisia is the large role still played by the public sector in telecommunications services. In fact, the government continues to press ahead with large investments in telecommunications despite the international trend toward divestiture that allows for more competition, better quality, and more efficient services.[36] Deeper reform of the telecommunications sector will be required to speed the progress initiated over the past few years and strengthen the competitiveness of the whole Tunisian economy. Reform could include privatizing traditional telecommunications services while ensuring adequate coverage of rural demand, as was done in Chile where the government worked in partnership with private investors to develop rural telephony. Other measures could include strengthening the regulatory framework to ensure that competition rules are followed by the private investors whose number is bound to grow in the future, and introducing more competition in Internet service provision.

117. The development of the Internet in Tunisia had long been held back, but the country is gradually shaping its Internet outlook to the requirements of a modern economy. Tunisia was first connected to the Internet in 1990, but the market grew slowly under government stewardship. In 1996 the authorities created the *Agence Tunisienne Internet* (ATI) to monitor and coordinate Internet expansion. Due to the exorbitant prices charged by ATI, connectivity remained low. In March 1997 ATI tendered two licenses to provide commercial Internet services to residential subscribers and private corporations. Monthly subscription fees were reduced dramatically and the numbers of Internet accounts leaped from 111 in 1996 to 30,000 in 1999.

118. However, Internet usage in Tunisia is below its potential and fast demand growth is to be expected in the near future. In a 1999 survey, 52% of the heads of enterprises participating in the *mise à niveau* program said they planned to create company websites within a year or so.

C. The Incentives Framework for the Private Sector

119. The development of the private sector in Tunisia has been accompanied by generous tax breaks for investment and export, and by progressive rationalization of the regulatory framework. The incentives framework for private sector development is currently characterized, on the one hand, by low administrative barriers to entry and, on the other, by a complex set of investment and export promotion measures. While low administrative barriers to entry facilitate the creation of new firms as opportunities evolve, the small and medium enterprises that dominate the manufacturing sector[37] are

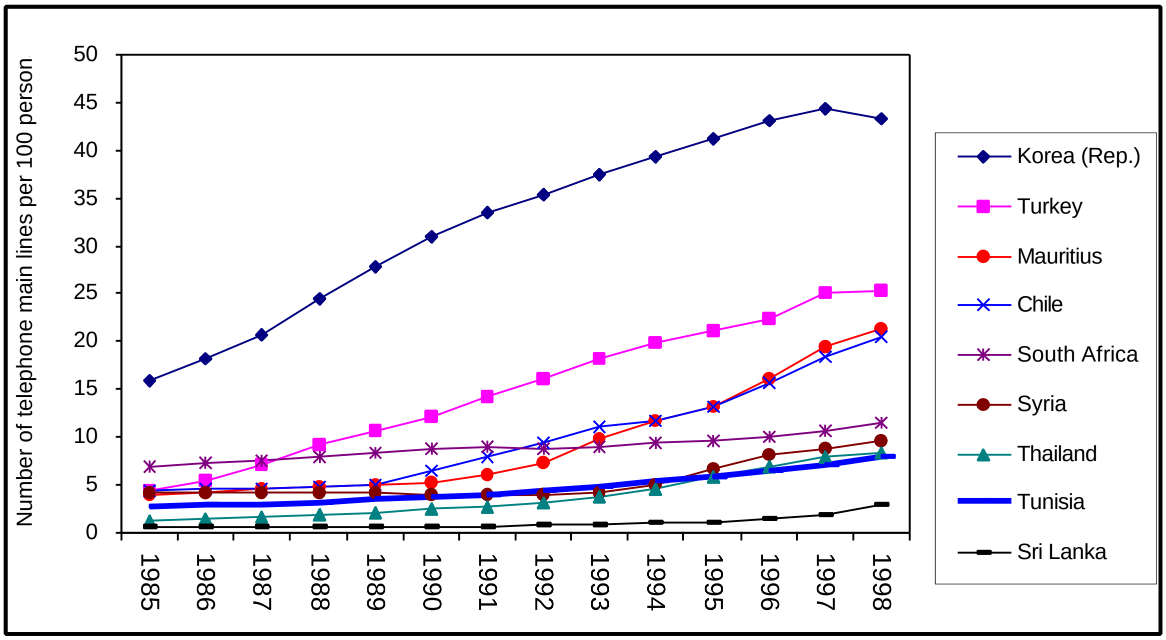
[35] It should however be noted that fixed lines density is lower in Sri Lanka (Figure 3.3). In Sri Lanka, mobile phones seem to be used as a substitute for fixed lines, more so than in Tunisia.

[36] See World Bank (1998b).

[37] In the industrial sector, firms with fewer than 20 employees account for almost 60% of all active private companies; and 77% of manufacturing firms have a sale of less than 2 million TD (see World Bank (2000a) for more details).

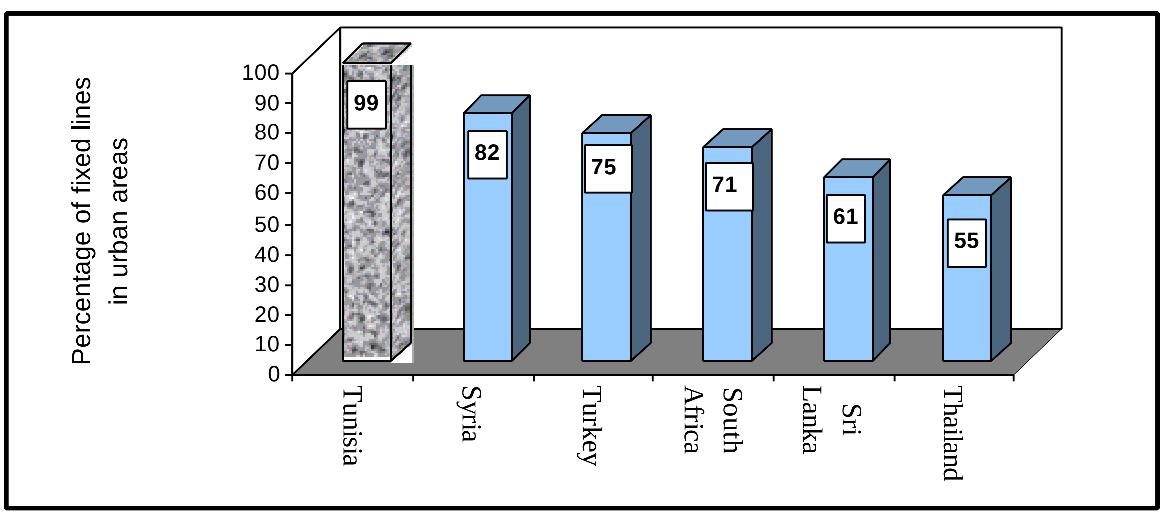
less likely to benefit from existing programs than large firms because of their complexity. Complex rules are also likely to generate uncertainty, as public officials need to decide which measures apply to whom.

Figure 3.3: Telephone density: Tunisia and comparators, 1985-98



Source: World Bank: *World Development Indicators* and International Telecommunications Union data base.

Figure 3.4: Urban-rural gap in teledensity: Tunisia and comparators, 1998



Source: World Bank: *World Development Indicators* and International Telecommunications Union data base.

Taxation

120. Tunisia has a single income tax for individual income and corporate profits. The corporate income tax is generally 35% except for agricultural companies and handicrafts, which pay 10%. Public and private enterprises are subject to identical taxation. To encourage firms to issue shares on the Tunis stock exchange—and thus adopt sound and transparent accounting standards—a measure was recently introduced to reduce the corporate tax rate from 35 to 20% for firms that issue shares on the stock market for the first time. The most important domestic indirect tax is a value added tax with a base rate of 18%, reduced rates of 6% for "sensitive products" and 10% for certain capital goods, and a higher rate of 29% for luxury products. The tax base and rates for the VAT have been expanded since 1996, as this tax is being used to progressively recover revenues lost as a result of import tariff elimination under the EU agreement.

121. Tariffs on international trade are not excessively high in Tunisia, and have begun to decrease under the EU agreement.[38] However, the proceeds of trade taxes have historically represented a large share of general revenues (about 26%), compared to other lower-middle-income countries (about 10%) and the MENA region (about 14%) because of the relatively larger share of trade in Tunisia's GDP (Figure 3.5). The large weight of trade taxes in Tunisia's general revenues can create a fiscal challenge because of the large revenue shortfalls that can result from the decreases in tariffs scheduled contained in the EU agreement (Chapter 1).

[38] The maximum tariff rate was 43% in 1997; the authorities plan to rationalize tariff rates schedule and reduce the maximum rate to 25% by 2001.

The Investment Code

122. Over the years, the government has established a generous system of fiscal and financial benefits for enterprises (set out in the *Loi n^o 93-120 du 27 Décembre 1993, portant promulgation du code d'incitation aux investissements*). The law and supporting regulations provide incentives for investments in the export sector, in certain regions, and in agriculture (Box 3.2). Since 1994 investments in supporting sectors also qualify, including professional development, education, health, energy management, R&D, environment, culture (cinematography), and handicrafts.

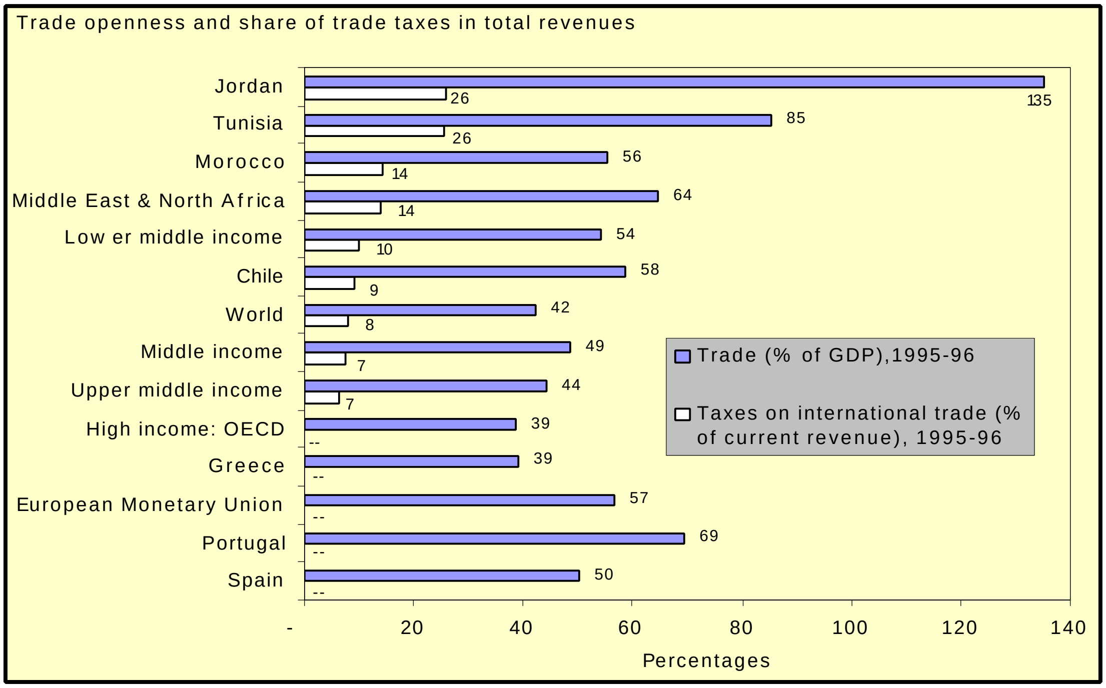
123. In response to the prospect of heightened competition for Tunisian producers at home and overseas, the *Conseil Supérieur de l'Exportation* and the *Commission Supérieur d'Investissement* have introduced investment and export incentives that complement the Investment Code. The main incentives provided are summarized in Annex 3.

124. The total value of fiscal and financial incentives provided by the investment code was estimated by the Ministry of Finance at TD400 million in 1997. Of this amount, TD323 million were for fiscal incentives—of which TD190 million were for tax reductions (*dégrèvements*)—and TD76 million for financial incentives.

125. The main beneficiaries of the incentives provided by the investment code are offshore enterprises, which are at least 80% exporters, even though exporters are excluded from financial incentives. Offshore enterprises, in addition to benefiting from full exemption from tariffs on imported inputs, benefit from the most generous tax holidays provided by the investment code: those directed to exporters. Onshore enterprises, on the other hand, benefit from exemption from tariffs on imported inputs only to the extent they export (through the duty-drawback system) and receive

incentives provided by the investment code on a selective or pro-rata basis.

Figure 3.5: Tunisia: Reliance on trade tax revenues



Source: World Bank, *World Development Indicators*.
Note: "--" is used to represent shares (or numbers) that are not significantly higher than zero.

Box 3.2: The Investment Code

The main provisions on the Investment Code include:

- *Tax Holidays*. Investments in exports, specific regions, and agriculture qualify for a 10-year tax holiday applied to income from the investment. Afterwards, tax is paid at half rates for a period of 10 years in specific regions, and indefinitely in the export sector. For enterprises that are classified as partial exporters (whose production is not mostly for export) tax reductions are pro-rated.

- *Reduction of Indirect Taxes*. Importation of equipment for qualifying investment is exempted from import tariffs and other taxes (except for the imposition of the value added tax at the rate of 10%), as long as there is no similar equipment available locally. Local equipment purchases are exempted from value added and consumption taxes.

- *Investment Premiums*. Financial incentives are provided in the form of premiums paid for certain investments in activities that the government wants to encourage, but excluding export activities (which however benefit from the other two types of incentives). For instance, investment in agriculture qualifies for a premium of 7 to 25% of the investment. Investment in certain regions can earn premiums ranging from 15 to 25%. Newly created SMEs qualify for premiums of 10% on up to TD3 million of own investment. The *Commission Supérieur d'Investissement* can grant an additional premium of 5% for investments that are important for the national economy or are located in border regions. The premiums—which can add up to 30% in the case of a new investor in a high priority zone—are paid in three installments (40, 30, and 30%), with the final payment disbursed when the investment is completed. The premium is not deducted from the value of the investment used in calculating amortization for tax purposes, resulting in an additional benefit for the investor.

126. Less developed regions have benefited less than expected from the incentives provided by the investment code. On the basis of poor indicators of education, unemployment and electrification, the code specifically targets 138 *Communes* (out of 252) with investment premiums of 15% (for new investments located in 125 *Communes*) or 25% (for new investments in the 13 most disadvantaged *Communes*). Most disadvantaged areas benefit also from other incentives, targeted to agriculture and newly established small enterprises. Despite these incentives, the realization rate of investment plans in disadvantaged areas has been disappointing, reaching only 42% in the south, 24% in the northwest, and 8% in the center west region as of end-1998.

Foreign Investment Promotion

127. Tunisia has a long-standing record as a location friendly to foreign investors, who have generally invested in the energy sector—until recently, almost the exclusive beneficiary of FDI—and the offshore manufacturing sector, where incentives are most generous (Figure 3.6). Between 1995 and 1997, non-energy FDI rose modestly, possibly as a result of positive investor sentiments following the signing of the EU agreement. In 1998 non-energy FDI increased markedly, corresponding to the privatization of two large cement companies (*Cimenteries de Jebel Ouest* and *Enfidah*), which fetched about TD400 million and brought the overall level of FDI to TD760 million.

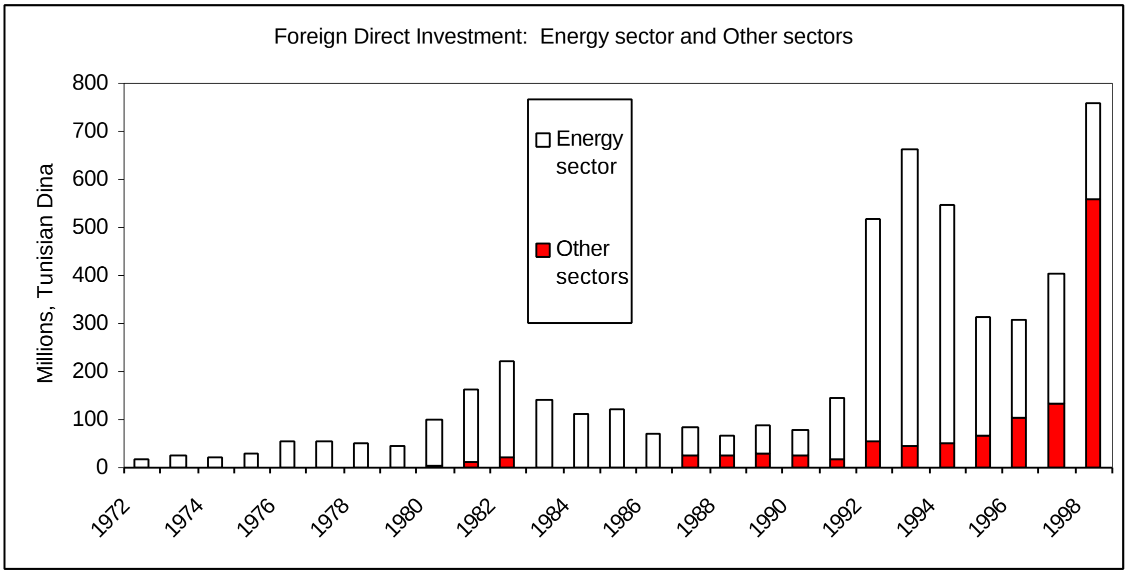
128. Two agencies are involved in foreign investment promotion: the Foreign Investment Promotion Agency, which actively promotes foreign investment through investment forums and seminars in Tunisia and abroad; and the *Agence de Promotion de l'Industrie*, which is charged with facilitating the entry of foreign investors. However, foreign investment reaching majority shares in enterprises that are not fully export-oriented remains subject to approval by the *Commission Supérieure d'Investissement*.

The *mise à niveau* program

129. A key government initiative to meet the twin competitive challenges of the EU agreement and the phasing out of the MFA is a comprehensive program to help manufacturing industry adapt and upgrade its methods and practices of organization, management, innovation, training, technology, distribution, marketing, communications, and research and development.

130. The program includes a component for the *mise à niveau de l'environnement*, aimed at improving basic and technological infrastructure and at upgrading institutions providing support and promotion. The program includes also a component for the *mise à niveau de l'entreprise*, which envisages public financing for the design and implementation of restructuring plans to enhance the competitiveness of enterprises identified as having high potential (Box 3.3). An overall investment of TD2.5 billion is expected over 1996-2001. Of this amount, which represents an average yearly investment of 2% of GDP, it is envisaged that 80 to 90% will be financed by bank credits and enterprise own funds and the remaining 10 to 20% by government funds in the form of investment premiums.

Figure 3.6: Tunisia: Trends in foreign direct investment.



Source: Government of Tunisia.

131. The program for the *mise à niveau de l'entreprise* targets 2,000 enterprises—400 a year over five years—out of an estimated total of 4,000 eligible enterprises.[39] To participate in the program (Box 3.3), an enterprise must submit a detailed application and demonstrate strong growth potential, a good market and promising products at existing quality/price ratios that can be improved. Size, industry, and location are supposedly not a factor determining acceptance in the program; however, the program has sectoral targets for participation that reveal an export-oriented bias in favor of the textile and clothing, and the mechanical and electrical subsectors.

132. Progress in the *mise à niveau de l'entreprise* program is shown in Table 3.6. Between March 1996 and February 2000, 645 restructuring plans were approved, for a total investment of TD1,216 million. The total value of investment premiums proposed was TD170 million. Another 625 restructuring plans are being considered, bringing the total number to 1,270, or 64% of the number to be achieved by 2001.

133. Over time, the program has increased its focus on SMEs. The average size of investments in the *mise à niveau* program declined from TD3 million in 1996 to TD1.9 million in 1999. In addition, the share of enterprises with less than 100 employees rose from 29% of total enterprises participating in the program in 1996, to 66% in 1999.

134. A government survey of a sample of restructuring plans approved between March 1996 and May 1999 showed that 59% of planned investments had already been realized, leading to the expectation that realizations will approach 100% as plans get implemented over time. The survey also showed that export sales of these enterprises have increased by 45%, and their employment by 21%.

Other Programs

135. In addition to the main *mise à niveau* program, other programs in support of the adjustment of Tunisian enterprises to

[39] Enterprises can take advantage of the program more than once if they have promising plans and produce good results.

increased competition are under design or implementation.

Box 3.3: Activities supported by *Mise à Niveau* program and its management

The *mise à niveau de l'environnement* supports the modernization of institutions and infrastructure to improve enterprise competitiveness, through the following activities: upgrading of existing technical centers, industrial and duty-free zones, and training centers, and creating new ones; modernization of information and statistical systems; simplification of administrative procedures; improvement of telecommunications, and of international transport.

The *mise à niveau de l'entreprise* supports approved restructuring plans of off-shore and on-shore enterprises, by providing a premium for investments in three types of activities:

- *Intangible investment*: technical assistance; acquisition and development of software targeting the competitiveness of the enterprise; studies of material investment; professional development, organization of the enterprise, search for partners, plans for quality, and ISO 9000 certification.
- *Fixed investment*: investment in plant; investment in equipment; modernization of technological and technical processes; reconversion of activities; adaptation to the market.
- *Financial restructuring*: reducing the debt load of the enterprise and balancing its financial structure by integrating new sources of financing such as own funds, private placements of shares, and government sponsored investment funds.

The program is managed by the *Comité de Pilotage* (COPIL), which is attached to the Ministry of Industry and is composed of 16 members representing the government (5 members), the employers' association UTICA (5), banks (5), and the labor union UGTT (1). The COPIL is chaired by the Minister of Industry or his designate. Upon request by an enterprise, the COPIL establishes eligibility to participate in the program and approves financing for 70% of the cost of an initial diagnostic study (up to TD30,000) to develop the restructuring plan for the enterprise. These diagnostic studies are usually carried out by private consultants, but can also be carried out by one of eight technical centers established for the main industries.

The enterprise restructuring plan, after approval by the COPIL, is financed by the enterprise itself, financial institutions (at market rates) and the government, through the *Fonds de Développement de la Compétitivité* (FODEC). The contribution of the government takes the form of a premium; this premium varies between 10 and 20% of the total investment envisaged in the restructuring plan, depending on the share of own financing (which earns a premium of 20%) and debt financing (which earns a premium of 10%).

Table 3.6: Status of the *Mise á Niveau* Program

	1996	1997	1998	1999	Jan-Feb 2000	Cumulative Total 1996-2000
Number of firms which joined the program	63	128	168	241	45	645
Investment (in millions of Dinars)	192	262	404.6	304.5	52.6	1,216
Investment premiums	24	37	54	47	8.4	170.4

Source: Ministry of Industry, Tunisia.

136. *Programme d'Assistance aux Entreprises*. Enterprises that are in financial difficulties are excluded from the *mise à niveau* program, but are provided assistance in resolving these problems under the law N° 95-34 of April 17, 1995. The law creates a *Commission de suivi des enterprises économiques* charged to collect information on the activities of enterprises and to provide information to the *President du tribunal de première instance*, who is responsible for administering the bankruptcy law, warning of enterprises in difficulty, and proposing restructuring plans. There is also a *Bureau de l'assistance aux enterprises* whose activities involve three phases of assistance. The first two phases are administrative and try to help enterprises reach an agreement with their creditors to continue their operations and, thus, avoid failure. The third phase is judicial and seeks to help enterprises to get recapitalized after bankruptcy. No financial support is provided for the enterprises, but when they are successfully restructured, they are eligible for support under the *mise à niveau de l'entreprise* program.

137. By the end of 1998, 262 enterprises had applied for assistance. Of these, 170 had been handled including 27 enterprises from the textile, leather and shoe sector, 21 from the agro-food sector, 21 from the mechanical and electrical sector, 15 from oils, 11 from construction materials, ceramics and glass, 11 from construction, and the rest from other sectors. The overall success rate for these enterprises was reported to be 54%. It was estimated that some 10,000 jobs were saved. Most of these jobs were in five large enterprises, two of which were in the textiles sector and two in mechanical and electrical.

138. *Mise à niveau des services*. The government has recently established a *mise à niveau* program for services tied to industry. These include the key services that are important in improving the productivity and competitiveness of the industrial sector. The service *mise à niveau des services* program covers business services, engineering, informatics, training, agricultural consultants. Other important services, such as financial services, telecommunications, electricity, and transportation, are already being upgraded under other programs. The program of *mise à niveau des services* is expected to function like the *mise à niveau* program for manufacturing enterprises, with similar approval procedures and funding from the *Fonds de Développement de la Competitivité* (FODEC).

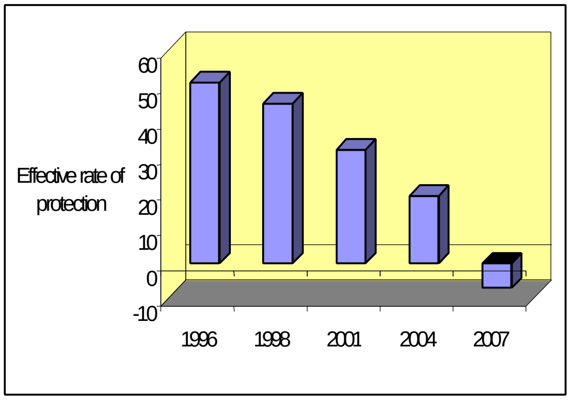
139. *Fonds d'Incitation à l'Innovation dans les Technologies de l'Information (FITI)*. The government created the FITI in February 1999 to support small-scale investments by the private sector in information technologies. The government cofinances up to 49% or a maximum of TD200,000 for information technology projects if the following conditions are met: (a) the project is approved by, and presented to, FITI by a venture capital firm (SICAR), and the SICAR commits to provide at least 30% of the startup capital of the project; (b) the investor provides at least 2% of the startup capital; and (c) FITI's cofinancing is not higher than the share of the SICAR in the startup capital.

D. Challenges Entering the 21st Century

140. The implementation of the Association Agreement with the EU and the elimination of the MFA pose new and difficult challenges for Tunisia as a whole and especially for the private sector. The elimination of import duties on manufactures imported from the EU will dramatically reduce protection of domestic industries and increase competition in the local market (Figure 3.7 and Box 3.4). The phasing out of MFA preferences by 2005 will greatly increase the competition that Tunisian textile exports, which currently

account for over 40% of goods exports, face in the international market. [40]

Figure 3.7: Tunisia: Effective Rate of Protection for Manufactures



Source: Hoeckman and Djankov (1997).

Box 3.4: The Association Agreement with the European Union

Since 1977 Tunisia has benefited from a cooperation agreement with the EU that granted Tunisian manufactured exports duty-free access to EU markets. The 1995 Association Agreement with the EU established reciprocal treatment by granting EU manufactured exports—now three quarters of Tunisia's imports from the EU—duty-free access to Tunisian markets after a 12-year adjustment period. The schedule for the removal of tariffs on manufactures is:

- *Immediately*. For primary materials and equipment not made in Tunisia, representing 12% of manufactured imports from the EU. Fully implemented.
- *Gradually over 5 years*. One fifth per year. For finished products not made locally and certain materials, representing 28% of manufactured imports from the EU. Implementation in progress.
- *Over 12 years*. One twelfth per year. For products produced locally that are capable of competing, representing 30% of manufactured imports from the EU. Implementation in progress.
- *Four-year delay*. One eighth per year thereafter. For products made locally for which the enterprises need restructuring, representing the remaining 30% of manufactured imports from the EU. Implementation to begin in 2000.

Currently in its fifth year of implementation, the agreement has resulted in a temporary but sizable increase in effective protection for most enterprises producing for the domestic market (Figure 3.7), as a result of the full or partial implementation of the first two measures above. The completion of the implementation of the third measure and, most important, the implementation of the last measure will gradually lead to a very large reduction in effective protection for enterprises producing for the domestic market.

40 The MFA had provided Tunisia with preferential access to European textile markets through quotas based on historical shares. Under the new WTO Textiles Agreement, the textile and clothing sectors are being returned to normal GATT disciplines over a 10-year transition ending in 2005. This will subject the Tunisian industry to increased competition in European markets as new low-cost textile and clothing producers are allowed to enter the market or increase their exports.

141. Meeting this competitive challenge will require a deep transformation of the incentives and environment for private sector development to support the adjustment of enterprises. Past performance has been good, but a continuation of previous trends will not be sufficient to achieve the level of growth that is necessary for Tunisia to join the ranks of the OECD. The main reasons for reaching this conclusion are:

- Private investment, both as a share of GDP and total investment, stagnated in the 1990s (Figure 3.2 and Table 3.1 above). Sectoral data are not available to analyze underlying causes, but the private sector seems to have adopted a wait-and-see attitude. The recent rise in imports of equipment as well as survey data on investment intentions[41] suggest however that private investment may soon accelerate.

- The continuing dominance of SMEs in Tunisia and growing complexity in the international markets suggest that Tunisia's industrial policy is likely to serve it less well in the future than it did in the past. The current approach—which implicitly or explicitly relies on picking winners—is in fact biased toward those sectors that performed well in the past and toward larger enterprises within those sectors.

- The experience with trade liberalization in the late 1980s indicates that the response of private investment to the competitiveness shock and associated policy measures was positive, but not as strong as in other countries that had liberalized earlier and more decisively—such as Chile, Korea, and Portugal (Table 3.7).

142. Five main policy directions emerge as priorities for improving prospects for private sector development:

- ➢ Maintain a prudent macroeconomic stance and a flexible management of the exchange rate.

- ➢ Improve labor market outcomes by promoting flexibility and skills development.

- ➢ Improve the cost/quality mix of services for private sector development by introducing competition or at least contestability in infrastructure and services.

- ➢ Deepen the restructuring of the banking sector and make it more responsive to the needs of SMEs.

- ➢ Establish a more consistent and transparent incentives framework to support the establishment and growth of SMEs.

143. The challenges brought about by the implementation of the Association Agreement also represent new opportunities. First, the agreement is already providing all Tunisian producers access to imported investment goods at world prices. As a result, the dichotomy between the onshore and offshore sectors will be greatly diminished, and with it the associated constraints in the expansion of value added and employment in the export sector. Second, when fully implemented, the agreement will inject unprecedented competition in the domestic market and may raise productivity in the industrial sector. Third, if in the future, the agreement is expanded to encompass services, the productivity of industrial enterprises will also benefit from increased access to higher quality and lower cost services.

---

[41] In 1998, investment intentions in manufacturing were reported 18% higher than investment realized one year earlier (see Banque Centrale (1998).

Table 3.7: Response of Private Investment to Trade Liberalization
(Average Private Investment/GDP Ratios, percent)

Country	Reform Period	Pre-reform Period (5-year average)	Reform Period (annual average)	Post-Reform Period (5-year average)	Post-Reform Period to 1995 (annual average)
Chile	1974-81	7.4	10.9	10.3	17.0
Indonesia	1966-72	5.9	6.7	11.5	15.5
Korea	1969-79	20.2	26.0	23.4	28.6
Portugal	1977-80	16.9	17.5	20.4	19.1
Tunisia	1987-90	13.2	10.6	11.6	10.0

Source: Dadush and Murell (1997).

Macroeconomic Management for Private Sector Restructuring

144. As discussed in Chapter 1, signs of a deterioration in the foreign trade balance are already apparent, resulting from an increase in imports and a deceleration in the growth rate of manufactured exports. As imports of equipment and exports of textiles and garments are the items most notably affected, it is likely that the start of the implementation of the Association Agreement and the phasing out of the MFA are direct causes of this deterioration.

145. As a result of these pressures on external balances and the simultaneous stagnation of private investment, policy makers are confronting difficult tradeoffs between macroeconomic objectives and industrial restructuring objectives. While there are no tradeoffs in the long run—as both macroeconomic stability and efficient industrial restructuring are key to growth—in the short term, the industrial restructuring objectives will call for expanding public expenditures for upgrading infrastructure, and expansion of both public expenditures and credit for the implementation of the *mise à niveau* program. This makes it difficult to maintain a tight fiscal stance.

146. Promoting foreign investment by accelerating the privatization program is a very attractive means of improving the short-term trade-offs between macroeconomic stability and restructuring objectives in Tunisia. On the one hand, it would provide revenues for government budget and, thus, facilitate management of macroeconomic balances; on the other, it could promote efficient industrial restructuring by bringing new technical, marketing and managerial knowledge.

147. Flexible management of the exchange rate will continue to be a valuable instrument in the future. In fact, the EU agreement, which amounts to a unilateral reduction in protection, will lead to downward pressures on the exchange rate. While it is unlikely that these pressures can be avoided, they can be mitigated in the short run by foreign investment inflows, and in the medium run by the gains in productivity brought about by higher competition.

Improving Labor Market Outcomes

148. The government has actively managed labor relations, which have been to a large extent institutionalized through collective contracts that are centrally negotiated between the trade unions and the employers associations; within this framework, the government assists the negotiations by playing the role of mediator. This policy has resulted in very limited conflict in the labor market; for example, the total number of layoffs per year has never

reached as much as one half of one percentage of the workforce. Incremental reforms of the Labor Code have been introduced to increase flexibility in labor relations. As a result, in some sectors, fixed-term contracts and sub-contractual arrangements now account for 90% of labor contracts, and layoff procedures have been simplified. However, hiring and, especially, firing processes remain time-consuming and complex.

149. As the economy adjusts to increased competition in domestic and export markets, the growth of more efficient sectors and the decline of less efficient ones will necessarily translate into the creation and destruction of jobs. A more flexible labor market is necessary to reap the benefits of the former and minimize the costs of the latter, and the real challenge will be to achieve this flexibility while preserving good overall labor relations.

150. One predictable consequence of industrial restructuring on the labor market is the intensification of the demand for higher skills. The shift away from agriculture and toward industry and services has been accompanied by a progressive increase in educational achievement of the workforce; this increase in educational achievement has also taken place within each sector of economic activity (Table 3.8). As a result of these trends, the share of workers with secondary or higher education increased from 28% of the workforce in 1989 to 36% in 1994.

Table 3.8: Education Level of Workers by Sector of Economic Activity (1989, 1994)

	Share of Workforce (%)					
	Secondary Education		Higher Education		Secondary or Higher	
	1989	**1994**	**1989**	**1994**	**1989**	**1994**
Agriculture and fisheries	6.0	8.4	0.3	0.5	6.3	9.0
Manufacturing	24.0	29.6	1.9	2.4	25.9	32.1
Food processing	23.9	28.2	1.7	3.0	25.6	31.1
Construction materials	21.1	29.6	2.7	3.9	23.8	33.5
Mechanical and electrical	35.7	40.9	4.3	5.4	40.0	46.3
Chemicals	44.0	49.6	8.4	9.6	52.4	59.2
Textiles and leather	19.5	26.1	0.6	1.2	20.1	27.3
Others	26.5	29.8	1.9	2.0	28.4	31.8
Non Manufacturing	16.7	19.3	1.4	1.8	18.0	21.1
Construction and public works	13.1	15.9	0.6	0.9	13.7	16.8
Market Services	27.2	31.5	3.4	4.7	30.6	36.2
Trade	2.2	31.9	2.2	3.4	27.1	35.3
Transport and communication	5.1	42.5	5.1	6.4	41.6	48.8
Hotels	1.6	40.4	1.6	3.1	31.8	43.5
Financial Services	21.4	57.8	21.4	31.6	86.4	89.4
Other tradable services	0.4	31.6	0.4	9.0	20.9	40.5
Non Market Services	44.0	54.2	15.9	23.6	59.9	77.8
Education, health, administrat.	46.8	54.7	17.2	26.3	64.0	81.1
Other non tradable services	31.5	23.3	10.1	3.2	41.7	26.4
Not declared	25.7	32.3	11.7	7.2	37.5	39.5
Total	23.5	29.0	4.7	6.9	28.1	35.9

Source: INS Employment survey, 1989; Population Census, 1994.

151. Despite this marked shift to a more educated workforce, there remains an important unfinished agenda for education reform (Chapter 4). Two issues are however of particular importance for Tunisia's ability to meet the upcoming competitive challenges: first, the share of workers that cannot read or write remains high, at 24%; and second, the predominantly public education system has been slow in responding to the demand for new skills. As a result, the skill mix of the workforce remains inadequate: as shown in Table 3.9, Tunisia has far fewer students enrolled in engineering, mathematics and computer science—in proportion to tertiary enrollments—than countries such as Korea, Malaysia, and Indonesia.

Table 3.9: Tertiary enrollment by field of study: Tunisia and comparators
(% of total enrollment in tertiary education)

Field	**Tunisia 1996**	Korea 1996	Portugal 1994	Slovenia 1996	Japan 1994	Germany 1995	Indonesia 1995	Algeria 1995	Jordan 1996	Morocco 1994
Engineering	**8.19**	17.86	16.67	19.05	18.25	15.47	12.76	22.97	9.38	0.77
Architecture and Town Planning	**1.00**	1.57	2.11	1.60		2.78	1.40	2.30	2.56	0.16
Mathematics and Computer Sc.	**2.11**	5.82	4.27	0.41		5.34	5.56	7.28	8.49	
Medical Sciences	**8.44**	5.06	5.49	5.98	8.14	10.42	1.94	10.02	10.60	2.97
Natural Science	**11.24**	3.94	3.06	2.10	2.42	6.11	1.09	12.91	4.24	25.95
Agriculture	**0.65**	2.73	3.93	3.82	2.24	2.13	6.62	3.90	2.52	1.06
Transport and Communication	**0.36**	1.52		2.40	0.04	0.00	0.55	0.19		0.21
Trade, Craft and Industr. Planning	**3.31**	0.63				0.40	1.23	0.28		0.67
Commercial and Business Administration	**7.58**	13.45	19.08	30.53		3.05	18.69	1.45	21.13	0.49
Educ. Science and Teacher Training	**1.87**	5.91	11.67	11.29	7.93	5.52	17.15	0.66	11.69	0.10
Mass Communication and Document.	**0.99**	0.89	3.89	2.25		0.69	0.75	1.34	0.23	0.25
Fine and Applied Arts	**1.11**	5.51	1.93	1.63	4.05	2.76	2.67	1.24	2.19	
Home Economics and Domestic Science	**0.00**	2.85	0.12		5.19	0.55		0.00	0.22	
Humanism, Religion and Theology	**22.50**	11.00	6.50	6.07	14.10	12.68	3.74	13.20	15.61	30.33
Law	**11.66**	2.51	7.64	4.69	31.56	5.17	6.57	7.65	5.24	22.06
Social and Behavioral Science	**11.71**	4.50	11.11	4.78		21.03	19.74	14.52	4.37	14.09
Not Specified	**7.30**	13.23	2.53	2.36	4.98	5.77		1.09	1.25	0.71

Source: UNESCO electronic database.

Improving Services for the Competitiveness of the Private Sector

152. Realizing the opportunities brought about by increased competition will depend also on improving the cost/quality mix of services for private sector development, especially transport, telecoms, and business information services. Tunisian firms will increasingly benefit from access to inputs at world prices; but they will be handicapped if the cost of services provided in Tunisia remain significantly higher, and their quality lower, than for competitors.

153. In Tunisia, transport, telecommunications, and business information services are generally recognized—including in the context of the program of *mise à niveau environment*—as limiting the competitiveness of Tunisian enterprises, especially SMEs. Yet measures already identified to improve access, cost and quality of these services, and increase competition in the sectors producing them, largely remain to be implemented.

154. Improving these services will require a dramatic shift in the attitudes of the public sector—away from ownership toward regulation. With regard to the telecoms sector, it remains firmly under the control of the government. In addition, the pace of liberalization foreseen by the WTO agreement on telecoms, signed by Tunisia in 1996, is very slow; many countries—from Chile to Sri Lanka to Ghana—already have implemented their telecoms liberalization agendas to the point where Tunisia wants to be in 2003. For maritime transport, despite initial steps toward liberalization, industry ownership remains dominated by the public sector. The restructuring and privatization of the *Compagnie Tunisienne de Navigation*, the state maritime company, and the *Société Tunisienne d'Acconage et de Manutention*, the state port handling company, have been delayed. Much more rapid liberalization, together with tighter regulation to prevent the formation of cartels, will be needed if the competitiveness of Tunisian exporters is to be markedly improved.

155. Improving business information support services could greatly benefit SMEs, which cannot afford to invest in systematically acquiring information on foreign market opportunities or on better technologies. Nor do they have the incentive to sufficiently invest in acquiring business information due to externalities associated with such investments. Experience from countries like Malaysia or Taiwan (China) shows that these services can play a key role in economic development. In addition, improving private sector performance and especially export performance requires the development of high quality public institutions such as judicial services, enforcement of patents, metrology services, contract and property rights, conflict resolution and arbitration.

Strengthening the Financial Sector

156. Access to, and cost of, funds are reported by private enterprises to be important constraints. This problem has long been recognized by the government, which has directly created a number of special financing mechanisms and also encouraged the development of private venture capital funds. The Tunisian financial system remains, however, characterized by the dominance of the banking system and by a strong government presence within it; public banks represent more than 50% of total bank assets. In addition, despite important progress in liberalizing the financial sector (in 1996 mandatory lending requirements to priority sectors and central bank rediscounting facilities at preferential rates were eliminated) some interest rate restrictions on deposits remain, and the central bank's priority refinancing facilities for certain sectors of the economy (e.g. agriculture) still influence bank credit allocation.

157. The problems that have dominated the financial sector reform agenda in recent

years are the large size of non-performing loans in bank portfolios and the weakness of their capital base. Bad loans as a share of total commitments in Tunisian banks decreased from 36.7% in 1993 to 24.4% in 1999, but remain large compared to other countries (in Morocco non-performing loans represent about 10% of total banks' commitments) and as a share of GDP (8.4% in 1999, though down from 12.7% in 1994).

158. The Tunisian authorities have recently taken steps to restructure the non-performing loans of state owned enterprises, which accounted for about one third of non-performing loans. In addition, the authorities are responding to the problem of non-performing loans of the private sector by establishing a framework for the creation of private loan recovery agencies. A few such agencies have been created during the past few months, and it is still unclear whether this mechanism will prove effective.

159. On the governance side, the government is committed to strengthening the capital base of public banks by mergers of selected development banks with commercial banks, and by privatization. In particular, the government has recently raised the capital adequacy ratio from 5% to 8% as defined by the Basle Committee on banking supervision. In fact, while commercial banks were generally undercapitalized in the early 1990s, in 1998 for the first time the average risk-weighted capital adequacy ratio reached 8% as prescribed by international standards.[42] In addition, the government plans to improve loan recovery and the quality and foreclosure of loan collateral, and raise the threshold of the public sector's share of banks' capital from 34% to 51% for banks to be considered public. The authorities also plan to soon adopt a new bank accounting framework in line with international standards, as well as the establishment of a more reliable and efficient inter-bank payments system.[43] These measures have the potential—when implemented— to improve the services provided to private businesses by increasing both competition among banks and their ability to assume commercial risks. However, bringing the quality and choice of financial services available to private enterprises in Tunisia to the level available to competitors will require a much more radical liberalization of the financial sector, including entry of foreign banks.

Improving the Incentives Framework

160. The industrial policy pursued by Tunisia has long been shaped by two sets of considerations: to encourage employment generation, especially in disadvantaged areas, and to promote competitiveness in the international market. Industrial policy has also been characterized by strong activism, which implicitly or explicitly has involved picking winners, and which has introduced significant often unintended distortions.

161. To meet the twin challenges of the EU agreement and the phasing out of the MFA, industrial policy will need to be more focused on promoting competitiveness as a means to generate sustainable employment opportunities, rather than on immediate job creation or preservation; and on improving the overall environment for the creation and growth of businesses, rather than on restructuring a few enterprises judged to have potential based on past achievements.

---

[42] In Tunisia, until 1999, the minimum risk-weighted capital adequacy ratio was set at 5%, based entirely on tier 1 capital. Although this tier 1 capital requirement is higher than the minimum international norm, the overall minimum capital adequacy ratio was short of minimum international standards (8%).

[43] This will require a performing telecommunications network, the standardization of payment instruments, and legal improvements to create the proper legal foundation for electronic bank payments and to combat possible fraud.

162. Yet, the overall public policy response to these challenges to date can be characterized as more of the same. This may not be a bad policy, in light of past successes as well as in consideration of the fact that public resource allocation is currently not grossly distorted. However, the emphasis placed on the *mise à niveau* of individual enterprises should not be accompanied by benign neglect of the enabling environment—the rules of the game, the implementing institutions, and the basic infrastructure whose *mise à niveau* is critical for the development of new successful enterprises.

163. The investment code provides highly differentiated levels of support across industries and sectors, involves numerous agencies, and interacts with many narrowly targeted initiatives. As a result, it is likely to be implemented in an *ad hoc* fashion, as public officials administering the various programs determine what incentives apply to which investors. In addition, providing tax holidays encourages the establishment of footloose industries that shut down when the tax holidays expire, and results in unequal treatment of enterprises undertaking the same activities when some are benefiting from tax holidays and other have completed them.

164. It is unclear to what extent specific incentives have contributed to attracting foreign direct investment—a source of learning new methods of producing, managing, and selling goods and services, and a key to diversifying exports, modernizing and integrating Tunisia fully in the world economy. FDI has remained below 2% of GDP—except in 1998 when it rose to nearly 4% as a result of the sale of two large cement factories.

165. The *mise à niveau* program provides significant investment premiums to specific enterprises—among those exposed to shocks from the Association Agreement with the EU and the phasing out of the MFA—that are judged to have high potential in the new environment. In this context, it is likely that past performance is being used as an indicator of future success. There are two difficulties in this regard. First, past performance may be a good predictor of future performance at the enterprise level within industries that are already exposed to international competition, such as those in the offshore sector; but this is less likely for enterprises in the onshore sector, which have developed behind high protection. Second, even if targeted industries successfully adjust, they may not be those that will generate the most growth, exports, and employment in the new environment.

166. The Tunisian private sector is still held back by a less than conducive incentives and regulatory framework. While the importance of the competition framework will eventually be diminished by free trade in manufactures with the EU and some Arab states, adequate competition will be key to ensuring strong supply response by the private sector during the adjustment period. Lack of competition can result from a multiplicity of causes, none of them totally foreign to Tunisia. For example, the presence of large enterprises with disproportionate influence on price setting and thus acting as de facto monopolists, public ownership, a history of discretionary public interventions—through procurement contracts, or favorable tax and regulatory treatment—and special connections with the banking sector. Increasing competition in the domestic economy will require (discussed above for the telecoms and transport sectors) a combination of policy actions (such as fast privatization, regulatory reform, anti-monopoly legislation) as well as institutional reform to implement the policy actions (Chapter 2).

Chapter 4. Adapting Poverty Reduction and Social Development Strategies to Changing Economic Conditions

A. Introduction

167. Improving access to basic services and social conditions has historically been a public policy priority in Tunisia. Tunisia has distinguished itself by its success in strengthening social achievements even during economic stabilization and adjustment. Tunisia's emphasis on social development has resulted in dramatic improvements for all social development indicators. According to our estimates, between 1960 and 1990, the incidence of poverty fell from 40% to about 7% of the population.[44] During the same period, the population growth rate declined and life expectancy increased markedly, regional disparities were reduced, and improvements were also achieved in education, access to health care, and basic infrastructure.

168. There are indications that progress in social development during the 1990s has not been as rapid as would have been predicted on the basis of economic growth and past social achievements. On the one hand, health and education indicators continued to improve steadily; on the other, however, neither poverty incidence nor unemployment was reduced. Data in this area are incomplete and preliminary, but the following conclusions can be reached:

- *Poverty incidence has not fallen, and the poor have increased in number between 1990 and 1995.* Between 1990 and 1995 (the most recent year for which household data on consumption are available) per capita GDP growth averaged over 3% —yet poverty incidence hovered around 7%, and the absolute number of the poor increased from about 600,000 to 690,000.[45] The main cause of these developments was a prolonged drought leading to a severe drop in agricultural production over 1993-95, which was most likely accompanied by a deterioration in income inequality (even though partial data on the distribution of household consumption do not indicate increased inequality).

44 Although estimates from the National Statistical Institute show a poverty rate of 6.7% in 1990, the institute's methodology underestimates poverty in rural areas [for more detail, see World Bank (1995)].

45 The National Statistical Institute estimates that in 1995 the incidence of poverty was 6.2%, and the number of people below the poverty line around 550,000.

- *The unemployment rate remains high at about 16%*. Success in job creation—employment grew at an average rate of 3% between 1989 and 1997—has not resulted in a decline in the unemployment rate. According to 1994 census data, the working age population has been growing at a slightly higher rate (3.1%) than employment, and the participation rate has remained approximately constant.

- *There are indications that social tensions may be growing*. Tunisia's ambition to join the ranks of the developed countries early in the next century has generated expectations that achieving a level of social development comparable to that in high-income countries is within reach. At the same time, competitive pressures brought about by globalization and privatization have been accompanied by rising uncertainty about job tenure, changing wage differentials across workers, and reforms of social security.

169. Meeting the expectations of the most rapidly growing segments of society while at the same time reducing the number of the poor and the unemployed will be a difficult challenge for policy makers. Recommendations in this area can only be as preliminary and incomplete as the data on which the analysis is based. The very first recommendation is, thus, to improve household level statistical information by undertaking an in-depth assessment of poverty, inequality, and employment developments. It should be noted that limited data availability is not caused by lack of well managed surveys that collect relevant and comparable information, but rather by a lack of timely exploitation of the data by government agencies or its dissemination within the community of Tunisian and international experts. Additional recommendations include:

➢ *Refocus anti-poverty interventions*. While the stagnation of poverty incidence in Tunisia despite rapid economic growth is disappointing, it is not surprising that reducing poverty becomes harder as progress is made. Accurate targeting of anti-poverty interventions is likely to become more difficult as poverty incidence falls. This implies that the design of targeted anti-poverty interventions becomes more important at lower levels of poverty, as does the value of information necessary for policy formulation.

➢ *Increase labor market flexibility*. The institutionalization of labor relations has resulted in very few labor disputes in the recent past, but at the cost of limiting the ability of public and private firms to restructure. As the economy moves toward closer international integration, the ability of firms to adjust to competitive pressures —including by shedding labor and changing the skill mix of their labor forces—becomes critical to their competitiveness and their ability to create new jobs in the longer run. The government will, thus, need to redirect its role in the labor market to introduce greater flexibility, while at the same time maintaining and consolidating Tunisia's positive record in labor relations and worker conditions.

➢ *Address the social dimensions of increased competition.* As Tunisia deepens its partnership with the EU and becomes more integrated in the world market, opportunities will increase, as will competitive pressures. Better jobs for higher-skill workers will be generated, and at the same time less skilled workers will encounter greater difficulties in finding and retaining jobs. Social tensions are likely to increase in the groups most at risk of a deterioration in their relative—and possibly absolute—economic and social status. Appropriate labor market interventions may be necessary. These interventions will most probably involve improved monitoring of unemployment—including the duration of unemployment—for different types of workers, industries and regions. Policies to deal with redundancies in the public and private sectors will also be needed, as will microfinance programs to support entrepreneurship, and policies to encourage firms to invest in on-the-job training for their workers.

- *Broaden public debate and participation in decision making*. Increased awareness of the challenges facing Tunisia, broader consensus on the corresponding choices, and effective feedback on actual outcomes can significantly improve public policy, and especially the design and implementation of programs for social development.

B. Trends in Poverty Incidence and Inequality

170. The findings presented below are based on information from the 1994 population census, the 1995 household survey, and the 1997 employment survey. The information collected through these instruments is not yet available in a sufficiently disaggregated format to allow for full consistency in intertemporal comparisons and in-depth analysis of trends and their causes. The findings in this chapter are thus *ad interim*; they are nonetheless presented here because they still represent the best available information on Tunisia's achievements in improving the quality of life of the poorest.

Poverty

171. A recent update of social conditions undertaken as background work for this report estimated the national poverty line—defined as the value of a basket of goods which satisfies minimum basic nutritional and non-food consumption needs—at TD258 per year per person in 1995, up from TD196 in 1990. Between 1990 and 1995 the percentage of the population living below this poverty line stagnated at just above 7%; and the number of people living in poverty grew to 690,000 up from 600,000 in 1990 (Table 4.1).

Table 4.1: Poverty Lines and Poverty Incidence, 1990-95

	Year	*Share of Population (%)*	*Poverty Lines (DT/p.c./year)*	*Poverty Incidence (%)*	*Number of poor (in million)*
National	1990	100	196	7,4	0,60
	1995	100	258	7,6	0,69
Large Cities	1990	26.6	248	2,8	0,06
	1995	26.6	310	1.9	0,04
Other Urban	1990	32.9	208	4,0	0,11
	1995	34.6	286	5,0	0,16
Total urban	1990	59.5	218	3,5	0,17
	1995	61.2	290	3,6	0,20
Total rural	1990	40.6	185	13,1	0,43
	1995	38.8	242	13,9	0,49

Note: Poverty lines for total urban and total national correspond to the percentile of the per capita consumption distribution for the aggregated stratum calculated for the aggregate number of poor obtained when using disaggregated poverty.
Source: World Bank staff estimates based on INS Household Consumption Surveys.

172. The stagnation of poverty incidence in the first half of the 1990s is in stark contrast with the gains in poverty reduction achieved in the preceding decades; the incidence of poverty declined from 40% to just over 7% between 1960 and 1990. The

stagnation of poverty during the first half of the 1990s is particularly disappointing in light of the overall positive growth of per capita income during the same period. This outcome is however likely to have been caused, at least in part, by the persistent droughts of 1993-95.

173. The poverty profile of Tunisia did change dramatically in the 1990s. Poverty is more prevalent in rural areas. With less than 40% of the total population, rural areas accounted for more than 70% of the poor in 1995 (Table 4.1). Between 1990 and 1995, the number of poor fell in the larger cities by 20,000, it increased in smaller cities and peri-urban areas by 50,000, and increased in rural areas by 60,000. At least in part, the deterioration of poverty in rural areas was caused by the severe droughts that resulted in a cumulative decline of 23% in agricultural output in real terms between 1993 and 1995. The increase in the poverty incidence in smaller cities and peri-urban areas was mainly caused by an accompanying demographic shift: the share of population in smaller cities and peri-urban areas increased from 33% in 1990 to 35% in 1995, while the share of the population in rural areas decreased from 41 to 39% during the same period.

174. As in all developing countries, poverty is more prevalent in larger households in Tunisia. The average size of poor households is about seven persons in rural areas and six in urban areas compared to the national averages of six and five respectively. Lack of schooling continues to be a major cause of poverty. The average number of years of education of the household head for the lowest expenditure groups is about 4.5 years in both rural and urban areas, compared to 8 to 10 years for the highest expenditure groups. Households whose heads operate in traditional activities seem more likely to remain or to become poor. Between 1990 and 1995, poverty incidence increased in agriculture and fishing and in the construction sectors (where the poor were already very concentrated), and fell in tourism and commercial activities. Finally, substantial disparities exist across regions. The overall incidence of poverty remains the highest in the northwest, and above the national average in the center-west and the south (the incidence of poverty has in fact substantially increased in the south). On the other hand, the incidence of poverty is low and declining in the District of Tunis and in the center-east. The northeast occupies an intermediate position.

175. The Tunisian authorities have recently taken a number of steps to strengthen the fight against poverty, including creating the *Banque Tunisienne de Solidarité*, the *Fonds National de solidarité*, also called program 26-26, which is in the process of being replaced by the *Fonds National de l'Emploi*, or program 21-21. Through these new programs, the authorities want to emphasize the reintegration of the poor into the economic sphere, introduce micro-enterprises, and contribute to employment creation, while maintaining, at the same time, their support to the poorest families.

Inequality

176. The only recent information available to measure inequality in 1995 is on the distribution of consumption expenditures by quintile; neither the Gini coefficient nor the mean consumption by decile for 1995 are available. The available data suggest that relative inequality did not worsen during the 1990-95 period (Table 4.2). The shares of the quintiles and the inter-quintiles intervals (Q5-Q1) show that inequality slightly decreased during that period.

Table 4.2: Percentage Shares of Household Consumption by Quintile

Quintile	1985	1990	1995
1	6.69	7.16	7.79
2	10.68	11.51	12.72
3	15.50	16.56	16.38
4	23.48	24.55	22.58
5	43.65	40.21	40.53
Total	100	100	100
Inter-quintile			
Q5 – Q1	36.96	33.05	32.74
Q4 – Q2	12.80	13.04	9.86
Memo: Consumption per capita (TD per annum)	471	716	1143.7

Source: World Bank staff estimates based on INS Living Standards Surveys.

177. It should however be noted that more disaggregated data may reveal a different picture, and that the data on the distribution by quintile is based on a smaller sample than the data on poverty incidence (3,600 households versus 11,000). Indeed, the near stagnation of the poverty incidence is hardly plausible in the presence of positive economic growth and improving income distribution. The elasticity of poverty to growth was found to be negative in Tunisia as in most countries; therefore positive growth of per capita income over 1990-95 should have resulted in declining poverty, all else being equal.[46] This did not happen, however. The inequality of income distribution is, thus, likely to have increased during that period. Income equality may have deteriorated between 1990 and 1995, as the severe drop in agricultural incomes is likely to have reduced the incomes of poor households and of households around the poverty line significantly more than the incomes of other households, which rely more on non-agricultural sources of income.

C. Labor Market Developments

178. Data from the 1989 and 1994 censuses and the 1997 employment survey show robust growth in employment opportunities in Tunisia, averaging 3% a year (Table 4.3). This record of employment generation is very encouraging, especially in comparison with the previous five-year period, when employment grew at 2% on average. Job creation, however, slowed during the most recent years, averaging 2.6% between 1994 and 1997. The implied income elasticity of employment was also significantly lower, at 0.51 for 1994-97, compared to 0.63 for 1989-94. Throughout the period, female employment grew more rapidly than male employment, reducing the unemployment rate for female workers.

---

[46] Van Eeghen (1995).

Table 4.3: Employment Trends by Gender: 1984-1997

	Number (thousands)				Average Annual Growth Rate			
Total:	**1984**	**1989**	**1994**	**1997**	**1984-89**	**1989-94**	**1994-97**	**1989-97**
Employed (15+)	1786.4	1978.5	2320.6	2503.6	2.1%	3.2%	2.6%	3.0%
Unemployed (18-59)	245.2	316.6	378.4	416.2	5.2%	3.6%	3.2%	3.5%
Non employed (15-17 and 60+)	105.5	65.2	73.4	58.6	-9.2%	2.4%	-7.2%	-1.3%
Total Actives	2137.2	2360.6	2772.4	2978.3	2.0%	3.3%	2.4%	2.9%
Population (15+)	4210	4907.2	5727.4	n.a.	3.1%	3.1%	n.a.	
Participation Rate	50.8%	48.1%	48.4%	n.a.				
Unemployment Rate	16.4%	16.2%	16.3%	15.9%				
First Time Job Seekers (18-59)	52.9	135.2	73.39	n.a.	20.6%	-11.5%	n.a.	
Male:	**1984**	**1989**	**1994**	**1997**	**1984-89**	**1989-94**	**1994-97**	**1989-97**
Employed (15+)	1398.2	1592.8	1785.7	1906.4	2.6%	2.3%	2.2%	2.3%
Unemployed (18-59)	199.8	226.6	279.6	307.4	2.5%	4.3%	3.2%	3.9%
Non employed (15-17 and 60+)	83.6	46.9	53.9	41.9	-10.9%	2.8%	-8.1%	-1.4%
Total Actives	1681.7	1866.3	2119.2	2255.7	2.1%	2.6%	2.1%	2.4%
Population (15+)	2127.5	2476.2	2873.3	n.a.	3.1%	3.0%	n.a.	
Participation Rate	79.0%	75.4%	73.8%	n.a.				
Unemployment Rate	16.9%	14.7%	15.7%	15.5%				
First Time Job Seekers (18-59)	39.1	82.6	41.9	n.a.	16.1%	-12.7%	n.a.	
Female:	**1984**	**1989**	**1994**	**1997**	**1984-89**	**1989-94**	**1994-97**	**1989-97**
Employed (15+)	388.2	386	534.9	597.2	-0.1%	6.7%	3.7%	5.6%
Unemployed (18-59)	45.4	90	98.8	108.8	14.7%	1.9%	3.3%	2.4%
Non employed (15-17 and 60+)	21.9	18.3	19.4	16.6	-3.5%	1.2%	-5.1%	-1.2%
Total Actives	455.5	494.3	653.1	722.6	1.6%	5.7%	3.4%	4.9%
Population (15+)	2082.4	2433.3	2854.1	n.a.	3.2%	3.2%	n.a.	
Participation Rate	21.9%	20.3%	22.9%	n.a.				
Unemployment Rate	14.8%	21.9%	18.1%	17.4%				
First Time Job Seekers (18-59)	13.8	52.6	31.5	n.a.	30.7%	-9.7%	n.a.	

Source: Recensement général de la population de l'habitat, 1984; Enquête nationale population-emploi, 1989; Recensement général de la population de l'habitat, 1994; Enquête nationale population-emploi, 1997; Institut national de la statistique, Tunis.

179. Recent labor market studies also reveal that job creation has been faster in urban areas, employment opportunities have been shifting toward higher skills, value added per worker is rising, and non-salaried jobs are increasing for men.

180. The workforce is becoming more educated. In 1994, about 36% of the workforce had secondary or higher education, compared to 28% in 1989, and 24% in 1984. Nonetheless, 24% of the workforce is still unable to read or write (mainly concentrated in agricultural and construction activities). Over 1989-94 the sectors with the largest annual growth rates were also those with above average improvements in the education levels of their workers. As it gets more educated, the Tunisian workforce is becoming more productive. Value-added per worker increased by 17% over 1989-97, with the largest increase coming from financial services (Table 4.4).

Table 4.4: Value Added per Worker (1989, 1994, and 1997)

Sector	Employed (thousands)			Value Added 1990 TD millions			Value Added/Worker 1990 TD hundreds		
	1989	**1994**	**1997**	**1989**	**1994**	**1997**	**1989**	**1994**	**1997**
Agriculture and fisheries	509.7	501.0	546.2	1277.0	1742.7	2094.9	2.5	3.5	3.8
Manufacturing	382.7	455.7	506.5	1925.8	2688.0	3110.3	5.0	5.9	6.1
Textiles and leather	191.2	239.9	259.2	495.9	791.1	917.4	2.6	3.3	3.5
Others	57.4	68.2	77.9	228.3	321.9	375.8	4.0	4.7	4.8
Non-Manufacturing	282.8	342.5	337.7	1633.2	1856.7	2052.5	5.8	5.4	6.1
Construction and public works	247.6	305.8	304.8	435.6	635.5	727.3	1.8	2.1	2.4
Market Services	374.7	509.7	579.1	3353.7	4275.2	5093.3	9.0	8.4	8.8
Trade	168.9	217.9	260.5	756.6	975.5	1098.3	4.5	4.5	4.2
Transport and communication	95.8	112.0	122.7	765.7	958.4	1211.1	8.0	8.6	9.9
Hotels and restaurants	49.1	75.7	83.8	588.3	690.8	786.5	12.0	9.1	9.4
Financial Services	15.4	22.0	24.8	323.6	576.1	745.7	21.0	26.2	30.1
Real estate, repairs and consultant services	45.5	82.0	87.4	919.4	1089.5	1251.6	20.2	13.3	14.3
Non-Market Services	429.5	511.7	534.1	1370.9	1722.1	1970.2	3.2	3.4	3.7
Total	1978.8	2320.6	2503.6	9283.4	11853.0	13786.0	4.7	5.1	5.5

Source: Enquête nationale population-emploi, 1989; Recensement général de la population de l'habitat, 1994; Enquête nationale population-emploi, 1997; National Accounts; Institut national de la statistique, Tunis.

181. While salaried jobs have always been prevalent in Tunisia (66% in 1989 and 71% in 1994), in 1997 the share of salaried occupations dropped. This overall drop hides gender differences, with men moving away from salaried jobs to become employers and family workers, and women moving away from participation in family work toward professional occupations.

182. Although increasing each year, the number of workers laid off due to privatization and restructuring of public and private sector enterprises remains small and has had a negligible impact on labor market developments. In 1996 3,900 workers were laid-off, in 1997 6,002, and in 1998 5,100. Public sector retrenchment was responsible for 2,000 layoffs a year during that period.

183. Over 1989-94 the share of wages in value added remained constant (at about 39 to 40%). However, at the sectoral level, the wage bill in manufacturing declined from 40% to 34% of value added, while salaried jobs increased from 255,000 to 350,000, accompanied by a reduction in compensation per worker (Table 4.5). The wage bill as a proportion of value added fell also in the marketable services sector.

184. Average compensation per salaried worker increased by an average of 0.2% in real terms between 1989 and 1994.[47] This compares favorably with the region, where wages fell during the 1990s.[48]

185. Wage movements at the bottom of the pay scale were contained over 1989-97 as real minimum wages for agriculture and industry remained relatively constant. Between 1989 and 1994 industrial minimum wages fell by 1% overall, and daily wages for agriculture sector laborers increased by 2% overall. These variations are minor and confirm government's policy of maintaining the real value of minimum wages.

186. Formal institutions are fairly developed in Tunisia for every aspect of the relationships between workers and employers. Labor market negotiations are governed by an extensive set of rules contained in the Labor Code and in various *Conventions Collectives*, which are negotiated by tripartite committees every three years with the aim of avoiding industrial conflicts.[49] They determine, among other things, the level of the wages and salaries, and their growth for the next three years. This policy has succeeded in recent years in making labor disputes very rare, and has been an asset in attracting investments. However, the institutionalization of labor relations and the high premium placed on social stability have hampered flexibility in the labor market. To increase the flexibility of labor regulations, the Labor Code was revised in 1994 and again in 1996 to clarify the conditions under which workers can be laid off for economic reasons and establish guidelines for financial compensation.

187. Despite recent progress, government's role is still important and the number of layoffs is still controlled for both private and public enterprises. Despite the recent reform of the Labor Code, the time required to obtain a retrenchment for economic reasons remains long in practice, hampering necessary restructuring.[50] As Tunisia deepens its partnership with the EU and becomes more integrated in the world market, opportunities will increase, as well as competitive pressures. Better jobs for higher-skill workers will be generated, and at the same time less skilled workers will encounter greater difficulties finding and retaining jobs. The role of the government in the labor market needs to change from exerting direct intervention to providing appropriate regulation. This new role will likely include: improved monitoring of unemployment—including the duration of unemployment—for different types of workers, policies to deal with redundancies in the public and private sectors while ensuring their coherence with existing programs (public works, training programs, etc.), microfinance programs to support entrepreneurship, policies to encourage firms to invest in on-the-job training for their workers, and measures to improve information for job suppliers and job providers.

47 As data on wages were not available at the time of the report's preparation, the evolution of the average compensation per worker was taken as an indicator of the evolution of wages.

48 World Bank (2000c).

49 The committees include representatives of the government (acting as facilitators), the employers' association UTICA and the labor union (UGTT).

50 Given the duration of unemployment for those who lose their jobs (about 13 months) and the average wages in the economy, severance packages, particularly for the public enterprises, seem too generous. Public sector severance packages ranged between TD10,000 and TD15,000 per worker, and private sector packages ranged from TD5,000 to TD10,000.

Table 4.5: Wage Bill by Sector (1989 and 1994)

Sector	Salaried Jobs (thousands)		Wage Bill (1994 TD millions)		Average Compensation (1994 TD per annum)		Average Growth Rate (per annum)
	1989	**1994**	**1989**	**1994**	**1989**	**1994**	**1989-94**
Agriculture and fisheries	182.2	194.6	147.8	208	81	107	5.7%
Manufacturing	254.5	349.8	940.3	1165.9	369	333	-2.0%
Non-Manufacturing	259.5	302.3	581.6	786.7	224	260	3.0%
Construction and public works	225	266	361.7	550.9	161	207	5.2%
Market Services	174.2	260.5	1160.4	1480.5	666	568	-3.1%
Non-Market Services	398.4	502.3	1724.1	2191.1	433	436	0.2%
Total	**1284.4**	**1627.9**	**4554.5**	**5832.2**	**355**	**358**	**0.2%**

Source: Enquête nationale population-emploi, 1989; Recensement général de la population de l'habitat, 1994; Enquête nationale population-emploi; National Accounts; Institut national de la statistique, Tunis.

D. Basic Education, Health Care, and Social Security

188. Tunisia's commitment to promoting social development has resulted in sizable public expenditures in the social sectors since the mid-1980s. Overall stability in total public social expenditures as a share of GDP has been accompanied by declining outlays for consumer food subsidies and an increase in social security (Table 4.6). Cost recovery has increased gradually, especially in health, which is likely to have led to increased private expenditures for these services.

Table 4.6: Public Spending in Social Sectors, 1986 and 1997

Sector	1986		1997	
	TD Mil	% GDP	TD Mil	% GDP
Education	476.3	6.7%	1 444.6	6.9%
Primary & Secondary	346.4	4.8%	1 048.3	5.0%
Higher Education	87.0	1.2%	266.5	1.3%
Vocational Training	2.9	0.6%	129.8	0.6%
Public Health	163.1	2.3%	472.7	2.3%
Consumer Food Subsidies (Caisse Générale de Compensation)	218.0	3.0%	370.0	1.8%
Social Security	255.8	3.6%	1 008.5	4.8%
Other Social Programs	216.6	3.0%	727.3	3.5%
Total Social Sectors	**1 329.8**	**18.6%**	**4 023.1**	**19.2%**

Source: Government of Tunisia.

189. This sustained emphasis on social development has continued to result in improved quality of life for the population. Table 4.7 summarizes the main achievements in comparison with the average for middle-income developing countries.

Table 4.7: Social and Economic Indicators of Development, Selected Years, 1975-98

Indicator	1975	1984	1987	1990	1994	1995	1996	1997	1998	Lower-Middle Income Countr. 1998 or latest year	Middle-Income Countr. 1998 or latest year
Income and population											
GNP per capita (current US$)	770	1,180	1,270	1,430	1,740	1,820	2,000	2,080	2,060	1,740	2,960
Population (in millions)	5.6	7.0	7.7	8.1	8.8	9.0	9.1	9.2	9,3	88.6	1,474.4
Population growth rate(%)	2.3	2.58	2.19	1.76	1.70	1.50	1.42	1.37	1.30	1.11	1.20
Urban population (% of total)	49.9	53.34	55.44	57.9	61.1	61.9	62.62	63.34	64.1	57.7	65.2
Health											
Life expectancy at birth	58.6	67.1	67.8	69	71.2	71.4	71.5	71.9	72	68.3	69.2
Female/Male difference	1.5	2.1	2.1	2.5	3.7	3.8	4	3.7	3.7	6.1	6.3
Maternal mortality rate (p. 100.000)		1,000		127	68.9						
Infant mortality rate (per thousand live births)	76.9	51.4	49	40.5	32.6	30.5	30.5	28.9	28.1	35.3	31.5
Total Fertility Rate (births per woman)		4.6	3.9	3.5	2.9	2.7	2.5	2.4	2.2	2.5	2.4
Contraceptive prevalence (% of women 15-49)			48		59.7	60	65			52.9	52.9
Population per physician	5,900	3,694	2,334	1,866	1,454	1,417	1,460	1,440			2,020
Populat. Per hospital beds	400	470	472	516	555	567	580	588			
Child malnutrition (% Stunting < 2 SD)	39.5		17.9				10.3				
Immunization (% of children under 12 mos)											
DPT		61	75	91	91	92	91	96		89 (96)	86.(97)
Measles		55	74	88	87	91	86	92		89 (96)	90 (97)
Education											
Adult illiteracy (% of 15+)	63.8	48.8	44.7	40.9	36.3	35.3	33.9	32.6	31.3	14.7	12.9
Female	77.1	62.3	57.9	53.5	47.9	46.7	45	43.5	42.1	17.8	15.6
Primary net enrollment rate		91.8	93.6	93.5	97.9	97.8	97.6				92.9 (96)
Male		98.5	98.8	97.2	100.4	100	99.3				
Female		84.7	88	89.6	95.4	95.4	95.7				
Urban	77.6	87.4			92.2						
Rural	41.9	64.9			77.8						
Pupil-teacher ratio (primary)	40	34	30.9	27.8	25.2	24.5	24.1				24 (96)
Secondary Gross enrollment rate, total (%)	21.1	36.1	39.9	44.9	56.8	60.4	64.6	64.3		67.4 (95)	66.1 (96)
Female	14.6	29.3	33.8	39.5	54.1	58.3	63.2	62.9		71.(92)	61 (96)

Note: For some indicators, data for 1970 and 1985 are used for the years 1975 and 1987 respectively.
Source: World Bank, World Development Indicators and Live Bata base.

Primary education and vocational training

190. Education has been one of the most important areas of progress in Tunisia over the past few decades. Achievements in education have not only helped reduce poverty, but have also created an increasingly educated and productive workforce. Primary education has almost universal coverage now, and there is very little difference in enrollment rates between boys and girls. Although disparities in enrollment rates continue to persist between urban and rural areas, the rural-urban gap has decreased from 35.7 to 14.3 percentage points between 1975 and 1994.

191. These results have been achieved thanks to a reform effort on the part of the Tunisian authorities.

- In July 1989 the authorities launched a major reform of the education system that increased the basic education cycle to nine years and introduced free and compulsory education until the age of 16.[51] The reform also aimed at reducing school dropouts (especially in the first cycle of basic education). At the same time, the authorities increased their efforts to recruit qualified teachers. As a result, the percentage of teachers with higher degrees rose from 67% to 78% in five years.

- The government has embarked on other large-scale activities in this area, such as the computerization of schools and an overall assessment of the basic education system.

192. As a result of these measures, dropout rates have decreased steadily. For example, for grades 1 to 6, about 48,000 pupils dropped out of school in 1996/97, compared to 97,000 in 1989/90. Moreover, these reforms have improved promotion rates in basic education and between basic education and secondary education. More specifically, the promotion rate between the first and second cycle of basic education has risen from 38.6% in 1986/87 to 68.5% in 1998/99. Nonetheless, the general progress of the education system over the long term hides the recent reversal of this trend: while promotion rates have remained stable over the last five years, repetition rates have slightly increased.

193. The picture changes slightly, however, once we consider the effects of the reforms in combination with the recent evolution of the population structure particularly in the upper cycle of basic education. Lower birth rates have recently decreased the number of children that begin school, which, together with the improvement of the promotion rate, has reduced the number of pupils in the first cycle of basic education (1.4 million in 1998/99). By contrast, in the second cycle of basic education, the number of pupils has increased at an average rate of 6.3% a year since 1986/87, and reached 874,814 in 1998/99.

194. While it is reassuring that the fall in the number of pupils per class in the first cycle of basic education has reduced the need for new schools, implementing the reforms remains of critical importance. First, there is an increasing need to rehabilitate and maintain existing schools, and for upgrading schools to new standards, such as inclusion of multipurpose rooms, computer laboratories, and upgraded schools reference libraries. Second, the next wave of reform of basic education will have to emphasize excellence for all instead of for the few, and ensure that all children who enter each cycle of education complete it satisfactorily, with an adequate level of quality. In turn, this will increase the productivity of the labor force

[51] The reform introduced a 9-year basic education cycle. The first cohort of students enrolled in this new system reached their 9th grade examinations in June 1998 and those who passed entered the first year of the four-year secondary cycle in September 1998. It is still to early to assess the effectiveness of the new system.

and provide more equal access to economic opportunities.

195. In general, the basic education system should be reformed so that first-time job seekers and today's workers are better equipped for a job market characterized by quickly changing technologies and high labor mobility. Two levels of intervention for future reform can be considered:

- *System-wide reforms*. These structural reforms should include introducing an evaluation and remediation system to improve performance at all levels of education (teacher, school, student achievement, and learning materials), increasing responsibility and accountability for different school-level actors and considering the decentralization of decision making to the local level, and supporting research at all levels of the system.

- *School-level intervention*. This should include introducing new methods of teaching and adapting the pedagogy and curricula to a changing economic environment, using new technologies (computers) as learning tools, increasing access while maintaining existing infrastructure, particularly at the primary level, and upgrading teaching quality by recruiting larger numbers of qualified teachers and improving teacher training and conditions of service.

196. The Tunisian authorities are also placing increasing emphasis on vocational training, which fulfills the double objective of educating and preparing workers for a modern job market. There are several institutions dedicated to vocational training, ranging from technical centers to newly established professional centers. Recently, the authorities have created a program to rehabilitate vocational training and employment, called *MANFORME (Mise à Niveau de la Formation Professionnelle et de l'Emploi)*, which goes hand in hand with the enterprise *mise à niveau* program. *MANFORME* covers 1996-2002 and aims to make vocational training more useful for enterprises and to link it to a nation-wide employment creation strategy. The program is being implemented in collaboration with vocational training institutions and the Ministry of Vocational Training and Employment. Moreover, the program introduces specific agreements between the vocational training institutions and the Ministry of Vocational Training and Employment, and it is run by a committee of representatives from both sides. In the near future, the authorities should consider how to involve private employers in vocational training to better match skills demand and supply.

Health Care

197. The health status of the Tunisian population continues to improve with the development of both preventive and curative health care services and the decline in birthrates (Table 4.7 above). Indicators of life expectancy, infant mortality, reproductive health, and malnutrition have also continued to improve. Tunisia has achieved better health indicators than the average for lower-middle-income, and even better than middle-income countries as a whole.

198. Despite progress, however, problems remain. Although, overall, rural areas are well covered in terms of basic care and suffer no shortcomings compared to urban areas, considerable disparities persist between east and west with regard to health status and the utilization of health services. Moreover, aging population and the needs and expectations of an increasingly urban and educated population are generating new pressures. Weaknesses in the service delivery system also persist, despite important achievements.

199. Over the past three decades Tunisia has developed a health care system that covers almost all the population and compares favorably with that of other middle-income developing countries. The public sector is the main provider of health

care services, supplying about 90% of all hospital beds and over 55% of medical staff. In 1998, public sector health care expenditures represented 35.4% of total health expenditures, with compulsory health insurance funds accounting for 17.2%, and households financing directly the remaining 47.4% (Table 4.8). The private sector is expanding rapidly: its bed capacity has doubled in the last five years and the outpatient visits are almost equal in number to those in the public sector. Although private sector facilities are mainly concentrated in urban areas, in some under-served areas there are interesting partnerships between the private providers and the public hospitals.

Table 4.8: Evolution of health expenditures per person and per source in dinars, 1985-98

	1985	1990	1995	1996	1997	1998
Health expenditures per person	39	71.5	104.7	112.4	121.3	134.3
O/w Households	13.5	33.5	49.4	53.7	58.5	63.6
Percentage of total	34.6%	46.9%	47.2%	47.8%	48.2%	47.4%
Compulsory health Insurance funds	5.8	10.6	16.3	16.8	20.5	23.1
Percentage of total	14.9%	14.8%	15.6%	14.9%	16.9%	17.2%
State	19.7	27.4	39	41.9	42.3	47.6
Percentage of total	50.5%	38.3%	37.2%	37.3%	34.9%	35.4%

Source: Ministère des Affaires Sociales, Tunis.

200. Access to basic health care is available to almost all the population regardless of income. The state provides free or subsidized health care to the lowest income groups through two public schemes. The *Assistance Médicale Gratuite, Type I* (AMG I) covers about 117,000 families classified as needy; and the *Assistance Médicale Gratuite, Type II* (AMG II) provides health care on the basis of a passbook (*carnet d'indigence*) issued for a small annual fee that allows the holder to pay reduced fees (*ticket modérateur*) averaging about 20% of the tariffs for medical services**,** with a ceiling of TD 30.[52]

201. Access to AMG II is very easy and gives a strong incentive to evade social security affiliation, particularly for the self employed, thus constituting a major budgetary drain for public health care. At present, roughly 700,000 families, or about 40% of the population, benefit from AMG II, which brings to over 800,000 the number of households (representing 50% of the population) benefiting from free or heavily subsidized health care. Although according to the law only the poor are eligible for these programs, the subsidized heath care schemes are available to many who are not really poor. Although tariffs have almost tripled for all services over 1991-98, user fees in public health structures cover only about 50% of the cost.

202. Since the early 1990s the government has successfully pursued a number of policies to improve the health status of the population further.[53] A key component of these reforms is the recent modification of the allocation terms for passbooks. This aims to ensure the free provision of health care for families classified as needy by the Ministry of Social

52 Following the circular MSP/26/DTH of March 30, 1998.

53 Government policy since early 1990s has focused on improving efficiency of health care services, better controlling the costing system, strengthening service delivery, improving control of pharmaceuticals products, and improving the financing mechanisms of health care services.

Affairs, and reduced fees (*ticket modérateur*) for other individuals who are not affiliated with any of the social security funds. The reform of the conditions for allocating passbooks was complemented by the creation of a poverty database at the Ministry of Social Affairs. Among other things, this database will help target access to passbooks more effectively (Box 4.1).

Box 4.1: Recent reforms to improve the targeting of poverty reduction with respect to health care

As part of the general effort to improve the use of health resources and the quality of health care, the Tunisian authorities reformed the terms for the allocation of passbooks (*carnets d'indigence*) through two decrees in 1998:

- **AMG I.** Decree 98-1812 established new terms for the allocation and withdrawal of passbooks (AMG I). The decree specified that free health care applies to those families that benefit from, or are eligible for, permanent aid programs; namely, the National Aid Program for Needy Families (*Programme National d'Aide aux Familles Nécessiteuses*), the National Aid Program for handicapped people unable to work (*Programme d'aide des handicapés incapables de travailler)*, and the Aid Program for needy old people lacking family support *(Programme d'aide aux personnes âgées nécessiteuses sans soutien familial)*.

- **AMG II.** Decree 98-409 determined which categories of people can benefit from reduced fees for health care and hospitalization in public health institutions. The decree also established the terms under which the AMG II passbooks are granted: namely, on the basis of annual family income adjusted for family size. The identification of beneficiaries is carried out in collaboration with the social security funds at the local and regional level. Moreover, the supervisory responsibility for the system has been transferred from the Ministry of Public Health to the Ministry of Social Affairs.

In addition, the Ministry of Social Affairs has recently created a database on the beneficiaries of social programs in order to better target government's interventions.

Source: Ministère des Affaires Sociales.

203. Although basic health services are available to almost all of the population, Tunisia's health care, and public health care particularly, face a serious challenge: to provide more and better quality basic health care services while relying less extensively on public resources. This means improving the equity and efficiency of operations, reexamining the financial burden sharing arrangements to reduce government financial responsibilities, and concentrating public resources on the poorest segments of the population.

204. To continue improving the quality, efficiency and equity of the health care system, the government will need to consider several specific key actions:

- Upgrade and define basic specialties in regional hospitals to enable them to utilize available resources more effectively.

- Redefine the role of the central and regional authorities and their links with health care providers (private and public sectors).

- Strengthen the management autonomy of public facilities.

- Reform the health insurance system, which will increase the integration of the private sector in the health system, make health care financially more accessible and regulate private providers.

- Establish a national health information system to monitor and evaluate the resources, activities, costs, quality, results and performance records of both the public and private health sectors.

The Social Security System

205. As part of its long history of emphasizing the social aspects of development, Tunisia has developed a comprehensive contributive social security system managed by the social security funds: the *Caisse Nationale de Sécurité Sociale* (CNSS) for private sector workers, and the *Caisse Nationale de Retraite et de Prévoyance Sociale* (CNRPS) for public sector workers. The system is mandatory and covers urban wage earners, the agriculture workers, and the self-employed. It provides benefits to both private and public sector workers including retirement, disability and survivor pensions, health care, and family benefits.

206. The coverage of the social security system has increased substantially in the last decade. In 1997, the system covered about 2 million people (active and retired), twice the number it covered in 1987. The coverage ratio of the active population increased from 55% in 1987 to 81% in 1997 (table 4.9).

Table 4.9: Percentage of workers covered by the Social Security System (in %)

	1987	1997
Total private sector (Affiliates to the CNSS)	41.6	74.6
Non-agricultural formal workers	66.3	94.0
Agriculture workers	16.9	41.7
Self-employed	9.2	48.5
Total public sector (Affiliates to the CNRPS)	100	100
Total covered eligible affiliates	**54.6**	**80.7**

Source: Ministry of Social Affairs.

207. *Pension System.* Pension is the most important component of the social security system. The formula for calculating benefits is generous, which jeopardizes the financial sustainability of the system in the long run. Replacement rates are extremely high and unsustainable in the long run. The maximum replacement (pension) rate is 90% of gross pensionable salary for the public sector and 80% for the private sector. The minimum length of service required to be entitled to a pension is also low by international standards. In Tunisia, on average, a contributor can retire after only 10 years (in the private sector) or 15 years (in the public sector) of contribution, provided he or she is 60 years old. The equivalent waiting period is 18 years on average in OECD countries and 25 years in East European countries. Moreover, in Tunisia, early retirement is available at age 50.[54]

208. Since 1994 the Tunisian authorities have taken steps to contain the deterioration of the finances of the social security system. Reform measures taken so far include improving investment performance (in 1997, over 60% of the reserves of social security funds were invested in the money market, compared to 13% in 1987). They have also rationalized the benefit formula (since 1996, the pensionable salary in the private sector has been calculated on the basis of average salary during the last ten years of service instead of the last three years). Financial sustainability has been improved—contribution rates paid by workers into the private fund were raised by 1.5 % between July 1994 and July 1996 to compensate, at

54 Since 1994, the authorities have restricted eligibility to early retirement in the public sector.

least partially, for the 2% reduction in the contributions paid by employers.[55] Social security schemes and benefits have been harmonized, and evasion reduced by narrowing the income categories on which income declarations for the self-employed are based and the choice of income categories narrowed to the highest ranges for some professions such as physicians. The links between benefits and contributions have been tightened And a reform of the workers' health insurance system has been initiated (Box 4.2).

209. These steps are gradual and mainly constitute short-term measures that address the immediate financial sustainability of the system. To prepare deeper reforms of the social security system, a social security research center was created in 1998 under the Ministry of Social Affairs. Its main responsibility is to create a social security database and prepare a more fundamental reform of the system. Further reform measures could include the creation of a multi-pillar scheme—a public scheme operating on a pay-as-you-go basis and offering basic pension benefits and a mandatory savings scheme based on individual capitalization accounts. Given the political economy of social security reform, in the context of a radical reform, it is also crucial that at an early stage the authorities inform the public, generate political consensus, and spell out key details of the reform.

Box 4.2: Outline of the workers' health insurance reform

In 1996 the Tunisian authorities designed a major reform of the health insurance system to satisfy the health coverage needs of the insured, while ensuring the financial viability of the health insurance system. The reform's major objectives are:

- To better integrate and coordinate existing health insurance systems in order to develop a unified basic and compulsory system that is to cover all sectors and guarantee sufficient coverage against the risk of illness;
- To gradually separate the bodies in charge of financing health care and those in charge of providing health care services;
- To maintain an optional complementary system in addition to the basic one, while, at the same time, avoiding double coverage. Social security funds and insurance companies will be in charge of providing the complementary insurance plan;
- To structure the relationship between public sector hospitals and social security funds in such a way that in a first phase, public hospitals would be reimbursed by insurance funds on the basis of bills after health care services have been provided to their members, and in a later stage, insurance funds would pay hospitals directly at real cost as and when health care services are provided;
- To rationalize the relations between social security funds and private health care services to enhance the private sector's role in the provision of health care;
- To manage health expenditures by clearly defining the responsibilities of the different parties as well as their respective contribution to the reduction of overall costs; where the parties are taken to include public health structures, private doctors and clinics, as well as patients.

Source: Ministère des Affaires Sociales.

55 The decrease in employers' contributions to private funds was introduced in 1996 to help Tunisian enterprises face international competition.

Reference List

Baccouche, Rafik, Rached Bouazizet, and Mohamed Goaied (1997), *"Croissance Potentielle et Fluctuations Conjoncturelles en Tunisie"*, *Economie Internationale, No. 69, premier trismestre 1997.*

Banque Centrale de Tunisie (1998), *Périodique de Conjoncture* No. 19, October 1998.

Bosworth, Barry, Susan Collins and Yu-chin Chen (1995) *"Accounting for Differences in Economic Growth*", in *Brookings discussion papers in international economics*, No. 115 : [1-63], 1995.

Bruno, Michael, Martin Ravallion and Lyn Squire (1996),*"Equity and Growth in Developing Countries: Old and New Perspectives on the Policy Issues"*, Policy Research Working Paper # 1563, World Bank, 1996.

Dadush, Uri and Kim Murell (1997), *"Trade Liberalization and Private Investment: The case of Tunisia"*, World Bank.

Freund, Caroline and John McLaren (1999), "*On the Dynamics of Trade Diversion: Evidence from Four Trade Blocs*", Mimeo Federal Reserve Board, Washington, DC, and Columbia University, New York.

Haddad, Afef (1999), *"Tunisia: Export Potentials in the Services Sector"* April 1999. Background Paper for the Social and Structural Review.

Hoekman, Bernard and Simeon Djankov (1997), "Towards a Free Trade Agreement With the EU: Issues and Policy Options for Egypt." The Egyptian Center for Economic Studies Working Paper No. 10. Cairo.

International Monetary Fund (1995), "*Guidelines for Fiscal Adjustment*" Pamphlet Series No. 49; Washington DC.

Jbili, Abdelali, and Klaus Enders (1996), "*The Association Agreement Between Tunisia and the European Union"*, Finance and Development, September 1996.

Kouamé, Auguste T. (1999), "*Achieving Faster Growth in Tunisia*", World Bank, Middle East and North Africa Region, May 1999. Background Paper for the Social and Structural Review.

Mohammed, Nadir A. (1999), "Tunisia's Fiscal Sustainability and Contingent Liabilities", World Bank, Middle East and North Africa Region, May 1999. Background Paper for the Social and Structural Review.

Ministère du Développement Economique (1996), *"Pour que la Tunisie Accède au Rang de Pays Développé"*, Travaux Préparatoires du IXème Plan, Ministère du Développement Economique, Tunis, June 1996.

Ministère du Développement Economique (1997), "Le Neuvième Plan en Bref 1997-2001" Tunis, novembre 1997.

Pack, Howard and Kamal Saggi (1998), "*Exporting, Externalities, and Technology Transfer*", Policy Research Working Paper # 2065, February 1999, World Bank, Washington, DC.

Robinson, Chenery and Moshe Syrquin (1986), "*Industrialization and Growth: A Comparative Study*", Oxford University Press.

Schiavo-Campo, Salvatore, Giulio de Tommaso and Amitabha Mukherjee (1997), *"An International Statistical Survey of Government Employment and Wages"*, Policy Research Working Paper No. 1806, World Bank, August 1997.

Stiglitz, Joseph (1999), "*Participation and Development: Perspectives from the Comprehensive Development Paradigm*". Speech delivered at the Political Leaders' Symposium on Leadership, Governance and Development, Seoul, Korea (Rep.), February 1999.

Vamvakidis, Athanasios (1999), "*Regional Integration and Economic Growth*", The World Bank Economic Review, Volume 12, Number 2, May 1998.

Van Eeghen, Willem (1995), "*Poverty in the Middle East and North Africa*", World Bank, Middle East and North Africa Region, August 1995.

World Bank (1994), *Republic of Tunisia, Private Sector Assessment*, Middle East and North Africa Region.

World Bank (1995), "*Tunisia: Poverty Alleviation: Preserving Progress While Preparing for the Future*", Middle East and North Africa Region, Report # 13993-TUN.

World Bank (1997), "*The Changing Role of Public Expenditures in Tunisia: Sustainability and Public/Private Partnership*" Policy Note, April 24, 1997.

World Bank (1998a), "*The Public Expenditure Management Handbook*". Poverty Reduction and Economic Management Network, Public Sector Group.

World Bank (1998b), "*World Development Report 1998/99: Knowledge for Development*". New York, N.Y.: Oxford University Press.

World Bank (2000a), "*Tunisia: Private Sector Assessment Update: Meeting the Challenge of Globalization*". Middle East and North Africa Region. Report No. 20173-TUN.

World Bank (2000b), "*Tunisia: Country Assistance Strategy*". Middle East and North Africa Region. Report No. 20161-TUN.

World Bank (2000c), "*The Employment Crisis in the MENA Region*" Middle East and North Africa Region (forthcoming).

ANNEX 1: International Lessons on Result-Based Governance

This annex reviews the overall approach to and the requirements for the implementation of a system of governance focused on the achievement of results, on the basis of the international experience accumulated during the past 20 years.

Basic Approach to Result-Based Governance

The general approach for establishing an environment conducive to continuous productivity growth within public organizations is relatively simple. International experience has clearly shown that:

- Significant productivity gains can be achieved by a governance system focused on responsibility for results instead of compliance with input-based regulations.
- Responsibility for results should be devolved to public officials at all levels – and especially at the point where services are provided to the public.
- Results must be clearly defined – in terms of the quality of public services produced, their quantity and their cost; rewards and sanctions must be linked to the achievement of these results; controls must be focused on establishing achievement of these results within general rules of integrity and scope of authority.
- Adequate managerial autonomy must be granted to allow the achievement of these results, including discretion over organization of work and choice of inputs.

Clear identification of priority results and measurement of their achievement are the quid pro quo key requirements to managerial autonomy, and constitute the basis of the accountability framework in such an environment conducive to continuous productivity growth within public organizations. The specification of clear measurable results is in general a complex task but is achievable – even for public organizations. To this end, again international experience provides the following lessons:

- Result indicators should be defined both in physical terms (e.g. training so many persons, maintains so many kilometers of roads) and in financial or productivity terms (e.g. reducing unit costs by x%). Cost accounting is a necessary condition for this; it must be complemented by more subtle measurements in order to insure that no confusion creeps in between genuine cost reductions and cutbacks in the level or services.
- Result indicators should be measurable in a transparent manner (e.g. by defining the specific characteristics that make up the quality of potable water); however, when results are achieved only in a distant future – as for health and education – intermediate measures (e.g. comparing various health organizations as to the number of procedures for a given level of equipment and personnel), or qualitative indicators (e.g. surveys on user or employers' ("clients") satisfaction) have been used with success.
- Extensive use of a very effective – and very underutilized – tool for continuous feedback on the performance of public organizations: the voice of users – households and businesses. In Tunisia, institutions recently created to improve the relations between citizens and the administration could already provide the building block for a robust system of continuous quality enhancement.
- Rewards should be based on achievement of results as measured by indicators, even though the rewards in question may vary greatly, depending on the public institution in question – ranging from distribution of realized savings within the agency, to bonuses to individual managers, to promotions tied to performance, to mechanisms for peers and public recognition

of achievements, etc. Rewards linked to performance should not be equated with performance pay schemes where the track record is mixed, whose implementation is very difficult.

Elements for the Implementation of Result-Based Governance

Owing to the critical importance and, at the same time, the difficulty of measuring results, implementing result-based management in the public sector is significantly more complex than in the private sector. International experience again indicates that implementation problems are surmountable, that success in implementation is critically dependent on the introduction of appropriate budgetary processes and financial management, and that the reform of budgetary systems has generally been pushed from the top – even though individual agencies with a strong managerial autonomy and inclination to innovation have contributed in some cases. This starting point is not only unavoidable (managerial autonomy without control over resource allocation does not mean much) but it also provides for solid risk management and gradualism, in line with Tunisian traditions. Finally, while the transformation of the budget system constitutes the essential structural element for the establishment of a result-based governance system capable to enhance productivity growth, at cruising speed it must be complemented by the setting up and systematic use of output and outcomes measurement and monitoring as alluded above, by openness to innovations in services delivery mechanisms and management, by increased flexibility in the management and deployment of human resources, etc.

The budgetary process is the single most important condition for the successful implementation of a system of result-based governance. It is in fact in the budget system that all the elements necessary for the exercise of managerial authority within the public sector are contained. Consistent with the approach discussed above, the following are necessary characteristics of the enabling budgetary processes:

- Budget envelopes for administrative units should be determined on the basis of targets defined in terms of results, measured by specific indicators (e.g. kilometers of roads to be maintained). This ensures consistency between allocations and results, and allows to track productivity growth within the administration – by program and administrative unit.

- Funds should be allocated to programs or target populations (allocation to administrative entities then becomes simply an implementation convenience), on the basis of a functional classification of expenditures. Within such programs, reallocation of funds should be allowed between the different inputs which form the basis of present expenditure classifications items, although most countries have retained centralized hiring controls because of the need to insure fairness and to preserve the traditional job security associated with the public sector. Reallocation could be limited to non-wage expenditures, or extended to wage expenditures as well, thereby giving managers flexibility to use contractors, automates, etc. Similarly, carry over of funds from one fiscal year to the next, in a regulated fashion, is normally allowed to favor the best timing in the achievement of results; the same logic grants managerial discretion in the choice of inputs combinations.

- Cost accounting should be introduced. Numerous countries have made significant progress in cost accounting including for capital consumption within public administrations. Increasingly financial management inside administrations is becoming essentially analogous to what enterprises do, and requires that administrative units impute depreciation in their budgets. In the vanguard of this change – the most important one in more than a century of public sector accounting – a few countries are now framing their overall budget within financial statements as comprehensive and as precise as those of commercial enterprises. It is expected that the shift to this type of accounting will expand to most industrialized countries within the next decade.

It should be noted that adoption of these budgetary practices has led in many countries to a number of indirect benefits. First, devolution of financial authority combined with a strong emphasis on results and costs has facilitated better understanding of the costs and better budgetary discipline – contrary to expectations that devolution would lead to a breakdown of discipline. Second, allocating budgetary resources on the basis of targets defined in terms of results has led to regular reporting of achievements of results to parliaments, and thus improved the appreciation for the trade-offs between policy objectives. Third, the introduction of cost accounting allows for cost comparisons between different modes of provision of public services, thereby facilitating the market test for public provision of public services. In the United Kingdom, for example, new initiatives submitted for consideration to the Council of Ministers are required to include a quantitative comparison between costs based on private and public provision, and between central and regional provision.

The determination to increase productivity in a continuous manner within the public sector, together with appropriate budget and control systems that encourage managerial innovation, opens a vast menu of possibilities – already experimented in other countries. The budgetary processes described above – specifying objectives in terms of costs and results – lead very naturally and at all levels, to explore the large available set of alternative modes of provision of public services. Tunisia has already introduced some limited innovations in this area, and sub-contracting arrangements are already in place for simple functions, such as maintenance and gardening; the provision of health services has also been transformed into an original mix of private, semi-private and public arrangements.

International Experience with Innovative Delivery Mechanisms

Several countries have experimented with various mechanisms to foster competition between the public sector and private providers or within the public sector itself, in the delivery of public services or the management of public resources. In some states in Canada, drivers' licenses and car registration services are sub-contracted to the private sector. In Ireland, the delivery of social services is contracted under a competitive market allocation mechanism. In Australia, bridges and tunnels are built and operated by the private sector, as are some prisons in the United States. In Sweden (with municipal services), England (with schools), Belgium and France (with hospitals), public providers are gauged against one another for their results and quality of service.

Generally, these mechanisms have led to better quality and/or lower prices for the services provided. The new mechanisms have allowed public entities undertaking procurement of services produced internally by other public sector providers (e.g. printing, real estate management, or computer servicing) to chose their provider and the level of service they want to buy. The privatization of service provision has also boosted the small and medium size enterprises sector, and helped reduce the size of the civil service by encouraging former public sector employees to set up businesses that provide services to the public sector.

ANNEX 2: Tunisia's Institutional and Administrative Setup

The Legislative Branch

In Tunisia, Parliament is a single chamber assembly made up of 163 members, elected directly by universal suffrage of Tunisians over twenty years of age.[1] Twenty five multi-membered constituencies covering the twenty three Governorates (with Sfax and Tunis, having two constituencies each) elect 144 candidates, while a nationwide constituency elects the remaining nineteen seats.

The voting system is mixed, with 144 deputies being chosen by party-list simple majority system. In each of the twenty five constituencies, the elector chooses a list of candidates without replacing the names given. All constituency seats go to the winning list. The nineteen remaining seats are allotted proportionately to parties that were unsuccessful in the constituencies on the basis of percentage votes own at the national level and the highest average formula.

In the last Parliamentary elections of 1994, the first in which opposition was allowed to participate, six parties, in addition to the ruling Rassemblement Constitutionnel et Démocratique (RCD) were allowed to participate. One party, the Islamist Al-Nahda was banned. The electoral campaign lasted two weeks (from March 6 to March 18).

The ruling RCD party is the predominant party in Tunisia, with the largest organizational structure, reaching into remote rural areas and closely affiliated with state Administration. The other parties, are generally small, financially weak, with no real party base, often relying on the single personality of their leader.

Polling day, monitored by foreign observers, saw a high turnout. The RCD won 144 out of 163 seats, with four other parties gaining the remaining nineteen. Some opposition parties alleged electoral fraud. Of the 163 deputies twelve (7.36%) are women.

The electoral code has been amended to limit to 80% the percentage of seats in the National Assembly that any single party may hold. This guarantees the legal opposition parties at least thirty seats in new parliament (as opposed to the nineteen in the past).

The Executive Branch

According to the Constitution, the President of Republic is the head of the executive and is assisted by a Government. Any Tunisian of Muslim religion, between the age of forty and seventy on the day of submission of his candidacy is eligible to run for President. He is elected to a five-year term by the free universal suffrage. He is limited to a maximum of three consecutive terms in office. In 1994, President Ben Ali, running unopposed, was re-elected with over 99% of the vote to his second consecutive five-year term. President Ben Ali has be re-elected in the recent elections with an equally large mandate (99.4% of the votes) for a last term in office according to the Constitution.

Under the Constitution, the President is the Supreme Commander of the Armed Forces. He nominates the Prime Minister and other members of his Government and presides over the Council of Ministers. He is entitled to dismiss the Government either on his own initiative or on recommendation of the President.

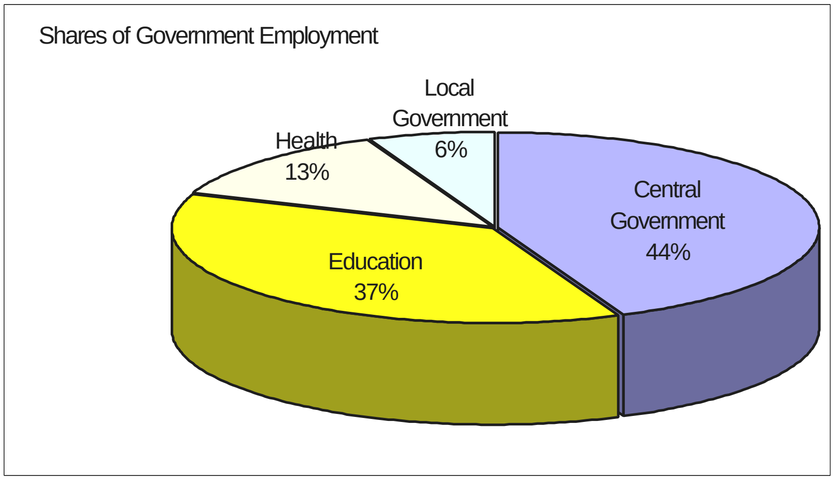
The Administration

General Civilian Government Employment in Tunisia, defined as Central Government Employment, Local (Communes) Government Employment, Education and Health Employment, is estimated at 345,900 employees in 1998, an increase of approximately 27,000 employees since 1995.

---

[1] Article 21 of the 1991 gives voter eligibility to all Tunisians who have retained their Tunisian citizenship for at least 5 years, and have not been convicted of crimes, been imprisoned, or declared insane.

The composition of Government Administration in Tunisia



Source: Staff estimates.

Women make up approximately one third of all General Administration Employment. The Wage bill accounts for approximately 10% of GDP in Tunisia in 1998.

International comparisons of Government employment show that, in relative terms, Tunisian Government employment is below the worldwide average (about 4.7% of the population for our sample) and in line with the rest of the MENA region.

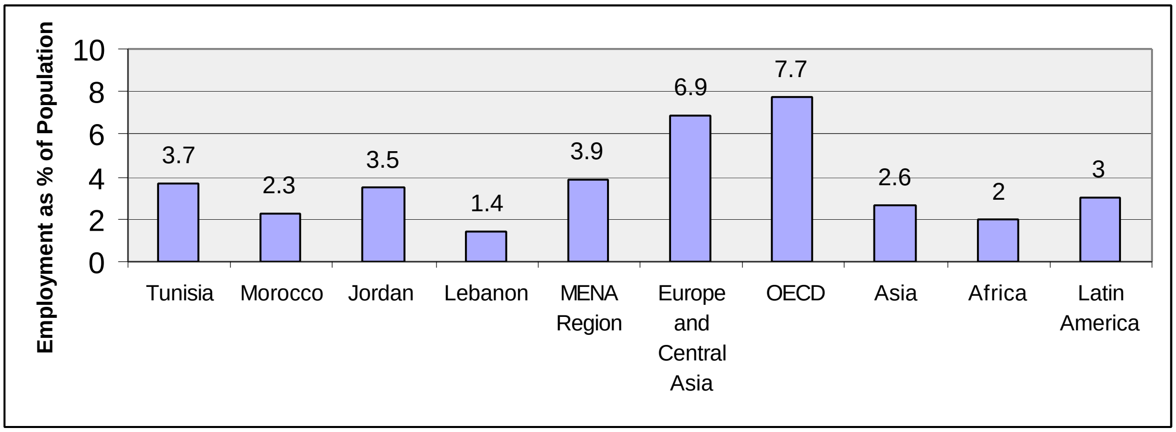
Moreover, international comparisons of wages and salaries show that, in relative terms, Tunisian Wages and Salaries expenditures are in line with other Middle East and North African countries, where the fiscal weight of central government wage bill is higher than in any other region. Asia, the OECD and Latin America are half the level of the Middle East and North Africa and in Europe and Central Asia is one third.

Tunisian Public Administration relies on a meritocratic, professional and competent civil service. The system is unitary and governed by a general statute applicable to both central and local government employees.

The employees covered by this statute are paid directly by the State. In Tunisia, therefore, there is no tradition of institution-specific or of territory-specific employment. Since 1995, municipalities and Governorate Councils are allowed to recruit personnel as long as their number falls within the limits approved by the oversight authority. Examinations are conducted in a decentralized way up to the level A2.

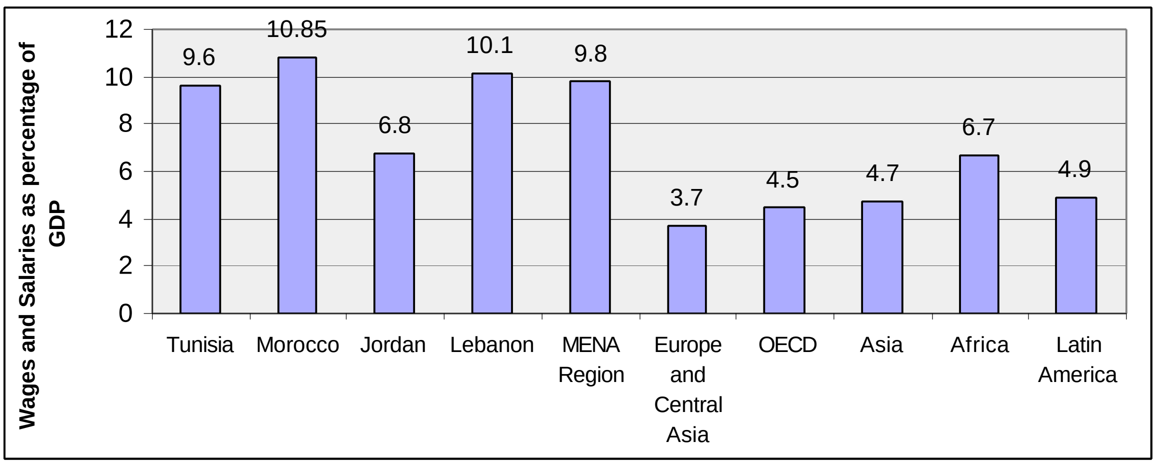
Overall, the system is very complex. There are approximately 150 special corps within the Tunisian civil service, each with a special statute governing it. The multiplication of these corps can be explained in all likelihood by the pressures exercised by labor unions seeking special working conditions and seeking to negotiate special statutes for their members.

Government Employment as Percentage of Population



Source: World Bank, Schiavo-Campo, de Tommaso and Mukherjee, 1997.

Wages and Salaries as Percentage of GDP, *various recent years*



Source: World Bank, MNA LDB, Schiavo-Campo, de Tommaso and Mukherjee, 1997.

Personnel redeployment at this stage is hampered by different problems, one of which is the presence of such a large number of corps. The primary obstacle is the great difference in culture which exists from institution to institution. Very noticeable is the one prevalent for example in the Education Sector or in the Ministry of Finance.

Despite encouraging international comparisons, country specific evidence suggests that Tunisian civil service may be overstaffed, especially in the lower ranks. Privatization of certain activities (such as cleaning services) has taken place, but recruitment has not been interrupted in the corps specific to those sectors.

In order to reduce some of the institutional rigidity highlighted above, term-employment or contracting was expanded and mainstreamed into public administration. As a result, the number of career civil servants has been reduced and the number of contract employees appears to have increased.

Compensation Issues

Tunisian Public Administration is characterized by a relatively flat salary structure. The Compression ratio (i.e. the ratio between the highest salaries and the lowest) is estimated around 5:1, compared to the 11:1 which appears to be the norm by international standards. Many of the people surveyed have confirmed that the salaries given to managers are not competitive and as a result the morale is relatively low.

However, if other forms of compensation are taken into account – such as professional prestige and job security – it appears that it is not too difficult to replace departing managers. In addition to the great number of college graduates, there are many applicants to different competitive examinations. The large number of applicants for examinations for the middle ranks of the administration seems to indicate that these employees are probably overpaid in relative terms.

A 1997 law created a new salary grid for civil service employees, harmonizing it among different "corps" and integrating many allowances into the base salary. Two thirds of allowances have been integrated into the basic salary, and, with the exception of posts of responsibility[2] all allowances will eventually be integrated into the basic salary. The basic monthly salary of employees has been fixed as of January 1, 1998 according to a new salary grid. The number of "echelons" has been increased in order to permit the advancement of employees over a longer number of years, and the ceiling has been modified so as to motivate the employees who were reaching those ceilings rapidly. The reform seems to have benefited the employees, however the benefit is rather small. In the case in which the reclassification of employees led to a reduction of the monthly salary, a compensatory indemnity is given.

The Judiciary Branch

According to the Constitution, the Independence of the Judiciary is guaranteed.[3] As a result, the Magistrates are not formally subjected to the authority of any of the other branches of government. The Supreme Council of the *Magistrature* is the guarantor of such independence and watches over the application of the guarantees accorded to Magistrates in areas of nomination, advancement, transfer and discipline.

2 *Emplois Fonctionnels.*

3 Article 65 of the 1991 Constitution.

ANNEX 3: Tunisia: Summary of Investment Code Incentives

Type of Incentive	Initial Capital	Investment	Tax Holiday	Reduced Rate after Holiday	Duties on Equipment	Suspension of VAT, and Consumer Taxes on equipment	Contribution to *Fonds de Promotion de Logement*	Investment Premium	Depreciation
Common		Deductibility of reinvested earnings up to a limit of 35% of revenues or net profits			Reduced to 10%	Yes			Can opt for declining balance rather than straight line for capital with life longer than seven years
Export			10 year	50% reduction	Reduced to 10%	Yes			
Partially Export			pro rata	pro rata	Reduced to 10%	Yes			
Regional	Deductible		10 year	50% reduction for 10 years	Reduced to 10%	Yes	5 year exemption	15-25%	
Agricultural	Deductible		10 year		Reduced to 10%	Yes		7-25%	
Anti-Pollution And Environmental Protection	Deductible up to 50% of revenue	Deductible	Revenues Deductible subject to constraint on taxes due		Reduced to 10%	Yes			
Promotion of Technology and R&D					Reduced to 10% Nil for R&D	Yes			
New Entrepeneurs of SMEs	Maximum 3mill.DT				Reduced to 10%	Yes		10%	
Supporting Investment	Deductible up to 50% of revenue			50% reduction	Reduced to 10%	Yes			
Discretionary			5 year		Reduced to 10%	Yes		5% additional <25 or 30%	

Annex Table 1: Tunisia: Sectoral shares and contributions to GDP growth

	Value added (constant 1990 prices)				Growth rates (%)			Share in GDP (%)				Percentage of GDP growth contributed by sectors		
	1995	1996	1997	1998	1995-96	1996-97	1997-98	1995	1996	1997	1998	1995-96	1996-97	1997-98
AGRICULTURE AND FISHERY	**1573**	**2038**	**2098**	**2077**	**29.5%**	**3.0%**	**-1.0%**	**13.7%**	**16.5%**	**16.1%**	**15.2%**	**52.5%**	**9.0%**	**-3.4%**
MANUFACTURING INDUSTRIES	**2404**	**2469**	**2645**	**2739**	**2.7%**	**7.1%**	**3.6%**	**20.9%**	**19.9%**	**20.3%**	**20.0%**	**7.3%**	**26.3%**	**15.4%**
Agro processing industries	426	434	517	491	1.9%	19.0%	-5.0%	3.7%	3.5%	4.0%	3.6%	0.9%	12.4%	-4.2%
MAN. OTHER THAN AGRO PROCESSING	**1978**	**2034**	**2128**	**2248**	**2.9%**	**4.6%**	**5.7%**	**17.2%**	**16.4%**	**16.3%**	**16.5%**	**6.4%**	**14.0%**	**19.7%**
Construction materials and glass	264	263	265	275	-0.3%	1.0%	3.5%	2.3%	2.1%	2.0%	2.0%	-0.1%	0.4%	1.5%
Mechanical and Electric industries	335	338	362	387	0.9%	7.0%	7.0%	2.9%	2.7%	2.8%	2.8%	0.4%	3.5%	4.1%
Chemical industries	254	267	275	288	5.1%	3.0%	4.5%	2.2%	2.2%	2.1%	2.1%	1.5%	1.2%	2.0%
Textile, Clothing and Leather	804	832	873	926	3.5%	5.0%	6.0%	7.0%	6.7%	6.7%	6.8%	3.2%	6.2%	8.5%
Other industries	321	334	352	373	4.1%	5.4%	6.0%	2.8%	2.7%	2.7%	2.7%	1.5%	2.7%	3.4%
NON MANUFACTURING INDUSTRIES	**1587**	**1656**	**1711**	**1819**	**4.3%**	**3.3%**	**6.4%**	**13.8%**	**13.4%**	**13.1%**	**13.3%**	**7.8%**	**8.2%**	**17.7%**
Mining	111	118	107	125	7.0%	-9.3%	16.4%	1.0%	1.0%	0.8%	0.9%	0.9%	-1.6%	2.9%
Hydrocarbon	602	635	639	662	5.6%	0.6%	3.6%	5.2%	5.1%	4.9%	4.8%	3.8%	0.6%	3.8%
Electricity	206	215	229	244	4.3%	6.8%	6.5%	1.8%	1.7%	1.8%	1.8%	1.0%	2.2%	2.4%
Water	70	72	76	80	2.4%	5.6%	5.0%	0.6%	0.6%	0.6%	0.6%	0.2%	0.6%	0.6%
Construction	599	616	659	709	2.8%	7.0%	7.5%	5.2%	5.0%	5.1%	5.2%	1.9%	6.5%	8.1%
SERVICES	**4582**	**4870**	**5161**	**5514**	**6.3%**	**6.0%**	**6.8%**	**39.9%**	**39.3%**	**39.6%**	**40.4%**	**32.5%**	**43.6%**	**57.6%**
Commerce	1215	1257	1304	1392	3.5%	3.7%	6.7%	10.6%	10.2%	10.0%	10.2%	4.8%	7.0%	14.3%
Transport	736	772	834	880	5.0%	8.0%	5.5%	6.4%	6.2%	6.4%	6.4%	4.2%	9.2%	7.5%
Communications	251	319	349	402	27.3%	9.5%	15.0%	2.2%	2.6%	2.7%	2.9%	7.7%	4.5%	8.5%
Hotels, Bars, Restaurants	680	706	758	800	3.7%	7.4%	5.5%	5.9%	5.7%	5.8%	5.9%	2.9%	7.8%	6.8%
Financial Services	593	658	696	742	11.1%	5.7%	6.7%	5.2%	5.3%	5.3%	5.4%	7.4%	5.6%	7.6%
Other Saleable services	1108	1157	1220	1299	4.4%	5.4%	6.5%	9.6%	9.3%	9.3%	9.5%	5.5%	9.4%	12.9%
o/w real estate renting	479	493	535	557	3.0%	8.5%	4.0%	4.2%	4.0%	4.1%	4.1%	1.6%	6.3%	3.5%
OTHERS	**456**	**516**	**535**	**560**	**13.1%**	**3.8%**	**4.6%**	**4.0%**	**4.2%**	**4.1%**	**4.1%**	**6.8%**	**2.9%**	**4.0%**
Non market services	1801	1861	1967	2073	3.3%	5.7%	5.4%	15.7%	15.0%	15.1%	15.2%	6.8%	15.8%	17.3%
o/w public Administration	1743	1803	1908	1990	3.4%	5.8%	4.3%	15.2%	14.6%	14.6%	14.6%	6.7%	15.7%	13.4%
GDP AT FACTOR COST	**11491**	**12377**	**13046**	**13663**	**7.7%**	**5.4%**	**4.7%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**			
Indirect taxes minus subsidies	1583	1631	1722	1842	3.1%	5.5%	7.0%							
GDP AT MARKET PRICE	**13074**	**14009**	**14768**	**15506**	**7.1%**	**5.4%**	**5.0%**							

Annex 2: Tunisia: Comparative Public Finance Indicators

Tunisia versus 3 MENA Low Middle Income Countries

(in % of GDP, unless otherwise indicated)

Indicator	Tunisia		Morocco		Jordan		Lebanon	
	1997	1998	1997	1998	1997	1998	1997	1998
PUBLIC FINANCE INDICATORS								
Current Revenues	23.9	25.1	22.7	25.5	33.4	28.7	17.4	19.4
Current Expenditures	21.6	20.6	23.8	22.8	29.2	29.9	30.7	28.5
Budgetary Savings	2.3	4.5	-1	2.6	4.1	-1.2	-13.3	-9.2
Capital Revenues	0.7	..	..	..	..	..	..	..
Capital Expenditures	6.5	8	6.1	6.4	6.4	5.7	5.5	5.6
Overall Balance	-3.5	-2.9	-7.2	-3.8	-2.3	-6.9	-18.8	-14.7
Official Capital Grants	0.3	..	..	..	..	..	0.3	..
Net External Borrowing	2.3	3.1	-1.9	-1.4	-0.1	-0.6	4.5	4.5
Monetary System Credit	-0.1	-0.2	-7.7	0.9	-1.2	7.5	4.3	2.8
Other Domestic Financing	0.9	0.6	16.8	4.3	3.6	0	9.7	7.5
Breakdown of Current Expenditures								
Interest on External Debt	1.92	2.1	2.31	2.26	4.42	4.19	1.12	1.45
Interest on Domestic Debt	1.84	1.49	3.1	3.24	0.42	0.44	13.91	12.52
Transfers to Private Sector	-2.22	-0.7	--	--	4.4	5.29	0	0
Transfers to Other NFPS	0	2	--	--	0.78	1.42	N/A.	N/A.
Subsidies	4.62	4	1.94	1.8	1.03	0.78	N/A.	N/A.
Consumption	15.48	11.7	16.41	15.53	18.18	17.78	15.69	14.55
Wages and Salaries	10	9.6	11.77	10.85	7.19	6.8	10.71	10.1
Other Consumption	5.48	2.1	4.64	4.68	10.99	10.98	4.98	4.45
GOVERNMENT DEBT (DOD)								
External Debt (US$ billions)	10.95	8.217	19.09	13.41	6.46	6.42	2.529	3.294
External Debt as a Ratio of GDP	38.43	43.37	42.71	37.12	92.41	86.91	16.8	19.29
Debt to Monetary System as a Ratio of GDP	5.97	18.22	19.92	25.48	10.13	17.07	-11.2	-7.07
Other Domestic Debt as a Ratio of GDP	14.03	-2.54	28.68	23.9	8.36	7.89	83.15	80.81
Total Government Debt as % of GDP	58.4	59.1	91.3	86.5	111.1	111.9	93	93.9
TAX BURDEN INDICATORS								
Direct Taxes/GDP	4.7	5.8	6.8	6.4	3.2	3.4	3.2	3.2
Indirect Taxes / GDP	12.8	12.5	8.5	12.1	8.6	7.1	3.3	3.7
Indirect Taxes / Private Consumption	19.9	19.5	12.8	18.1	12.4	10.9	3.2	3.8
Taxes on International Trade / Merchandize Imports	8.9	7	28	16.1	..	..	14.4	18

Notes: -- : Significantly small (lower than 0.05%)

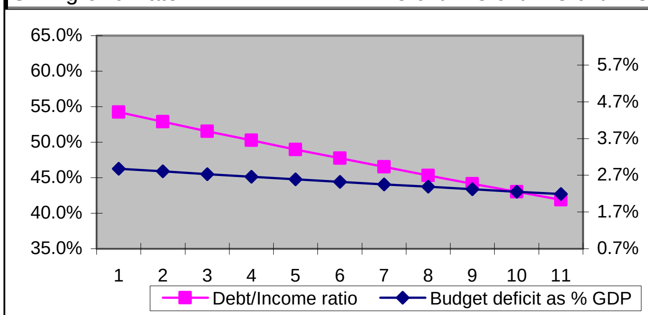
Figures for 1997 are actual and for 1998 are estimates.

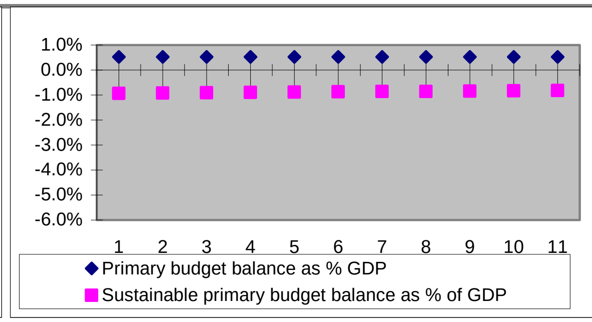
Sources: World Bank, MNA LDB

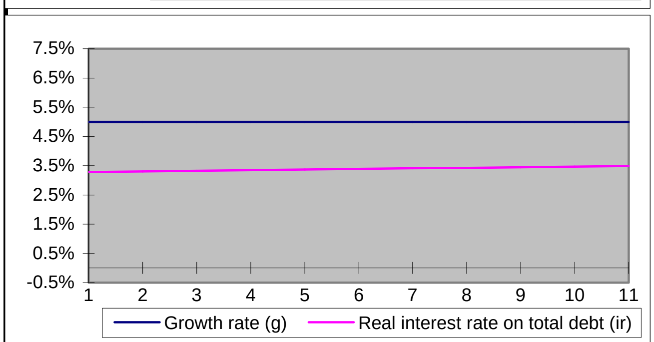
Annex Table 3: Tunisia: Fiscal Sustainability Analysis -- Baseline Scenario

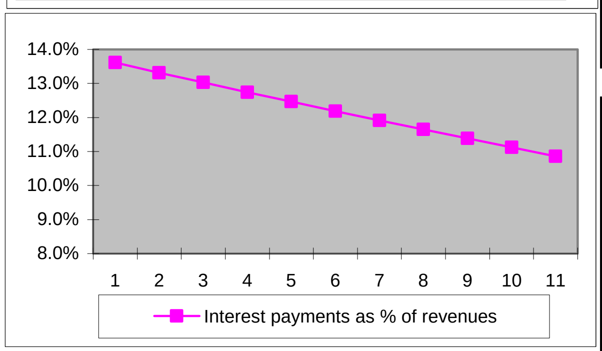
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Growth rate (g)	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Real GDP (Y)	22809	23950	25147	26404	27725	29111	30566	32095	33699	35384	37154
Ext. interst rate (i)	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%
Internal interst rate (r)	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Real domestic debt (Dd)	4275	4487	4704	4926	5153	5384	5619	5859	6103	6352	6604
Real external debt (Df)	8100	8179	8260	8342	8426	8512	8600	8689	8780	8872	8966
Domestic deflator (DEFd)	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Depreciation rate (DEV)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Beta (E/Y)	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245
Alpha (R/Y)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
delta	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729
Budget deficit (bd)	656	671	687	702	718	734	750	766	781	797	813
Primary expenditures (E)	5586	5865	6159	6467	6790	7129	7486	7860	8253	8666	9099
Revenues (R)	5707	5992	6292	6606	6936	7283	7647	8030	8431	8853	9295
Real interest rate on total debt (ir)	3.3%	3.3%	3.3%	3.3%	3.4%	3.4%	3.4%	3.4%	3.4%	3.5%	3.5%
Real total debt (D)	12375	12666	12964	13268	13579	13896	14219	14548	14883	15224	15570

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Debt/Income ratio	54.3%	52.9%	51.6%	50.3%	49.0%	47.7%	46.5%	45.3%	44.2%	43.0%	41.9%
Budget deficit as % GDP	2.9%	2.8%	2.7%	2.7%	2.6%	2.5%	2.5%	2.4%	2.3%	2.3%	2.2%
Primary budget balance as % GDP	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
Sustainable primary budget balance as % of GDP	-0.9%	-0.9%	-0.9%	-0.9%	-0.9%	-0.9%	-0.9%	-0.9%	-0.8%	-0.8%	-0.8%
Interest payments as % of revenues	13.6%	13.3%	13.0%	12.7%	12.5%	12.2%	11.9%	11.6%	11.4%	11.1%	10.9%
Foreign Int. payments as % GDP	1.9%	1.8%	1.8%	1.7%	1.6%	1.6%	1.5%	1.5%	1.4%	1.3%	1.3%
GDP growth rate	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%





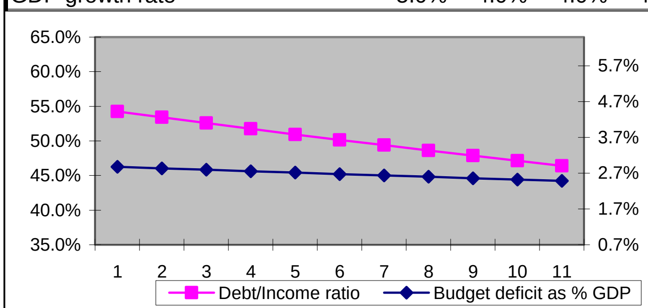


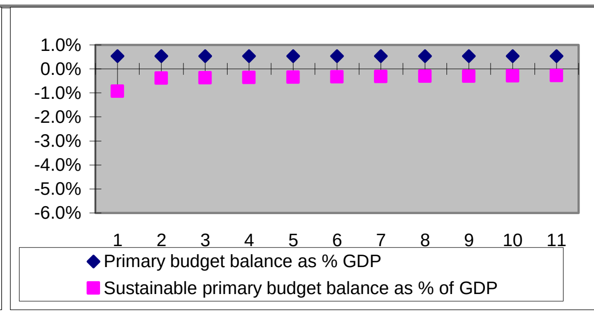


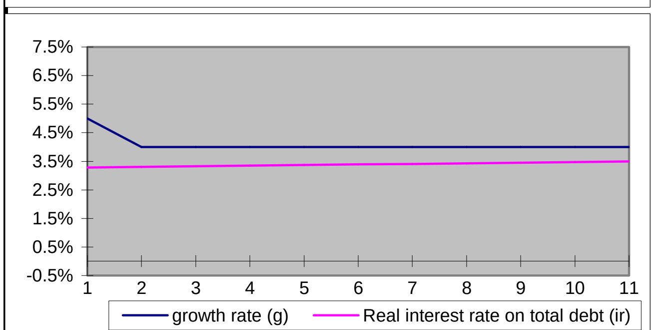
Annex Table 4: Tunisia: Fiscal Sustainability Analysis -- Scenario with Lower GDP Growth

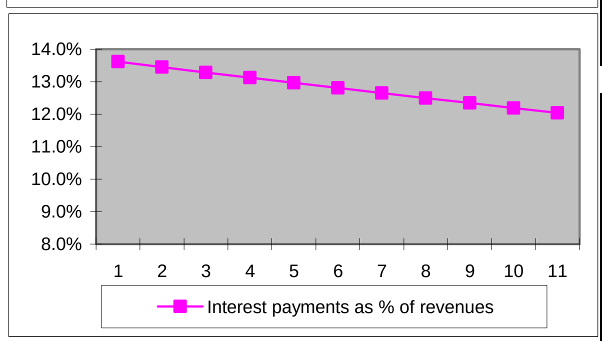
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
growth rate (g)	5.0%	**4.0%**	**4.0%**	**4.0%**	**4.0%**	**4.0%**	**4.0%**	**4.0%**	**4.0%**	**4.0%**	**4.0%**
Real GDP (Y)	22809	23721	24670	25657	26683	27751	28861	30015	31216	32464	33763
Ext. interst rate (i)	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%
Internal interst rate (r)	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Real domestic debt (Dd)	4275	4488	4707	4932	5163	5400	5643	5893	6148	6410	6679
Real external debt (Df)	8100	8179	8261	8344	8430	8518	8609	8701	8797	8894	8994
Domestic deflator (DEFd)	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Depreciation rate (DEV)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Beta (E/Y)	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245
Alpha (R/Y)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
delta	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729
Budget deficit (bd)	656	673	690	707	725	743	761	780	799	819	839
Primary expenditures (E)	5586	5810	6042	6284	6535	6796	7068	7351	7645	7951	8269
Revenues (R)	5707	5935	6172	6419	6676	6943	7221	7510	7810	8122	8447
Real interest rate on total debt (ir)	3.3%	3.3%	3.3%	3.3%	3.4%	3.4%	3.4%	3.4%	3.5%	3.5%	3.5%
Real total debt (D)	12375	12667	12968	13277	13593	13918	14252	14594	14945	15304	15673

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Debt/Income ratio	54.3%	53.4%	52.6%	51.7%	50.9%	50.2%	49.4%	48.6%	47.9%	47.1%	46.4%
Budget deficit as % GDP	2.9%	2.8%	2.8%	2.8%	2.7%	2.7%	2.6%	2.6%	2.6%	2.5%	2.5%
Primary budget balance as % GDP	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
Sustainable primary budget balance as % of GDP	-0.9%	-0.4%	-0.4%	-0.4%	-0.3%	-0.3%	-0.3%	-0.3%	-0.3%	-0.3%	-0.3%
Interest payments as % of revenues	13.6%	13.4%	13.3%	13.1%	13.0%	12.8%	12.7%	12.5%	12.3%	12.2%	12.0%
Foreign Int. payments as % GDP	1.9%	1.9%	1.8%	1.7%	1.7%	1.6%	1.6%	1.6%	1.5%	1.5%	1.4%
GDP growth rate	5.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%





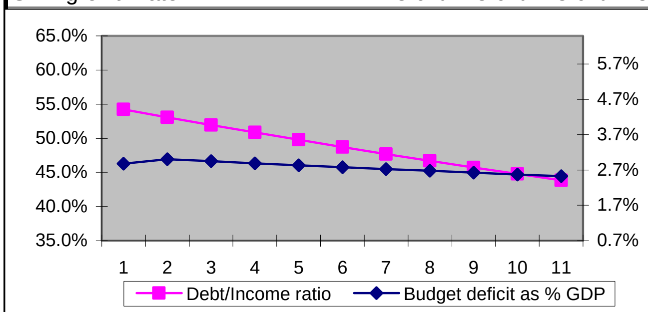


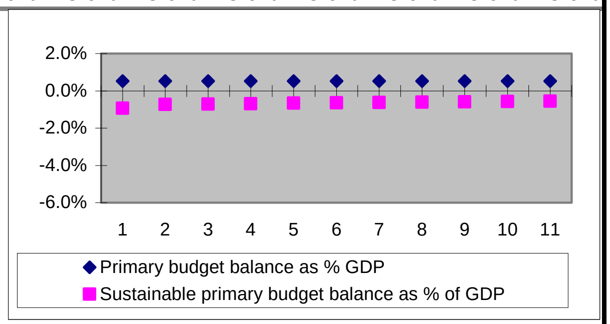


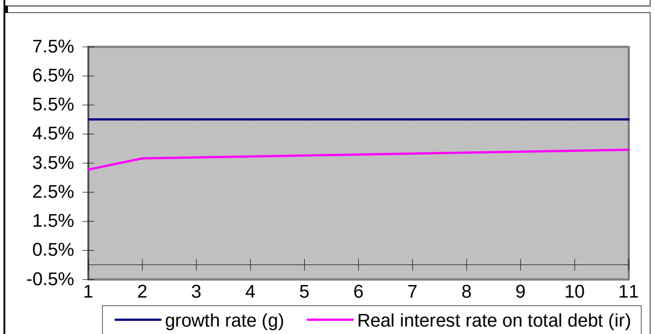
Annex Table 5: Tunisia: Fiscal Sustainability Analysis -- Scenario with Higher Domestic Interest Rate

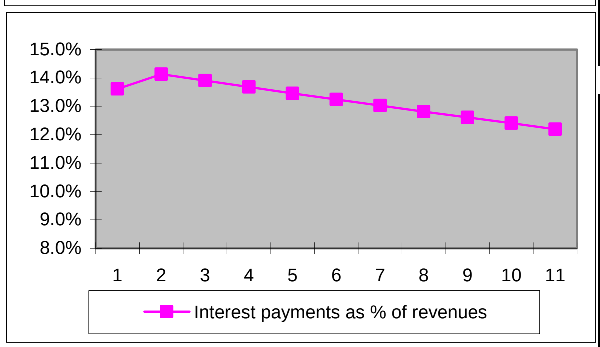
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
growth rate (g)	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Real GDP (Y)	22809	23950	25147	26404	27725	29111	30566	32095	33699	35384	37154
Ext. interst rate (i)	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%	2.4%
Internal interst rate (r)	5.0%	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**
Real domestic debt (Dd)	4275	4522	4777	5040	5312	5593	5883	6181	6490	6807	7134
Real external debt (Df)	8100	8192	8287	8385	8486	8590	8698	8809	8923	9041	9163
Domestic deflator (DEFd)	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Depreciation rate (DEV)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Beta (E/Y)	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245	0.245
Alpha (R/Y)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
delta	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729	0.729
Budget deficit (bd)	656	720	742	764	787	811	835	860	885	911	938
Primary expenditures (E)	5586	5865	6159	6467	6790	7129	7486	7860	8253	8666	9099
Revenues (R)	5707	5992	6292	6606	6936	7283	7647	8030	8431	8853	9295
Real interest rate on total debt (ir)	3.3%	3.7%	3.7%	3.7%	3.8%	3.8%	3.8%	3.9%	3.9%	3.9%	4.0%
Real total debt (D)	12375	12713	13063	13425	13798	14183	14580	14990	15413	15848	16297

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Debt/Income ratio	54.3%	53.1%	51.9%	50.8%	49.8%	48.7%	47.7%	46.7%	45.7%	44.8%	43.9%
Budget deficit as % GDP	2.9%	3.0%	3.0%	2.9%	2.8%	2.8%	2.7%	2.7%	2.6%	2.6%	2.5%
Primary budget balance as % GDP	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
Sustainable primary budget balance as % of GDP	-0.9%	-0.7%	-0.7%	-0.7%	-0.7%	-0.7%	-0.6%	-0.6%	-0.6%	-0.6%	-0.6%
Interest payments as % of revenues	13.6%	14.1%	13.9%	13.7%	13.5%	13.2%	13.0%	12.8%	12.6%	12.4%	12.2%
Foreign Int. payments as % GDP	1.9%	1.8%	1.8%	1.7%	1.6%	1.6%	1.5%	1.5%	1.4%	1.4%	1.3%
GDP growth rate	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%









Annex Table 6 : Tunisia: International Comparison of Selected Indicators

		New OECD		Prospective EU		Recent EU		Neighbours		Fast Grw.Small Econ.				
Indicator	**Tunisia**	**Korea**	**Slovenia**	**Hungary**	**Czech**	**Portugal**	**Greece**	**Morocco**	**Jordan**	**Ireland**	**Taiwan**	**MIC**	**MENA**	**LMIC** (Excl. China)
GNP per capita, PPP (constant 1987 international $)1996	3644	9976	9086	5259	8331	10236	9436	2596	2763	14131	..	..	..	
Average rank														
TABLE 1. GOVERNANCE														
i) Size of the State														
Government Employment (% of total) 1995	..	4.4	..	24.1	..	15.3	..	..	..	13.4	11.1	..	..	
General Govt. Expenditure (% of GDP)1995-1996	16.3	10.6	20.5	10.1	22.4	46.4	33.6	16.4	23.2	55.3	24.8		..	
ii) Government Effectiveness and Stability														
Socioeconomic Conditions [1] (0-12: Low-High)	6	6	5	4	7	8	6	4	5	9	9	..	..	
Institutional stability[2] (1-7: L- H)	..	2.8	..	5.76	3.61	6.01	4.75	..	4.46	5.67	3.98	..	..	
Government Stability[3](0-12: L-H)	11	10	11	11	9	10	10	11	11	10	11	..	..	
iii) Rule of Law														
Law and Order (0-6: L-H)	5	4	5	6	5	5	4	6	4	6	4	..	..	
Property Rights and Rule-based Governance [4](1-6: L-H)	4.5	4	5	4.5	4.5	..	..	4.5	4	..	..			
iv) Public Finance						..	..			..	..			
Quality of Budget and Public Investment Process [5] (1-6: L-H)	5	4.5	4.5	5	4.5	..	..	3	3.5	..	..			
Efficiency and Equity of Public Expenditures[6] (1-6: L-H)	4.5	4	4	4.5	4	..	..	3	3	..	..			
Efficiency and Equity of Revenue Mobilization[7](1-6:L-H)	4.5	4	5	4	4	..	..	4	3	..	..			
Management of Public Finances														
Collected Total Tax Revenues [8](% of GDP)	25.1	17.7	..	23.0	35.6	32.1	19.7	..	21.0	35.4	16.0	..	..	
Central Govt Budget Surplus/Deficit (% of GDP)	-3.2	0.3	..	..	0.4	-5.5	-9.6	..	1.1	..	..	..	..	
Corporate tax rate (1997)	..	30	..	18	39	36	35	..	..	10	25	..	..	
v) General Public Administration														
Bureaucracy Quality[9] (0-4:L-H)	2	4	3	4	3	3	3	2	2	4	3	..	..	
Public Service[10] (0-10:L-H)	..	2.93	..	3.33	3.61	2.7	1.56	..	..	6.07	3.67	..	..	
Accountability of the Public Service[11] (1-6:L-H)	4	4	4.5	4	4	..	..	3	3	..	..	..	..	
Irregular Payments (higher scale means less)[12] (1-6:L-H)	..	4	..	4.12	3.81	5.16	3.89	..	4	6.08	5.38	..	..	
vi) Business Environment														
Corruption, 1998 (0-6:higher scale means lower corruption)[13]	3	4	4	5	4	5	5	3	4	3	3	..	..	
Heritage Banking Index (1997) (1-6:L-H)	2	2	2	2	1	..	..	3	2	..	..			
Heritage Foerign Investment Index (1997) (1-6:L-H)	2	3	3	2	2	..	..	2	2	..	..			
Heritage Regulation Index (1997)														
Heritage Trade Policy Index (1997)	5	3	4	4	1	..	..	4	4	..	..			
Heritage Wage and Price Controls Index (1997)	2	2	3	2	2	..	..	3	3					
TABLE 2. POVERTY AND INCOME DISTRIBUTION														
Population below the poverty line (%)(1988-94)[a]	14.1 (1990)	..	..	25.3 (1993)	..	..	..	3.1 (1990-9	15 (1991	..	..			
TABLE 3. HEALTH														
Health expenditure per capita, PPP ($)(1990-95)[a]	..	518.0	..	496.0	970.0	..	706.0	126.0	347.0	..	..	382.9	362.5	270.0

Health expenditure, total (% of GDP)(1990-95)[a]	5.9	5.4	..	7.3	9.6	8.1	7.3	3.4	7.9	6.7	..	6.3	4.3	5.7
Health expenditure, public (% of GDP)(1990-95)[a]	3.0	1.8	7.4	6.8	7.7	4.5	5.5	1.6	3.7	5.4	..	3.6	2.6	3.4
Physicians														
per 1,000 people, 1994	0.6	1.2	2.2	3.6	2.9	2.9	4.0	0.4	1.6	2.0	..	1.6	1.1	2.5
per 1,000 people, % change 1980-94	5.4%	5.3%	..	2.6%	..	2.6%	3.6%	14.6%	5.3%	3.3%	..	0.9%	..	
Hospital beds														
per 1,000 people, 1994	1.8	4.1	5.8	9.6	7.4	4.3	5.0	1.1	1.6	5.0	..	4.6	1.8	6.4
per 1,000 people, % change 1980-94	-1.3%	6.5%	-1.4%	0.4%	..	..	-1.6%	-0.7%	1.9%	-4.6%	..	..	0.3%	
Safe water (% of population with access)(1995)	99.0	89.0	..	..	..	..	..	52.0	89.0	..	..	75.0	71.0	70.5 (1993)
Sanitation (% of population with access)(1995)	..	100.0	90.0	94.0	..	100.0	96.0	40.0	100.0	100.0	..	76.9	95.5	69.7
Prevalence of child malnutrition(1995)[a]	9	..	..	..	..	..	..	..	10	..	..	..	..	
TABLE 4. EDUCATION														
Public expenditure on education (% of GNP)(1993)	6.3	4.5	..	6.7	5.9	5.4	..	6.2	4.2	6.4	..	4.9	5.1	4.6 (1994)
Pupil-teacher ratio, primary	25.2	29.5	15.1	11.0	20.4	12.4	16.5	28.3	21.5	23.6	..	23.8	26.9	24.9 (1994)
School enrollment														
Primary														
% gross, 1996	116.5	94.0	97.9	97.0	103.0	..	..	86.0	..	104.0	..	104.9	93.2	97.9 (1994)
gross, annual average % change 1990-96	0.0%	-0.2%	0.0%	..	..	..	..	0.5%	..	..	..	..	..	
Secondary														
% gross, 1996	64.6	102.0	91.7	81.0	96.0	..	95.0	39.1	..	114.0	..	60.4	61.5	57.5
gross, annual average % change 1990-96	1.1%	0.2%	0.2%	..	..	..	..	0.3%	..	..	..	..	..	
Tertiary														
% gross, 1996	13.7	60.3	36.4	25.1	22.7	38.0	42.8	11.3	..	40.3	..	19.0	23.5	18.7
gross, annual average % change 1990-96	1.0%	2.5%	1.5%	0.9%	0.6%	0.4%	0.1%	0.1%	..	0.8%	..	..	..	
TABLE 5. GENDER														
Maternal mortality ratio(per 100,000 live births)(1990-96)[a]	30.3	30.0	5.0	14.0	7.0	15.0	10.0	372.0	150.0	10.0	..	36.9	50.0	
Births attended by health staff (% of total)(1992)	50	95	..	99	..	..	..	..	86	..	..	71 (1990)	80(1993)	67 (1990)
Illiteracy rate, adult female (% of females 15+)(1995)	45.4	3.3	..	..	..	..	..	69.0	20.6	..	..	22.2	50.1	25.3
Primary education, pupils (% female)(1994)	46.9	48.1	48.9	48.9	48.9	..	48.4	41.6	49.1	48.6		48.2	44.8	47.9
Secondary education, pupils (% female)(1995)	..	48.5	49.4	49.7	49.6	..	48.8	..	47.2	50.5	..	51.7	48.1	49.8
Secondary education, vocational pupils (% female)(1994)												39.7 (1993	34.2	42.3
Labor force, female (% of total)(1997)	10.83	93.82	46.11	21.27	26.87	21.7	16.804	36.9	29.11	50.52	..	36.60 (199	4.17(1996	36.46 (1994)
TABLE 6. ENVIRONMENT														
Organic water pollutant emissions														
kg/day/worker, 1993	..	0.125	..	..	..	0.156	0.190	..	..	0.175		..	..	
kg/day/worker, 1980-93, % change														
GDP per unit of energy use														
1987 US$ per kg of oil equivalent, 1995	2.429	1.753	..	0.951	0.846	2.700	2.778	2.825	1.864	4.370	..	2.650	2.127	2.680 (1994)
1980-95, % change														
Air Pollutants (micrograms per cu.m.)(1995)[14]														
CO2 Emmission, Industrial(Kg per 1987US$ of GDP-1996)	0.84	0.84	0.67	0.13	0.24	0.44	0.69	0.75	..	0.50	..	2.28 (1995	1.67 (1995	2.26 (1994)
TABLE 7. LABOR MARKETS														
Labor force, total (million)	3.4	22.0	1.0	4.7	5.6	4.9	4.4	10.5	1.2	1.4	0.0	694.7	89.3	9.4
Labor force, children 10-14 (% of age group)(1996)	0.0	0.0	0.0	0.1	0.0	1.7	0.0	4.6	0.6	..	..	6.9	5.5	6.1

Strikes and Lockouts, mandays lost per labor force participant p.a.(avg.1993-97)		893	..	2	16	53	450	..	..	115	..	..	..	
TABLE 8. TRADE														
Trade, exports and imports (% of GDP, PPP)(1996)	30.2	46.7	74.0	41.4	46.3	43.1	27.9	14.0	36.6	121.6		21.8	18.9	33.5
Exports of goods and services (annual % growth)(1996)	0.5	14.1	..	7.4	..	5.8	..	6.3	12.2	..	..	5.1	7.4	5.3
Imports of goods and services (annual % growth)(1996)	-2.9	14.8	..	5.7	..	7.0	..	-3.9	15.7	..	..	3.9	1.1	8.9
Manufactures exports (% of merchandise exports)	79.8	92.4	90.2	67.7	84.0	85.5	..	50.3	..	81.5	..	47.3	36.9	42.1
High technology[15] (1996)	10.2	38.7	15.7	19.0	13.5	11.6	13.5	23.8	..	62.4	..	20.2	18.3	20.1
Mean Tariff, % (1997)		7.9	..	12	3.8	3.6	3.6	..	14.4	3.6	4	..	..	
Short term debt (% of gross international reserves)(1996)	7.81	..	1.42	12.46	29.61	..	..	2.75	7.35	..	..	20.10	22.30	
TABLE 9. FINANCE														
Market capitalization of listed co.(% of GDP)(1996)	21.8	28.6	3.6	11.8	32.9	23.7	19.7	23.6	62.7	17.6		40.0	24.2	26.7
Domestic credit provided by banking sector (% of GDP)(1996)	65.4	74.5	36.0	..	78.6	99.7	84.2	74.8	86.1	84.5	..	46.0	70.0	46.7
Liquid liabilities (M3) as % of GDP(1996)	46.6	45.7	38.9	..	77.6	83.0	47.6	61.9	92.2	53.2		35.4	60.5	45.8
Interest rate spread (1996)	..	1.32	8.70	..	5.75	5.42	7.45	..	3.50	5.56	..	11.66	..	14.00
Interest rate spread over LIBOR(1996)	..	3.30	18.21	..	7.03	6.22	15.44	..	3.99	0.34	..	19.97	8.14	24.75
Average Credit Rating (1997)[16]	..	69.7	..	49.7	63.1	71.2	53	..	..	76.7	76.7	..	..	

[a]data are for most recent year available

[1]general public satisfaction/dissatisfaction with the government's economic policies; socioeconomic factors are identified which have the greatest political impact for the country being assessed, ICRG
[2]GCR
[3]government's ability to carry out its declared program(s) and its ability to stay in office, ICRG
[4]extent to which private economic activityis facilitated by a rule-based governance structureCPIA
[5]degree to which public expenditure and investment priorities are established by systematic and objective criteria; whether systems ensure that expenditures match budget allocations, CPIA
[6]efficiency of expenditure balance between and within sectors, and between publicly and privately provided services, CPIA
[7]tax structure (degree of distortionary taxes), revenue collection, tax administration, CPIA
[8]direct and indirect taxes, including social security contributions, WRY
[9]autonomy of bureaucracy from political pressure and established mechanism for recruitment and training, ICRG
[10]public exposure/immunity to political interference, WCY
[11]the degree to which accountability is ensured through audits, inspections etc, conflict if interest regulations for public servants are enforced, civil service promotion and recruitment are merit-based, CPIA
[12]degree of irregular payments in business and official transactions, GCR
[13]perceptions of degree of corruption as seen by business people, TI
[14]total suspended particles, sulfur dioxide, nitrogen dioxide, figure for most polluted city,
[15]include fine chemicals and pharmaceuticals, complex electrical and electronic machinery, aircraft and precision instruments
[16] average of ICRG, Institutional Investors, Euromoney ratings

Source: World Development Indicators 1998, World Bank; Yearbook of Labour Statistics 1998, International Labour Organisation; International Country Risk Guide(ICRG) database; "Structural trends in India's Manufactured Export Performance:International Comparisons, S. Lall; Business Environment Risk Intelligence (BERI) database; Center for Institutional Reform and the Informal Sector (IRIS) database; World Competitiveness Yearbook (WCY); Global Competitiveness Report (GCR);Country Policy Institution Indicators of the World Bank (CPIA); Transparency International (TI), 1998

Annex Table 7: Tunisia -- Key Economic Ratios

DESCRIPTION	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
KEY ECONOMIC RATIOS and LONG-TERM TRENDS, Percentage shares											
Ratio of Gross domestic investment to GDP(MP)	20.7	23.9	32.5	32.1	34.3	29.2	24.5	24.7	25.0	26.7	27.5
Ratio of Exports of goods and services to GDP(MP)	42.0	44.3	43.6	40.4	39.5	40.4	44.9	44.9	42.1	43.9	42.4
Ratio of Gross domestic savings to GDP(MP)	21.1	20.6	25.5	27.1	27.4	21.7	21.5	20.8	23.5	24.2	24.3
Ratio of Gross national savings to GDP(MP)	21.7	20.8	27.1	27.5	26.4	19.8	20.1	20.2	22.4	23.4	24.1
Ratio of Current account balance to GDP(MP)	1.0	-3.1	-5.5	-4.4	-7.0	-8.8	-4.2	-4.3	-2.6	-3.3	-3.4
Ratio of External Interest payments to GDP(MP)	3.7	3.7	3.2	2.9	2.6	2.9	3.0	2.7	2.6	2.5	2.4
Ratio of Total External debt to GDP	67.5	69.1	62.6	63.1	55.1	59.5	61.5	60.5	58.5	59.9	52.6
Ratio of Total External Debt Service to GDP(MP)	10.5	10.9	11.6	10.5	8.7	9.3	9.3	8.2	7.5	7.5	8.2
Ratio of Private Investment(fixed) to GDP(MP)	11.5	12.5	19.7	19.9	20.3	23.5	22.8	19.8	18.5	20.0	18.8
Ratio of Public Investment(fixed) to GDP(MP)	9.0	10.0	11.0	10.2	12.0	4.6	4.2	4.4	4.7	4.6	6.2
Trade Ratio											
Trade Ratio in current LCU, percent	83.7	92.0	94.2	85.7	86.0	88.4	92.7	93.7	85.8	90.3	88.0
Trade Ratio in constant LCU, percent	87.5	94.4	94.2	87.5	89.3	90.0	94.1	94.4	86.3	89.9	89.1
Export of Manufactures per capita, current US $	227.1	263.7	321.4	345.3	364.5	347.4	341.8	419.3	412.3	408.0	406.3
STRUCTURE of the ECONOMY, (% of GDP)											
Agriculture	11.8	12.9	15.7	16.7	16.1	14.7	12.6	11.4	13.7	13.3	12.4
Industry	30.6	31.1	29.8	29.0	28.5	28.1	29.2	29.4	28.5	28.5	28.4
Manufacturing	16.8	17.0	16.9	16.9	16.5	17.2	18.4	19.0	18.3	18.4	18.2
Services	57.6	55.9	54.5	54.3	55.4	57.2	58.3	59.2	57.8	58.1	59.1
Private consumption	62.3	62.1	58.2	56.3	56.6	66.1	66.2	66.7	63.7	62.8	62.7
General government consumption	16.6	17.3	16.4	16.6	16.0	12.2	12.4	12.5	12.8	13.0	13.0
Imports of goods and services	41.7	47.7	50.6	45.3	46.5	48.0	47.9	48.8	43.7	46.4	45.6
GROWTH RATES											
Growth Rate of Population	2.2	1.3	2.5	2.3	2.1	1.9	1.7	1.5	1.5	1.5	1.6
Growth rate of Labour Force	2.2	1.3	2.5	5.2	2.1	1.9	4.5	1.5	4.2	1.5	4.3
Growth rate in GDP(MP)	0.1	1.7	8.0	3.9	7.8	2.2	3.3	2.2	7.1	5.4	5.0
Growth rate in GNP per capita	-4.4	-1.6	5.6	-1.4	2.5	-3.0	-0.1	0.2	3.4	2.9	2.3
Growth rate in Exports of goods and services	21.4	5.0	4.4	-0.9	8.0	3.4	13.0	1.8	-0.8	10.5	3.9
Growth rate of Agriculture	-25.8	10.9	30.3	13.9	5.5	-5.1	-10.0	-9.9	29.6	2.9	-1.0
Growth rate of Industry	2.3	13.9	2.2	3.3	6.9	3.0	6.0	2.7	3.3	5.6	4.9
Growth rate of Manufacturing	3.9	19.1	-21.9	3.9	6.5	4.9	8.1	4.9	2.7	7.1	3.8
Growth rate of Services	6.4	-5.8	6.0	1.4	9.1	4.0	5.6	4.9	4.5	6.0	6.5
Growth rate of Private consumption	1.6	-1.5	9.0	1.3	6.8	10.0	3.2	2.5	2.9	4.3	5.0
Growth rate of General government consumption	0.1	6.4	2.5	4.9	3.1	-21.7	4.3	5.1	9.9	5.0	4.7
Growth rate of Gross domestic investment	-12.2	31.7	21.4	-0.6	19.8	-2.3	-11.5	3.5	11.3	5.6	5.5
Growth rate of Imports of goods and services	16.1	14.6	10.7	-5.6	11.8	2.7	3.5	3.5	-3.3	8.9	4.2
Growth rate of Gross national product	0.2	1.9	9.6	3.3	7.0	0.8	3.4	3.4	6.5	6.0	5.4
PRICES and GOVERNMENT FINANCE											
Inflation (Consumer prices)	7.2	7.7	6.5	8.2	5.8	4.0	4.7	6.3	3.8	3.7	3.1
Inflation (GDP deflator)	7.7	8.8	4.5	7.0	5.7	4.7	4.4	5.5	4.4	4.0	3.6
Export Price Index (annual % change)	3.2	2.9	14.8	1.0	6.2	-7.0	4.8	14.4	3.4	-6.5	-5.2
Import Price Index (annual % change)	4.2	1.8	15.3	1.8	10.3	-10.0	1.2	13.0	0.1	2.4	-7.7
Terms of Trade Index (annual % change)	-1.0	1.1	-0.4	-0.8	-3.7	3.4	3.6	1.2	3.3	-8.8	2.7
Government finance											
(% of GDP, includes current grants)											
Ratio of Current revenue in GDP(MP)	28.3	27.0	26.4	26.4	26.8	27.6	31.7	30.2	30.5	28.7	29.3
Ratio of Current budget balance to GDP(MP)	4.9	1.0	2.3	3.0	4.1	4.8	5.0	3.0	2.4	3.4	4.5
Ratio of Overall budget balance to GDP(MP)	-4.7	-5.3	-6.2	-5.9	-3.1	-3.2	-2.1	-4.2	-4.9	-3.9	-2.4
Share of Governemnt Wages and Salaries in GDP	10.5	11.0	10.6	10.9	10.8	10.9	10.2	10.4	10.3	11.1	11.1
External Debt											
DOD/Exports	160.3	153.4	148.2	161.4	143.0	150.7	139.2	136.8	139.0	136.3	130.6

Annex Table 8: Tunisia -- National Accounts

DESCRIPTION	SCALE	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
NATIONAL ACCOUNTS: Current Prices, LCU												
GDP at market prices	Millions	8661	9590	10816	12029	13706	14663	15807	17052	19066	20901	22724
GDP at factor cost	Millions	7567	8510	9587	10528	11877	14663	15807	17052	19066	20901	22724
Agriculture	Millions	1025	1239	1700	2011	2210	2157	1986	1938	2615	2787	2829
Industry	Millions	2650	2986	3222	3486	3900	4119	4609	5013	5426	5966	6462
Construction	Millions	334	378	440	459	609	726	790	820	844	936	1037
Gas, electricity, water	Millions	754	843	854	889	937	803	830	868	956	1014	1060
Mining and quarrying	Millions	105	139	102	99	88	67	79	91	137	169	219
Manufacturing	Millions	1458	1627	1826	2039	2266	2522	2910	3234	3489	3847	4146
Services, etc	Millions	4986	5365	5894	6532	7596	8387	9212	10101	11025	12148	13433
Resource balance	Millions	31	-318	-762	-596	-950	-1103	-476	-666	-296	-516	-728
Exports of GNFS	Millions	3639	4253	4711	4855	5419	5931	7091	7657	8030	9183	9638
Imports of GNFS	Millions	3608	4571	5473	5452	6368	7033	7567	8323	8326	9699	10366
Total Expenditures	Millions	8629	9908	11578	12625	14656	15766	16283	17718	19362	21417	23452
Total consumption, etc	Millions	6836	7615	8063	8769	9954	11478	12414	13505	14586	15841	17195
Total consumption	Millions	6836	7615	8063	8769	9954	11478	12414	13505	14586	15841	17195
General government	Millions	1436	1656	1769	1993	2193	1787	1956	2133	2434	2719	2948
Private, etc	Millions	5400	5959	6294	6775	7761	9692	10458	11372	12152	13122	14247
Private	Millions	5400	5959	6294	6775	7761	9692	10458	11372	12152	13122	14247
Statistical discrepancy		0	0	0	0	0	0	0	0	0	0	0
Gross domestic investment	Millions	1794	2293	3515	3856	4701	4287	3869	4213	4776	5576	6257
Gross domestic fixed investment	Millions	1779	2157	3317	3621	4428	4122	4268	4121	4422	5136	5690
Nonfinancial public sector	Millions	779	956	1189	1224	1644	681	666	746	902	955	1408
General government	Millions	363	431	504	550	603	681	666	746	902	955	1408
Nonfinancial public enterprises	Millions	416	525	685	673	1040	1558					
Private sector	Millions	1000	1201	2128	2397	2785	3441	3602	3375	3520	4181	4282
Change in stocks	Millions	14	136	198	235	273	165	-399	92	354	440	567
Public sector	Millions											
Private sector	Millions										104	643
Net factor income	Millions	-427	-454	-359	-468	-631	-874	-918	-811	-1004	-998	-988
Net current transfers	Millions	480	478	539	518	504	594	703	712	801	834	942
Gross domestic savings	Millions	1825	1975	2753	3260	3751	3185	3393	3547	4480	5060	5529
Gross national savings	Millions	1878	1998	2933	3310	3624	2904	3178	3448	4277	4896	5483
Public	Millions											
Private	Millions											
Net indirect taxes	Millions	1094	1080	1229	1501	1829	1953	2061	2187	2045	2643	2953
Indirect taxes	Millions											
Subsidies	Millions											
Gross national product	Millions	8234	9136	10457	11561	13075	13788	14889	16241	18062	19903	21736

Annex Table 8: Tunisia -- National Accounts

DESCRIPTION	SCALE	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
NATIONAL ACCOUNTS: Constant Price, LCU												
GDP at market prices	Millions	9847	10019	10816	11238	12115	12381	12789	13075	14009	14761	15493
Net indirect taxes	Millions	1145	1130	1229	1257	1377	1444	1538	1583	1631	1722	1842
GDP at factor cost	Millions	8702	8890	9587	9980	10738	12381	12789	13075	14009	14768	15505
Agriculture	Millions	1176	1305	1700	1937	2043	1939	1746	1573	2038	2098	2077
Industry	Millions	2768	3153	3222	3327	3558	3666	3886	3991	4124	4355	4570
Construction	Millions	#N/A	#N/A	440	437	493	562	622	599	616	659	699
Gas, electricity, water	Millions	#N/A	#N/A	223	224	233	901	881	877	921	944	991
Mining and quarrying	Millions	805	816	734	769	812	84	91	111	118	107	135
Manufacturing	Millions	1963	2337	1826	1898	2020	2120	2292	2404	2469	2645	2745
Services, etc	Millions	5903	5561	5894	5974	6515	6775	7157	7511	7847	8315	8858
Resource balance	Millions	-17	-432	-762	-496	-728	-716	-243	-350	-187	-104	-128
Exports of GNFS	Millions	4299	4512	4711	4670	5044	5214	5894	5999	5953	6581	6838
Imports of GNFS	Millions	4316	4945	5473	5165	5772	5930	6137	6349	6140	6685	6966
Total Expenditures	Millions	9864	10451	11578	11733	12843	13097	13032	13425	14196	14865	15621
Total consumption, etc	Millions	8033	8039	8650	8825	9359	9692	10018	10306	10724	11198	11752
Total consumption	Millions	8033	8039	8650	8825	9359	9692	10018	10306	10724	11198	11752
General government	Millions	1621	1725	1769	1856	1913	1499	1564	1643	1806	1896	1985
Private, etc	Millions	6412	6314	6881	6968	7446	8193	8454	8663	8918	9301	9767
Private	Millions	6412	6314	6881	6968	7446	8193	8454	8663	8918	9301	9767
Statistical discrepancy		0	0	0	0	0	0	0	0	0	0	0
Gross domestic investment	Millions	1831	2412	2928	2909	3484	3405	3014	3119	3472	3668	3869
Gross domestic fixed investment	Millions	1905	2321	2635	2687	3181	3088	3332	3113	3181	3505	3642
Nonfinancial public sector	Millions											
Change in stocks	Millions	-74	91	293	221	303	317	-318	6	291	162	227
Net factor income	Millions	-487	-482	-359	-437	-557	-726	-735	-614	-736	-693	-658
Net current transfers	Millions	548	504	539	481	441	494	563	539	587	579	627
Gross national product	Millions	9360	9537	10457	10801	11558	11654	12054	12461	13273	14069	14835
Gross domestic savings	Millions	1869	2068	2165	2344	2623	2475	2628	2611	3254	3312	3380
Gross national savings	Millions	1930	2090	2346	2388	2507	2242	2456	2536	3105	3198	3349
Capacity to import	Millions	4354	4601	4711	4600	4911	5000	5751	5841	5922	6329	6477
Terms of trade adjustment	Millions	55	88	0	-69	-133	-214	-143	-158	-31	-252	-361
Gross domestic income	Millions	9902	10107	10816	11169	11982	12167	12646	12917	13978	14510	15132
Gross national income	Millions	9415	9625	10457	10732	11425	11441	11911	12302	13242	13817	14473

Annex Table 9: Tunisia -- Balance of Payments

DESCRIPTION	SCALE	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
MERCHANDISE TRADE: EXPORTS												
Total Merchandise Exports (fob, US$)	Millions	2396.3	2930.7	3516.6	3707.9	4013.7	3753.6	4643.0	5469.0	5519.0	5679.0	5722.0
Fuel	Millions	385.4	585.1	607.3	529.4	608.8	453.7	437.0	462.0	578.0	555.9	367.0
Agriculture	Millions	180.7	197.1	240.0	249.7	251.1	245.2	274.9	245.2	187.0	283.4	193.5
Phosphates	Millions	45.5	49.5	47.8	49.1	51.3	42.4	44.4	64.2	70.4	69.9	47.4
Manufactures	Millions	1784.7	2099.0	2621.3	2879.6	3102.4	3012.3	3012.4	3749.4	3742.1	3759.4	3803.6
Other Exports	Millions							874.2	948.2	941.5	1010.4	1310.5
Total Merchandise Exports (fob, 1987 US$)	Millions	2832.8	3365.5	3516.6	3672.0	3742.2	3763.2	3857.7	4249.5	4029.6	3904.5	3981.7
Fuel	Millions	574.1	721.2	607.3	579.0	637.8	564.7	503.5	558.0	572.7	468.0	439.9
Agriculture	Millions	202.2	206.1	240.0	244.9	251.6	293.2	247.5	183.2	127.1	213.4	217.7
Phosphates	Millions	64.6	65.6	47.8	49.4	54.4	59.0	45.6	51.0	52.2	45.6	46.5
Manufactures	Millions	1991.9	2372.6	2621.4	2798.7	2798.4	2846.3	2297.3	2717.4	2594.3	2455.2	2516.6
Other Exports	Millions							809.4	790.9	735.5	767.9	
MERCHANDISE TRADE: IMPORTS												
Total Merchandise Imports (cif, US$)	Millions	3691.9	4372.3	5524.5	5179.5	6431.8	6202.0	6210.0	7458.0	7280.0	8106.0	7872.0
Food	Millions	554.2	578.3	505.9	336.3	429.7	416.6	536.0	814.7	712.0	745.4	655.0
Other Consumer Goods	Millions	932.5	1122.6	1570.4	1522.9	1894.7	1938.9	1900.6	2314.5	2171.0	2498.5	2777.9
POL and Other Energy	Millions	243.4	379.6	486.8	395.6	449.0	455.4	466.0	541.0	607.0	644.0	374.8
Intermediate Goods	Millions	1344.2	1455.8	1726.4	1620.9	2080.7	1822.2	1874.7	2271.8	2229.0	2358.2	2249.8
Capital Goods	Millions	617.5	835.9	1235.0	1303.8	1577.7	1568.9	1432.6	1515.9	1561.0	1859.8	1814.4
Total Merchandise Imports (cif, 1987 US$)	Millions	4331.9	5040.5	5524.5	5089.5	5728.8	6140.5	6077.8	6460.1	5761.0	5787.0	6640.6
Food	Millions	716.2	625.1	505.9	326.2	397.7	407.0	492.9	666.1	476.0	443.0	497.2
Other Consumer Goods	Millions	1057.5	1298.3	1570.4	1491.2	1504.4	1804.5	2014.2	2076.0	1895.9	1667.5	2052.7
POL and Other Energy	Millions	362.1	490.5	486.8	422.6	486.2	566.3	622.0	666.0	573.0	580.0	653.5
Intermediate Goods	Millions	1496.0	1660.0	1726.4	1572.7	1792.6	1680.2	1665.4	1821.9	1717.1	1751.5	1997.1
Capital Goods	Millions	700.2	966.6	1235.0	1276.8	1548.0	1682.5	1283.3	1230.1	1099.0	1345.0	1440.0
MERCHANDISE TRADE: Price Indices (1987=100)												
Merchandise Export Price Index		103.2	106.2	122.0	123.2	130.9	121.7	127.5	145.8	150.8	140.9	133.6
Merchandise Import Price Index		104.2	106.1	122.3	124.5	137.3	123.5	125.0	141.2	141.3	144.8	133.7
Merchandise Terms of Trade		99.0	100.2	99.8	99.0	95.3	98.5	102.0	103.3	106.7	97.3	99.9

Annex Table 10: Tunisia -- Government Finances

DESCRIPTION	SCALE	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
GOVERNMENT FINANCE: Overall												
Overall Surplus/Deficit	Millions	-411	-504	-668	-713	-429	-474	-329	-715	-936	-805	-555
Total Revenues, incl. current Grants	Millions	2507	2739	2934	3208	3730	4083	5008	5150	5828	5999	6668
Expenditures and Net Lending	Millions				3830	4144	4497	5337	5865	6764	6804	7223
Overall Surplus/Deficit, excl. current Grants	Millions	-411	-504	-668	-713	-429	-474	-393	-760	-978	-871	-644
GOVERNMENT FINANCE: Current Revenue/Expenditure												
Current Budget Balance, incl. current Grants	Millions	425	100	253	361	559	706	794	510	449	710	1019
Total Current Revenues, incl. current Grants	Millions	2452	2593	2859	3173	3675	4050	5004	5147	5811	5992	6663
Total Current Revenues, excl. current grants	Millions	2358	2487	2745	3173	3675	4050	4940	5102	5769	5926	6574
Direct Taxes	Millions	320	362	403	504	563	701	1535	1702	2033	2262	2560
Indirect Taxes	Millions	1347	1548	1726	1958	2246	2378	2427	2561	2743	2962	3323
On domestic goods & services	Millions	954	1090	1230	1388	1630	1723	1586	1649	1855	2112	2438
On international trade	Millions	393	458	496	534	572	610	771	815	782	736	751
Nontax Receipts	Millions	691	578	616	711	865	972	978	839	993	702	691
Grants, total current	Millions							64	45	42	66	89
Total Current Expenditures	Millions	2026	2493	2606	2812	3116	3345	4210	4637	5362	5282	5644
Interest on External Debt	Millions	180	209	222	200	250	281	267	339	475	317	257
Interest on Domestic Debt	Millions	76	87	104	153	193	238	321	345	350	403	435
Other Current Transfers	Millions	104	136	147	166	188	194	1347	1474	1685	1465	1656
o/w Transfers to NFPS	Millions											
Subsidies	Millions	449	643	597	560	552	625	319	346	418	378	348
Consumption	Millions	1217	1417	1536	1732	1933	2077	1956	2133	2434	2719	2948
Wages and Salaries	Millions	913	1054	1148	1311	1481	1598	1609	1776	1969	2320	2533
GOVERNMENT FINANCE: Capital Receipts/Payments												
Total Capital Revenues	Millions	55	146	75	35	56	33	4	3	17	7	5
Total Capital Expenditures and Net Lending	Millions	481	574	828	870	864	960	1127	1228	1402	1522	1579
Capital Transfers	Millions	170	195	321	369	300	330	461	482	500	567	171
Budgetary Investment	Millions	312	379	507	501	564	629	666	746	902	955	1408
Total Deficit Financing	Millions	411	504	668	713	429	474	314	699	925	803	136
External Capital Grants	Millions											
External Borrowing (net)	Millions	311	269	232	286	141	175	218	490	526	492	4
Monetary System Credit (net)	Millions							-78	-89	-102	299	-114
Other Domestic Borrowing (net)	Millions	100	234	436	427	288	299	174	298	501	12	246
GOVERNMENT FINANCE: Debt (at end year)												
Total Government Debt (LCUs)	Millions				7198	7607	8697	9358	9958	11554	13063	13203
External Debt	Millions	3454	3728	3385	4870	4958	5710	6170	6556	6969	8048	9889
Domestic To Monetary System	Millions								1316	1271	1636	4155
Domestic Debt:	Millions	-4131	-4358	-4692	2329	2649	2986	3166	3421	3857	4199	-577
GOVERNMENT FINANCE: Other Series												
Primary Deficit, excluding interest	Millions											
External Debt (US$)	Millions	3844	4121	4642	5060	5321	5778					

Annex Table 11: Tunisia -- Monetary Statistics

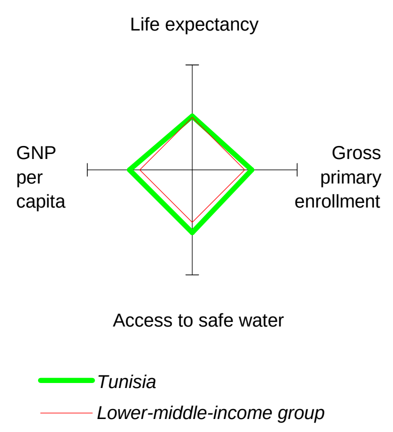
DESCRIPTION	SCALE	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
MONEY & CREDIT: Annual Flows (LCU)												
Net Foreign Assets	Millions	5131.0	136.0	-72.0	-67.0	43.0	-6.0	324.0	-42.0	295.0	373.0	-158.0
Net Domestic Credit	Millions	-507.0	1152.0	227.0	776.0	1052.0	-263.2	493.2	718.0	1179.0	1281.0	754.0
To Government	Millions	258.5	114.0	87.0	100.0	-230.0	-411.1	-77.9	-89.0	-102.0	299.0	-114.0
Government Budget	Millions	258.5	114.0	87.0	100.0	-230.0	-1056.6	-98.4	52.0	-98.0	-24.0	10.0
Other Official Entities	Millions							20.5	-141.0	-4.0	323.0	-124.0
To Rest of Economy	Millions	-765.5	1038.0	140.0	676.0	1282.0	147.9	571.1	807.0	1281.0	982.0	868.0
Private Sector	Millions	-765.5	1038.0	140.0	676.0	1282.0	52.9	646.1	812.0	323.0	1067.0	949.0
Other financial institutions	Millions						95.0	-75.0	-5.0	958.0	-85.0	-81.0
Total Assets & Liabilities	Millions	288.7	1288.0	155.0	709.0	1095.0	-269.2	817.2	676.0	1474.0	1654.0	596.0
Money and Quasimoney	Millions	667.0	694.0	367.0	316.0	434.0	27.0	493.0	410.0	983.0	1352.0	505.0
Demand deposits	Millions										797.0	745.0
Time deposits	Millions										812.2	451.2
Net Other Liabilities	Millions	-378.3	594.0	-212.0	393.0	661.0	-296.2	324.2	266.0	491.0	302.0	91.0
MONEY & CREDIT: End-of-Year Stocks (LCU)												
Net Foreign Assets	Millions	527.0	663.0	591.0	524.0	567.0	561.0	885.0	843.0	1138.0	1511.0	1353.0
Net Domestic Credit	Millions	5131.0	6283.0	6510.0	7286.0	8338.0	8074.8	8568.0	9286.0	10465.0	11746.0	12500.0
To Government	Millions	980.0	1094.0	1181.0	1281.0	1051.0	639.9	562.0	473.0	371.0	670.0	556.0
Government Budget	Millions	980.0	1094.0	1181.0	1281.0	1051.0	-5.6	-104.0	-52.0	-150.0	-174.0	-164.0
Other Official Entities	Millions						645.5	666.0	525.0	521.0	844.0	720.0
To Rest of Economy	Millions	4151.0	5189.0	5329.0	6005.0	7287.0	7434.9	8006.0	8813.0	10094.0	11076.0	11944.0
Private Sector	Millions	4151.0	5189.0	5329.0	6005.0	7287.0	7339.9	7986.0	8798.0	9121.0	10188.0	11137.0
Other financial institutions	Millions						95.0	20.0	15.0	973.0	888.0	807.0
Total Assets & Liabilities	Millions	5658.0	6946.0	7101.0	7810.0	8905.0	8635.8	9453.0	10129.0	11603.0	13257.0	13853.0
Money and Quasimoney	Millions	4480.0	5174.0	5541.0	5857.0	6291.0	6318.0	6811.0	7221.0	8204.0	9556.0	10061.0
Other Liabilities	Millions	1178.0	1772.0	1560.0	1953.0	2614.0	2317.8	2642.0	2908.0	3399.0	3701.0	3792.0
MONEY & CREDIT: Memorandum Items:												
Net International Reserves (end year - US$)	Millions	0.0	1262.4	1125.3	996.5	1079.1	-1448.9	18971.4	20257.5	22840.9	30185.3	2812.0
MONEY & CREDIT: Real Interest Rates												
Real discount interest rate (IFS, line 60 deflated by CPI)	Percent	10.6	12.1	11.9	11.0	9.9	7.5	7.1	6.7	5.7		
Real money market interest rate (IFS, line 60b deflated by CF	Percent	10.5	10.0	11.5	10.9	10.2	8.8	7.1	6.6	6.3	4.8	4.7
MONEY & CREDIT: Nominal Interest Rates												
Discount interest rate, (nominal) (IFS line 60), (percent)	Units	9.3	11.4	11.9	11.9	11.4	8.9	8.9	8.9	7.9		
Money market interest rate (IFS line 60b) (percent)	Units	9.2	9.4	11.5	11.8	11.7	10.5	8.8	8.8	8.6	6.9	6.9

Annex Table 12: Tunisia -- Key Prices

DESCRIPTION	SCALE	YR88	YR89	YR90	YR91	YR92	YR93	YR94	YR95	YR96	YR97	YR98
PRICES: Exchange Rates (LCU per US$)												
Nominal official (average)(rf)		0.860	0.950	0.880	0.920	0.884	1.004	1.012	0.946	0.973	1.106	1.139
Nominal official (end-of-year)(ae)		0.900	0.900	0.840	0.951	1.047	0.991	0.991	0.951	0.999	1.148	1.101
IEC conversion factor (Atlas)	Units	0.860	0.950	0.880	0.920	0.884	1.004	1.012	0.946	0.973	1.106	1.139
PRICES: Price Indices												
Real effective exchange rate (IMF)		104.6	102.9	100.0	101.0	103.1	101.7	97.9	100.0	100.7	100.6	100.5
Consumer price index (1990=100)		87.2	93.9	100.0	108.2	114.5	119.1	124.7	132.6	137.6	142.7	147.1
GDP at market prices deflator (end period) (1990=10	Units	88.0	95.7	100.0	107.0	113.1	118.4	123.6	130.4	136.1	141.6	146.7
MUV-Manuf. (% change)												-3.900
PRICES: Other Series												
London gold price (US$ per ounce)		410.3	381.3	385.0	353.6	333.3	390.7	383.4	386.8	369.3		

Tunisia at a glance

POVERTY and SOCIAL	Tunisia	M. East & North Africa	Lower-middle-income
1998			
Population, mid-year *(millions)*	9.4	285	908
GNP per capita *(Atlas method, US$)*	2,050	2,050	1,710
GNP *(Atlas method, US$ billions)*	19.2	586	1,557
Average annual growth, 1992-98			
Population *(%)*	1.6	2.2	1.1
Labor force *(%)*	2.9	3.0	1.5
Most recent estimate (latest year available, 1992-98)			
Poverty *(% of population below national poverty line)*	7.6	..	..
Urban population *(% of total population)*	64	58	58
Life expectancy at birth *(years)*	70	67	68
Infant mortality *(per 1,000 live births)*	30	49	38
Child malnutrition *(% of children under 5)*	9	14	..
Access to safe water *(% of population)*	90	81	75
Illiteracy *(% of population age 15+)*	33	38	14
Gross primary enrollment *(% of school-age population)*	117	96	103
Male	120	103	105
Female	113	89	100

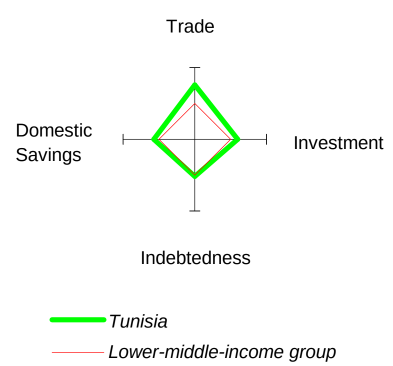


Development diamond*

KEY ECONOMIC RATIOS and LONG-TERM TRENDS

	1978	1988	1997	1998
GDP *(US$ billions)*	6.0	10.1	18.9	20.0
Gross domestic investment/GDP	30.8	20.7	26.7	27.5
Exports of goods and services/GDP	31.0	42.0	43.9	42.5
Gross domestic savings/GDP	23.0	21.1	24.2	24.5
Gross national savings/GDP	..	21.7	23.4	24.1
Current account balance/GDP	-9.2	1.0	-3.3	-3.4
Interest payments/GDP	1.8	3.7	2.5	2.8
Total debt/GDP	49.3	67.5	59.9	52.6
Total debt service/exports	12.4	21.9	15.3	17.4
Present value of debt/GDP	..	..	55.7	..
Present value of debt/exports	..	..	114.2	..

	1978-88	1988-98	1997	1998	1998-02
(average annual growth)					
GDP	3.9	4.6	5.4	5.0	5.8
GNP per capita	1.1	2.7	4.4	3.8	4.1
Exports of goods and services	3.8	4.8	10.5	3.9	5.0

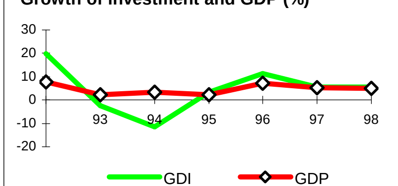


Economic ratios*

STRUCTURE of the ECONOMY

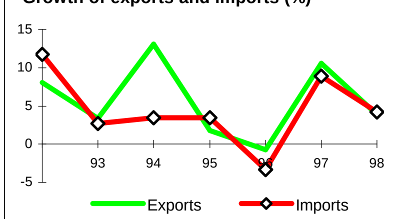
	1978	1988	1997	1998
(% of GDP)				
Agriculture	15.1	11.8	13.3	12.4
Industry	26.4	30.6	28.5	28.4
Manufacturing	11.1	16.8	18.4	18.2
Services	58.5	57.6	58.1	59.1
Private consumption	60.7	62.3	62.8	62.5
General government consumption	16.3	16.6	13.0	13.0
Imports of goods and services	38.7	41.7	46.4	45.5

Growth of investment and GDP (%)



	1978-88	1988-98	1997	1998
(average annual growth)				
Agriculture	2.7	4.4	2.9	-1.0
Industry	3.6	4.6	5.6	4.9
Manufacturing	5.6	3.4	7.1	3.8
Services	4.4	4.7	6.0	6.5
Private consumption	4.4	4.6	4.3	5.0
General government consumption	5.0	0.9	5.0	4.7
Gross domestic investment	-2.1	5.5	5.6	5.5
Imports of goods and services	1.3	4.1	8.9	4.2
Gross national product	3.8	4.6	6.0	5.4

Growth of exports and imports (%)

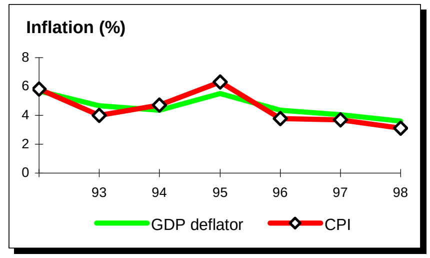


* The diamonds show four key indicators in the country (in bold) compared with its income-group average. If data are missing, the diamond will be incomplete.

Tunisia

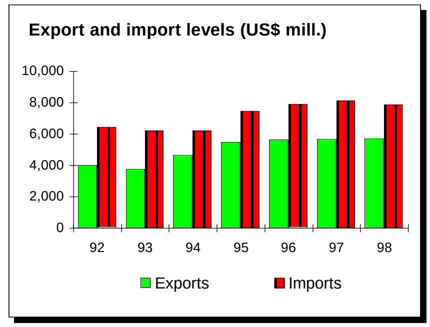
PRICES and GOVERNMENT FINANCE

	1978	1988	1997	1998
Domestic prices				
(% change)				
Consumer prices	..	7.2	3.7	3.1
Implicit GDP deflator	6.5	7.7	4.0	3.6
Government finance				
(% of GDP, includes current grants)				
Current revenue	..	28.3	28.7	29.0
Current budget balance	..	4.9	3.4	4.2
Overall surplus/deficit	..	-4.7	-3.9	-2.4



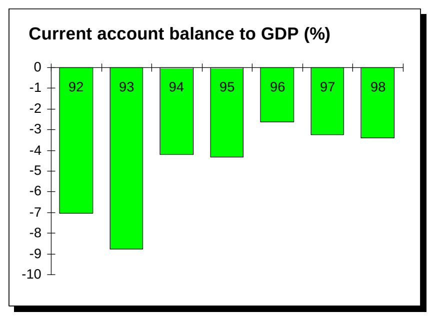
TRADE

	1978	1988	1997	1998
(US$ millions)				
Total exports	1,126	2,396	5,679	5,722
Fuel	433	385	556	367
Agriculture	57	181	283	193
Manufactures	590	1,785	3,759	3,804
Total imports	2,162	3,692	8,106	7,872
Food	254	554	745	655
Fuel and energy	226	243	644	375
Capital goods	678	618	1,860	1,814
Export price index *(1995=100)*	..	..	97	92
Import price index *(1995=100)*	..	..	103	95
Terms of trade *(1995=100)*	..	..	94	97



BALANCE of PAYMENTS

	1978	1988	1997	1998
(US$ millions)				
Exports of goods and services	1,848	4,242	8,304	8,479
Imports of goods and services	2,423	4,206	8,771	9,077
Resource balance	-575	36	-467	-598
Net income	-216	-498	-903	-858
Net current transfers	240	558	754	776
Current account balance	-551	96	-615	-680
Financing items (net)	651	282	951	493
Changes in net reserves	-100	-378	-336	187
Memo:				
Reserves including gold *(US$ millions)*	..	..	1,989	1,854
Conversion rate *(DEC, local/US$)*	0.4	0.9	1.1	1.1



EXTERNAL DEBT and RESOURCE FLOWS

	1978	1988	1997	1998
(US$ millions)				
Total debt outstanding and disbursed	2,941	6,799	11,321	10,489
IBRD	189	1,019	1,434	1,458
IDA	67	62	45	43
Total debt service	260	1,058	1,413	1,632
IBRD	28	199	265	265
IDA	2	2	3	2
Composition of net resource flows				
Official grants	28	124	95	82
Official creditors	170	209	104	-136
Private creditors	335	37	587	194
Foreign direct investment	91	110	355	697
Portfolio equity	0	0	0	0
World Bank program				
Commitments	67	241	167	222
Disbursements	35	173	127	141
Principal repayments	13	112	175	178
Net flows	22	61	-48	-37
Interest payments	16	89	103	89
Net transfers	5	-28	-151	-126