IMF Country Reports 16/138

Tunisia: Request for an Extended Arrangement Under the Extended Fund Facility-Press Release; Staff Report; and Statement by the Executive Director for Tunisia

INTERNATIONAL MONETARY FUND

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IMF Country Report No. 16/138

TUNISIA

June 2016

REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR TUNISIA

In the context of the Request for an Extended Arrangement under the Extended Fund Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on May 20, 2016, following discussions that ended on March 3, 2016, with the officials of Tunisia on economic developments and policies underpinning the IMF arrangement under the Extended Fund Facility. Based on information available at the time of these discussions, the staff report was completed on May 2, 2016.
- A **Staff Supplement** updating information on recent developments.
- A **Statement by the Executive Director** for Tunisia.

The documents listed below have been or will be separately released:

Letter of Intent sent to the IMF by the authorities of Tunisia*
Memorandum of Economic and Financial Policies by the authorities of Tunisia*
Technical Memorandum of Understanding*
*Also included in Staff Report

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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International Monetary Fund
Washington, D.C.

Press Release No. 16/238
FOR IMMEDIATE RELEASE
May 20, 2016

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$2.9 billion Extended Arrangement under the Extended Fund Facility for Tunisia

The Executive Board of the International Monetary Fund (IMF) today approved a 48-month extended arrangement under the Extended Fund Facility (EFF) with Tunisia for an amount equivalent to SDR 2.04 billion (about US$2.9 billion, or 375 percent of Tunisia's quota) to support the country's economic and financial reform program detailed in the authorities' economic vision. This program aims at promoting stronger and more inclusive growth by consolidating macroeconomic stability, reforming public institutions—including the civil service, facilitating financial intermediation, and improving the business climate. Following the Board's decision, an amount equivalent to SDR 227.29 million (about US$319.5 million) is available for immediate disbursement; the remaining amount will be phased in over the duration of the program, subject to eight program reviews.

Following the Executive Board discussion on Tunisia, Mr. Mitsuhiro Furusawa, Deputy Managing Director, and Acting Chair, said:

"Tunisia's economy has shown resilience but continues to face important fiscal, external, structural, and social challenges. Macroeconomic stability has been preserved and important reforms have been initiated, including with the support of the recently expired Fund-supported program.

"The authorities have developed a comprehensive and new economic program—to be supported by a four-year Extended Fund Facility—to address remaining vulnerabilities. The program aims at consolidating macroeconomic stability and promoting more inclusive growth. Strong commitment to sound policies, early and decisive action on key structural reforms, and consensus-building and communication efforts, particularly on socially difficult reforms, are crucial to create jobs and yield the largest gains for Tunisia's population.

"A prudent fiscal policy that puts public debt on a downward path will help ease financing constraints, reduce external imbalances, and ensure sustainability. A comprehensive civil service reform will improve public service delivery and increase fiscal space for priority investment and well-targeted social spending. A more progressive and efficient tax system

will broaden the tax base and improve equity. Fiscal risks should continue to be monitored; and governance efforts, accelerated.

“Enhanced central bank independence will strengthen the effectiveness of monetary policy, while greater exchange rate flexibility will strengthen reserve buffers and facilitate external adjustment.

“The adoption of critical banking sector legislation is welcome. Further action is needed to restructure public banks and strengthen the banking resolution and supervision frameworks. Developing credit bureaus and relaxing caps on lending rates will increase access to finance.

“Efforts to streamline existing business procedures and enhance market access through a new investment code and the implementation of the competition law and the law on public-private partnerships are essential to promote private-sector development and create jobs.”

ANNEX

Recent Economic Developments

With the implementation of the IMF-supported Stand-By Arrangement (SBA) that expired in December 2015, Tunisia has managed to preserve macroeconomic stability and initiate fiscal and banking reforms in a context marked by a prolonged political transition, spillovers from the crisis in Libya, and numerous exogenous shocks, including terror attacks. However, important challenges remain: economic activity is weak, employment is low, social tensions linger, spending composition has deteriorated, and external imbalances are high.

To tackle these challenges, the authorities formulated in 2015 a five-year economic vision, which is being developed into a detailed plan. This vision aims at promoting stronger and more inclusive growth by transforming Tunisia’s growth model through a strategy based on macroeconomic stability and including five pillars: effective public institutions; economic diversification; human development and social inclusion; regional development; and green economic growth.

Program Summary

The new program aims at achieving more inclusive growth and create jobs, with implementation centered around four pillars: i) consolidating macroeconomic stability; ii) reforming public institutions, iii) promoting financial intermediation, iv) and improving the business climate.

Consolidating macroeconomic stability. Key measures include: (i) an appropriate fiscal policy that creates space for priority capital spending and aims at putting public debt on a

downward path; (ii) a prudent monetary policy aimed at containing inflation; and (iii) greater exchange rate flexibility that preserves reserves in the face of important exogenous shocks.

Reforming public institutions and modernizing the public administration to improve its efficiency and effectiveness and support inclusive growth remains a priority. The policy package will include reforming civil service to improve public service delivery and help contain the wage bill, progressing with energy subsidy reform while strengthening the social safety net, fostering the monitoring and performance of the State Owned Enterprises (SOEs), boosting equity-friendly revenue mobilization, and strengthening public financial management and transparency efforts, including through enhanced anti-corruption initiatives.

Promoting financial intermediation. Important steps have been taken towards establishing a modern banking system, subject to strong supervision and competition. The new program will include measures aimed at strengthening banking sector resilience and promoting financial intermediation. This requires continued progress on public bank restructuring, a risk-based supervision system, a proper resolution framework, and strengthened regulations. All these reforms, and the implementation of the new bankruptcy law, will help banks actively resolve their non-performing loans. Financial inclusion will be helped through the development of microfinance institutions.

Improving the business climate. Key measures include improving the adoption of a new investment code, the streamlining of tax incentives, and the simplification of procedures to reduce entry barriers and protect investor rights. The simplification of about 530 tax, customs, and business formalities completed over the past two years are expected to reduce administrative burden faced by businesses and increase government efficiency. Labor market reform will proceed gradually by building upon consensus amongst stakeholders to finalize a national employment strategy to address the main labor market issues including skills mismatch and worker protection.

Tunisia: Selected Economic and Financial Indicators, 2012–17

	2012	2013	2014	2015	2016	2017
				Pre.	Proj.	
Production and income (percent change)						
Real GDP	3.9	2.4	2.3	0.8	2.0	3.0
GDP deflator	5.0	4.3	5.2	4.9	5.1	3.3
Consumer price index (CPI), average	5.1	5.8	4.9	4.9	3.9	3.9
Consumer price index (CPI), end of period	5.9	5.7	4.8	4.1	4.0	3.9
Gross national savings (in percent of GDP)	16.1	14.4	14.0	12.9	14.1	15.3
Gross investment (in percent of GDP)	24.4	22.7	23.2	21.8	21.8	22.3
Central government (percent of GDP, unless indicated otherwise 1/						
Total revenue (excluding grants)	24.0	24.9	25.4	23.0	23.9	24.1
Total expenditure and net lending	29.8	32.4	29.7	28.5	28.5	28.0
Central government overall balance (excluding grants)	-5.8	-7.5	-4.3	-5.5	-4.6	-3.9
Central government overall balance (excluding grants, cash basis)	-5.5	-9.8	-5.4	-4.7	-4.6	-3.9
Structural fiscal balance 2/	-5.7	-6.4	-4.3	-4.3	-4.0	-3.3
Change in the structural fiscal balance (+: improvement)	-2.4	-0.7	2.1	0.0	0.3	0.7
Central government debt (foreign and domestic)	45.5	44.5	49.0	53.2	54.6	54.5
Foreign currency public debt (percent of total debt)	61.6	59.6	62.6	62.6	68.0	68.6
Total external debt						
External debt (US$ billions)	24.0	26.0	26.7	26.7	29.3	30.7
External debt (in percent of GDP)	52.9	57.0	61.4	63.5	69.0	71.4
Debt service ratio (percent of exports of GNFS)	12.1	9.5	8.4	10.2	12.8	16.7
Money and credit (percent change)						
Credit to the economy	8.8	6.8	9.4	6.4	7.1	7.3
Broad money (M3 of the financial system)	8.4	6.6	7.8	5.3	6.5	6.8
Velocity of circulation (GDP/M2)	1.46	1.45	1.45	1.46	1.47	1.46
External sector (percent change)						
Exports of goods, f.o.b. (in $)	-4.6	0.3	-1.9	-15.9	-2.6	5.8
Imports of goods, f.o.b. (in $)	2.1	-0.5	1.8	-18.4	-4.3	3.9
Exports of goods, f.o.b. (volume)	1.6	-0.7	-2.9	-2.8	1.6	5.5
Import of goods, f.o.b. (volume)	9.0	-0.5	2.1	-1.7	3.5	2.1
Trade balance (in percent of GDP)	-13.6	-12.8	-14.0	-11.5	-10.4	-10.1
Current account (in percent of GDP)	-8.3	-8.4	-9.1	-8.9	-7.7	-7.0
Foreign direct investment, net (in percent of GDP)	1.5	1.1	2.3	2.5	2.1	2.2
Terms of trade (deterioration -)	0.2	1.1	1.4	4.2	3.7	-1.5
Official reserves						
Gross official reserves (US$ billions, e.o.p)	8.7	7.7	7.7	7.6	8.3	8.5
In months of next year's imports of goods and services, c.i.f.	3.9	3.4	4.2	4.3	4.6	4.5
Memorandum items:						
GDP at current prices (TD millions)	70,354	75,152	80,816	85,491	91,658	97,495
GDP at current prices (US$ billions)	45.0	46.3	47.6	43.6	44.0	44.4
Real effective exchange rate (percent change, depreciation -) 3/	-1.49	-1.90	-0.20	...	...	...
Interest rate (money market rate, in percent, e.o.p)	3.3	4.8	4.7	...	...	...
Stock market TUNINDEX (12/31/1997=1000)	4,580	4,381	4,674	...	...	...

Sources: Tunisian authorities; and IMF staff estimates and projections.

1/ Excludes the social security accounts.

2/ Excludes banking recapitalization costs and one-off arrears payments for energy subsidies. Different figures from sixth SBA review account for updated output gap estimation.

3/ Information Notice System.

INTERNATIONAL MONETARY FUND

TUNISIA

May 2, 2016

REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY

EXECUTIVE SUMMARY

Context. With support from the Stand-By Arrangement (SBA) that expired in December 2015, Tunisia has managed to preserve macroeconomic stability and initiate fiscal and banking reforms in a context marked by a prolonged political transition, spillovers from the crisis in Libya, and numerous exogenous shocks, including terror attacks. However, important vulnerabilities remain: economic activity is weak, employment is low, social tensions linger, spending composition has deteriorated, and external imbalances are high.

The authorities' program. To tackle these challenges, the authorities formulated in 2015 their five-year economic vision 2016–20, which is being developed into a detailed plan. The authorities' vision aims at promoting stronger and more inclusive growth by transforming Tunisia's growth model through a strategy predicated on macroeconomic stability and including five pillars: effective public institutions; economic diversification; human development and social inclusion; regional development; and green economic growth. To help realize this vision, the proposed program would focus on promoting inclusive growth by consolidating macroeconomic stability, reforming public institutions—including the civil service, facilitating financial intermediation, and improving the business climate.

EFF Request. In support of their program, the Tunisian authorities have requested a four-year Extended Fund Facility, in the amount of SDR 2.046 billion (375 percent of quota, US$2.8 billion), with 41 percent of quota available upon Board approval. The size and timing of disbursements should ensure that the arrangement provides enough buffers in case external shocks materialize.

Risks. The proposed arrangement faces risks stemming from security and social tensions, political instability, and opposition by vested interests. Slower growth in Europe or a rebound in international oil prices could exacerbate vulnerabilities. The commitment of the authorities and of a broad spectrum of stakeholders to the reform agenda is essential to avoid delays and reversals in program implementation.

Approved By
Daniela Gressani and Sanjaya Panth

The team comprised Amine Mati (head), Maria Mendez, Andrea Gamba and Gomez Agou (all MCD); Amr Hosny (SPR), Franck Dupont and Thierry Bayle (MCM), Robert Blotevogel (Resident Representative) and Adnen Lassoued (local economist). Ms. Saadaoui and Mr. Jbili (OED) participated in the discussions. During the missions on December 9-18, 2015 and on February 18-March 3, 2016 staff met with the Governor of the Central Bank, the Minister of Finance, the Minister of Development and International Cooperation, the Minister of Energy, Industry and Mines, the Minister of Social Affairs, the Minister of Tourism, the Minister in charge of Economic Affairs at the Prime Ministry, and other senior officials, and representatives of workers' unions, the corporate and banking sector, the diplomatic and donor community, political parties, civil society, academia, media, and parliament.

Kadia Kebet, Geraldine Cruz, Rafik Selim, Greg Auclair, and Samira Kalla provided excellent assistance.

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APPENDIX

BACKGROUND

1. **Tunisia's vulnerabilities have been reduced in recent years, but important challenges remain.** The policies supported by the recently expired SBA—which were impacted by a protracted political transition, social unrest, and security incidents—led to gradual fiscal consolidation, reduced inflation, stable reserve buffers, stronger monetary policy framework, and a reduction in banking sector vulnerabilities (Annex I). However, growth has remained below expectations, productivity is declining, unemployment remains high, budget composition has worsened, the dinar remains overvalued, banking sector fragilities remain, and progress on business climate reforms has been uneven.

2. **The end of the political transition renewed the reform momentum.** The broad-based coalition government that took office in February 2015 has successfully pushed ahead with a number of longstanding legislation critical for private investment, leading to the adoption of laws on competition, PPPs, central bank statutes, and bankruptcy procedures. The creation of a reform coordination unit at the Prime Ministry's office in December 2015 is helping to align the legislative calendar with the government's economic priorities.

3. **The Tunisian authorities formulated a new economic vision to modernize the country's growth model and reduce vulnerabilities.** Based on a comprehensive diagnostic, the authorities' five-year economic vision (Box 1) aims at maintaining macroeconomic stability and generating stronger and more inclusive growth through: (i) transparent and effective public institutions; (ii) economic diversification; (iii) human development and social inclusiveness; (iv) reduced regional disparities; and (v) green economic growth. This economic vision—accompanied by a published plan of major reforms—will be fully fleshed out in the forthcoming five-year development plan, which is expected to be approved in June and will be the focus of an international donor conference later this Fall.

4. **Reform implementation continues to face risks.** Public disillusionment over the lack of adequate job creation may lead to unrest and delay the implementation of difficult measures that can cause short-term economic pain but are necessary to lower unemployment and raise living standards over the medium term. Further deterioration of the security situation arising from terrorism and spillovers from the crisis in Libya—highlighted by the most recent attack in the city of Ben Guerdane near Libya—represent additional challenges. A recent split within the ruling Nidaa Tounes party and political campaigning ahead of municipal elections in March 2017 highlight political risks in a situation where the implementation of policies continues to require strong parliamentary support.

Box 1. Tunisia: Five-Year Economic Vision (2016–20)

The vision rests on five pillars—of which the main driver is private sector development. Macroeconomic stabilization—including fiscal consolidation, improved budget composition, and reduced external imbalances through larger exports and FDI—is considered a pre-requisite for growth.

- **Effectiveness of public institutions through good governance.** Priorities include: (i) the adoption and the implementation of an anti-corruption and good governance national plan; (ii) the establishment of a supreme authority for good governance; and (iii) the civil service reform.

- **Economic diversification through a competitive business climate and greater access to finance.** To this end, the government will focus on: (i) adopting a more transparent investment code, (ii) improving the existing transport infrastructure, (iii) enhancing the public procurement system; (iv) reforming the tax system by broadening taxation base and reducing informal sector; and (v) implementing a customs modernization program that will help prevent smuggling. Access to finance will be enhanced through the recapitalization and restructuring of public banks, reducing NPLs, adopting a new banking law, deepening capital markets, and strengthening micro-financing activities.

- **Human development and social inclusion** mainly by: (i) reforming labor markets; (ii) undertaking a comprehensive reform of the education, healthcare, and pension systems; and (iii) subsidy reform and strengthening the social safety nets. The education system will be revamped to reduce the mismatch between job seekers' skills and firms' needs. Healthcare reform will aim at providing insurance coverage to all Tunisians. The current pension system will be made financially viable. The existing safety nets, based on a unique identifier and targeted transfers, will be expanded.

- **Regional development** largely through: (i) access to finance; (ii) increasing regional public investment for greater provision of water, electricity, schools and healthcare centers; and (iii) enhancing decentralization policies.

- **Green economic growth** mainly by: (i) ensuring water, food and energy security; and (ii) increasing renewable energy production. In that vein, a national plan will be adopted to modernize agriculture, diversify energy production sources, and protect biodiversity.

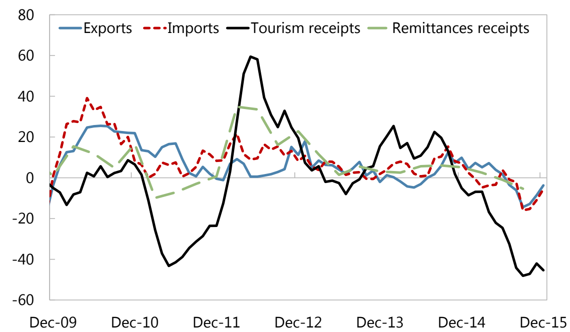
Specific policies underlying the economic vision will be detailed in a five-year development plan to be formally presented in an international donor conference in September 2016. Plans for tax policy, financial sector and SOE reforms are well advanced. Civil service reform was mentioned by all stakeholders as a priority, with a strategy to be developed in the next few months. Work on energy subsidy reforms, targeted transfers, and pension reform is ongoing, while strategies on healthcare, education, decentralization and labor markets still need to be elaborated and will require consensus building with all stakeholders. Donor TA is expected to help the authorities in these areas.

MACROECONOMIC CONTEXT

5. Economic outcomes were mixed in 2015. Social unrest (including work stoppages in mining) and security tensions affected negatively economic activity, in particular tourism.

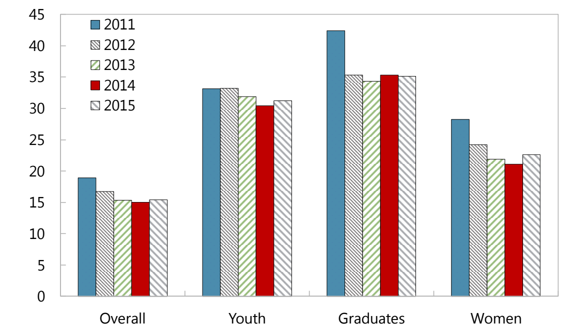
- **Real GDP growth** averaged 0.8 percent (y-o-y) in 2015, with record agriculture production offsetting declines in mining, energy, and tourism activities (arrivals and FX receipts declined by 25 percent and 54 percent (y-o-y), respectively). A revision in the GDP series led to a significant reduction in historical nominal GDP levels and a shift towards higher contributions from investment and exports. Despite having declined from 19 percent in 2011, unemployment remains high at 15 percent, particularly for youth (35 percent), young graduates (67 percent), and women (23 percent).

Key Indicators of Economic Activity
(Y-o-y growth of 3-month moving average, in percent)



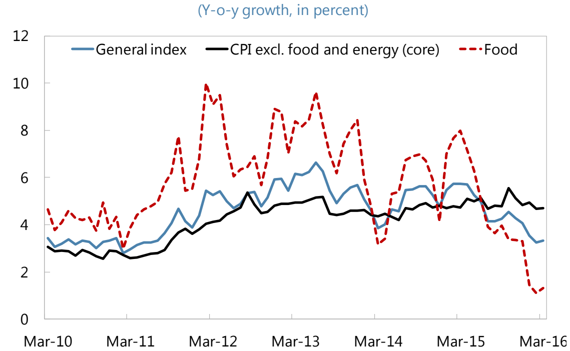
Sources: Tunisian authorities; and IMF staff calculations.

Unemployment Rate
(In percent)



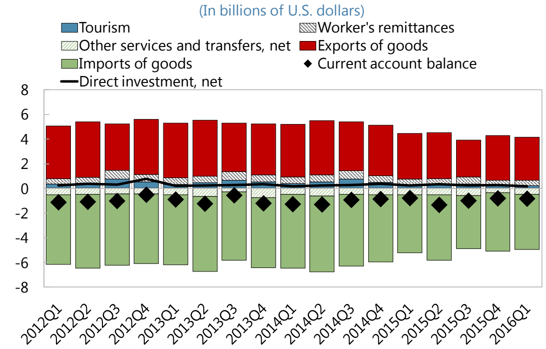
Source: Tunisian authorities.

Inflation
(Y-o-y growth, in percent)



Sources: Tunisian authorities; and IMF staff calculations.

Current Account Balance
(In billions of U.S. dollars)



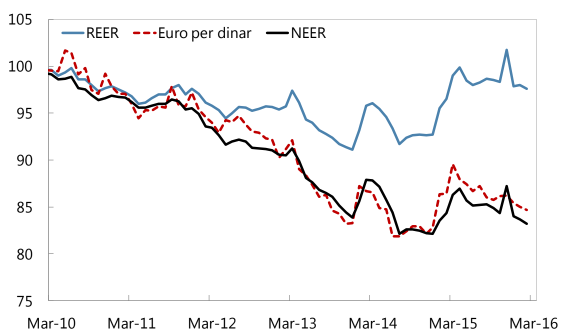
Sources: Tunisian authorities.

- After a one-off spike in October 2015, **headline inflation** continued its decline, reaching 3.3 percent in March 2016, on account of moderating food prices. Core inflation has remained stable at 4.7 percent.

- Declines in remittance and tourism inflows—driven by the repercussions of recent terror attacks—worsened the **current account deficit**, which is estimated at 8.9 percent of GDP in 2015.

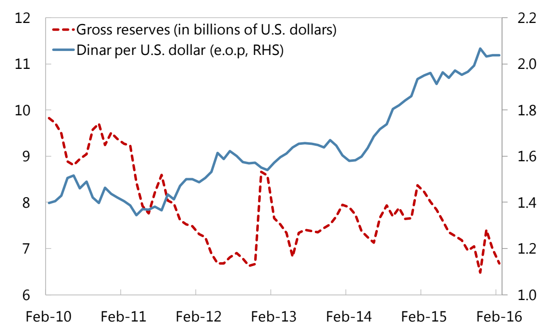
- Loan disbursements by the World Bank (US$500 million) and the African development Bank (US$200 million) in December 2015 brought **gross reserves** back to US$7.6 billion, above four months of import coverage but slightly below 100 percent of the Fund's adjusted ARA reserve metric. During 2015, the dinar appreciated by about 2 percent in nominal effective terms, despite the modest depreciation of the dinar against the US dollar over the last few weeks of 2015.

Exchange Rates
(Jan. 2010 = 100; +: appreciation)



Sources: Tunisian authorities; INS; and IMF staff estimates.

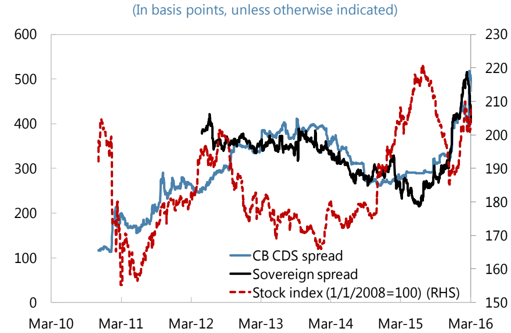
Gross International Reserves and U.S. dollar Exchange Rate



Sources: Tunisian authorities; and International Financial Statistics.

- **Financial markets** have been volatile as sovereign spreads increased to about 450 bps vis-à-vis US Treasuries at end-March 2016. The Tunisian stock market is recovering from the sharp fall of 2015, driven by bank shares.

Sovereign and CDS Spreads and Stock Index
(In basis points, unless otherwise indicated)



Sources: Markit; Bloomberg; and IMF staff calculations.

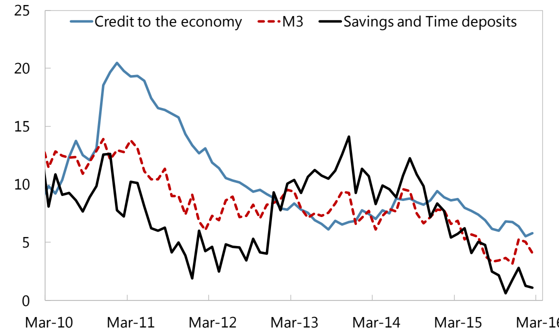
- Weaker economic activity is depressing **credit and deposit growth**; the 50 bps reduction in the CBT's policy rate (to 4.25 percent) in October 2015 did not reverse the deceleration in **private sector credit** growth (5.8 percent (y-o-y) at end-February 2016). Reliance on direct CBT refinancing has remained high, amounting to TD 4.7 billion at end–March 2016. While capital adequacy has improved significantly following the recapitalization of two public banks, the banking system remains weak as total NPLs averaged 16 percent of total loans in December 2015.

Financial Soundness Indicators, December 2015

	Public banks	Private banks	All banks
NPLs (in percent of total loans)	24.9	10.4	16
NPLs, net of provisions	11.2	3.4	6.2
Provisions (in percent of NPLs)	55.6	63.9	59
Liquidity ratio	58.9	97.2	80
ROA 1/	0.5	1.1	0.9
ROE 1/	7.3	14.2	11.2
Capital adequacy ratio (CAR)	11.2	12.4	12.2
Tier 1 capital adequacy ratio (CAR)	7.7	10.0	9.5

Source: Tunisian authorities.
1/ Data is for 2014.

Private Sector Credit and Deposit Growth
(Y-o-y growth, in percent)



Sources: Tunisian authorities, and IMF staff calculations.

- **The structural fiscal deficit**—i.e., excluding economic cycles and one-off costs linked to bank restructuring and civil service reform—remained at 4.3 percent of GDP in 2015. The overall cash deficit stood at 4.7 percent of GDP, lower than expected because of stronger tax revenue and deferred "customary" payment of expenditures authorized under the 2015 budget during the "complementary period" (January 1-20 2016, about 1 percent of GDP) and be paid in Q1 2016.

THE FUND-SUPPORTED PROGRAM

6. **The authorities' five-year economic vision aims at transforming Tunisia's economic model to generate faster and more inclusive growth, and provides the platform for an IMF-supported program.** In addition to consolidating macroeconomic stability—a key pre-requisite to more inclusive growth, the overriding goals of the Fund-supported program are to reform public institutions, facilitate financial intermediation, and improve the investment climate. The broader ownership of the economic program—beyond the government coalition—will be strengthened by the ongoing efforts at consensus building.

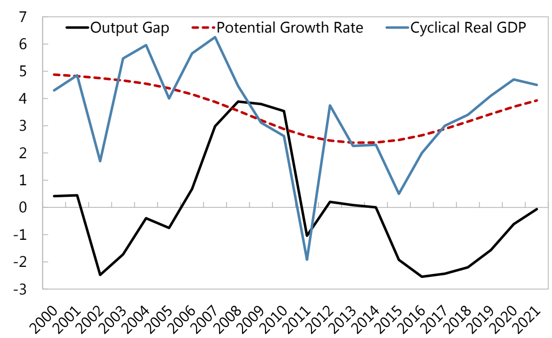
7. **Discussions revolved around macro-critical reform priorities and the pace of adjustment and reform implementation.** Staff and the authorities agreed on a gradual and evenly phased fiscal adjustment that would reduce debt and financing needs over the medium term, with strong upfront action to create space for priority investment spending. Staff urged the authorities to engage in a strong communication campaign to explain to the public the need for reforms and highlight that the burden of adjustment will be shared by all while protecting the most vulnerable.

A. The Macroeconomic Framework

8. Staff and the authorities agreed that the program's macroeconomic framework should be built on a gradual rebound in growth, stable inflation, and a steady build-up of external buffers. Key assumptions underlying the forecasts include receding security risks, steady reform implementation, and a gradual return of investor confidence. The situation in Libya is expected to remain broadly unchanged, with no significant improvement nor deterioration.

- **Growth** in 2016—at 2 percent—reflects continued uncertainty despite some recovery in the phosphate and manufacturing sectors. Over the medium term, economic activity would regain the momentum with growth gradually converging to its medium-term potential by 2019. This would reflect stronger investor confidence—including through FDI—and a boost from public investment. Mining, tourism, and manufacturing sectors will continue their recovery, although tourism levels will remain below pre-2011 levels.

Output Gap and Potential Output



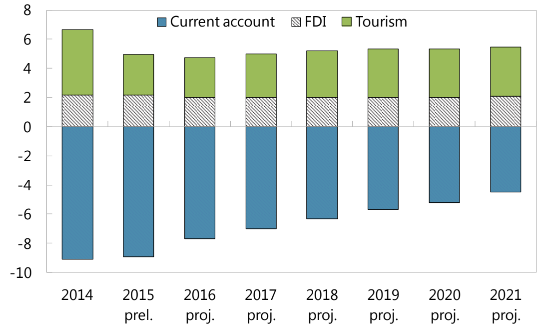
Source: IMF staff estimates.

- **Headline inflation** is expected to decline to 4 percent by end-2016, aided by a 5 percent reduction in retail fuel prices. A decline to 3.5 percent over the medium term will be helped by prudent monetary policy, a contained wage bill, and moderate increases in international food and fuel prices.

- The **current account** deficit would narrow to 7.7 percent of GDP in 2016, helped by low international oil prices. Over the medium term, the deficit would decline to 4.4 percent of GDP by 2021, reflecting a rebound in tourism and phosphate exports, recovering demand from Europe, and moderate import growth. Gross reserves are expected to exceed 100 percent of the Fund's adjusted reserve metric by the end of 2016, with Fund resources providing sufficient cushion in case of shocks.

External Position

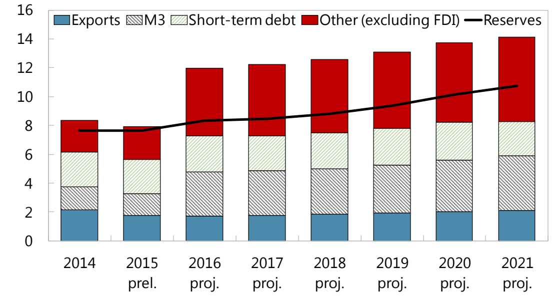
(In percent of GDP)



Sources: Tunisian authorities, and IMF staff calculations.

ARA Metric Decomposition (Adjusted /1)

(In billions of U.S. dollars)



Sources: Tunisian authorities; and IMF staff calculations.

/1 The adjusted metric assumes a floating exchange rate regime and lifting of capital controls in 2019 onwards.

Tunisia: Selected Economic Indicators, 2014–21

	Prel.	Proj.						
	2014	2015	2016	2017	2018	2019	2020	2021
Real GDP growth (in percent)	2.3	0.8	2.0	3.0	3.7	4.3	4.7	4.5
Consumer price index (CPI), (period average, in percent)	4.9	4.9	3.9	3.9	3.8	3.7	3.5	3.5
Current account (percent of GDP)	-9.1	-8.9	-7.7	-7.0	-6.2	-5.5	-5.1	-4.4
Gross official reserves (US$ billions, eop)	7.7	7.6	8.3	8.5	8.8	9.4	10.1	10.7
Gross official reserves (months of next year's imports)	4.2	4.3	4.6	4.5	4.5	4.6	4.7	4.8

Sources: Tunisian authorities; and IMF staff estimates and projections.

9. **Risks to the outlook remain high** (Box 2). A deteriorating security situation—including increasing spillovers from Libya—and high social tensions are the most immediate risks, as these could derail policy implementation. Other risks include tighter or more volatile global financial conditions and a rebound in energy prices. Vested interests—particularly against civil service or business climate reforms—and political uncertainty could further complicate reform implementation. On the upside, the authorities point out that large infrastructure projects in the pipeline, anti-terrorism efforts, and prospects of social peace underpinned by agreements with the unions for the next three years could rapidly restore investor and consumer confidence.

Box 2. Tunisia: Risk Assessment Matrix*

Source of Risk and Relative Likelihood	Expected Impact and Recommended Policy Response
Domestic Risks	**Domestic Risks**
High	*High*
A deteriorating security situation, political instability and high social tensions due to intensified terrorist activity, spillovers from the crisis in Libya, slow consensus-building, and/or push-back from vested interests.	Renewed focus on security and heightened social tensions would undermine economic activity and affect the government's ability to undertake pressing economic policy reforms, negatively impacting investment and growth. Authorities should build consensus on the government's five-year development plan, both with the public and with potential multilateral and bilateral donors, and implement rapidly economic reforms needed to promote inclusive growth. Building public confidence and ownership through continuous communication will also be essential.
External Risks	**External Risks**
High	*Medium*
Tighter or more volatile global financial conditions, triggered by (i) sharp asset price adjustments as investors respond to unanticipated changes in growth prospects and Fed policy rate path; and/or (ii) sovereign and financial sector stress re-emerging across the Euro area due to protracted policy uncertainty, delays in debt servicing by Greece, faltering reforms, and political and social upheaval.	Increased global financial volatility could destabilize global recovery and financial markets, adversely affecting partner countries' economies, slowing FDI inflows, and increasing financing costs. Recommended policy responses include: (i) creating fiscal space by containing the wage bill, reforming energy subsidies and the tax system; (ii) countercyclical monetary policy (assuming inflationary pressures are not present); and (iii) completion of banking reforms.
Medium	*High*
Structurally weak growth in key advanced and emerging economies, driven by weak demand and persistently low inflation in Europe, and incomplete structural reforms and maturing of the cycle in key emerging markets, including China.	Growth would be adversely affected through trade, remittances, and investment channels, especially from Europe, Tunisia's main trading partner. Authorities should (i) diversify export markets; (ii) accelerate structural reforms to increase productivity and competitiveness; and (iii) let revenues decline in line with economic activity (e.g., through automatic stabilizers).
Medium	*High*
Heightened risk of fragmentation/state failure/security dislocation in the Middle East, leading to higher migrant flows with negative global spillovers.	Growth may fall on account of shaken investor confidence, increased security spending, sharp increases in oil prices, and tighter financing conditions. Authorities should (i) rebuild fiscal and external buffers; and (ii) accelerate economic and structural reforms.
Medium	*High*
Risks to energy prices, including through (i) increased volatility due to uncertainty about the persistence of the oil supply shock and the underlying drivers of the price decline, and/or (ii) persistently low prices triggered by supply factors reversing only gradually, and weaker demand.	Increased price volatility may adversely affect decisions to reform energy taxes and fuel subsidies. Lower energy prices will likely ease external and fiscal pressures, and lower inflationary pressures. Authorities should (i) urgently implement the symmetric automatic fuel price adjustment formula; (ii) save any external windfalls from lower oil prices; and (iii) strengthen fiscal and external buffers.

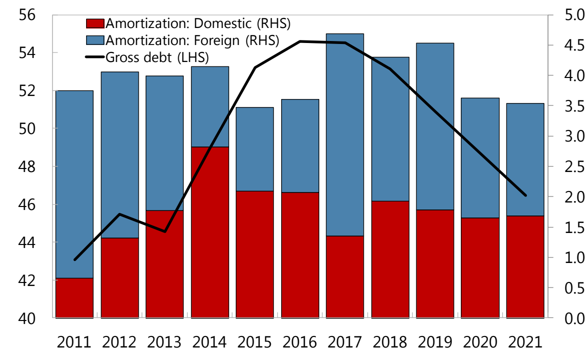
*The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

B. Consolidating Macroeconomic Stability

Fiscal policy

10. Fiscal policy will aim at putting public debt on a downward path. Staff agree with the authorities that a 2.2 percent of GDP reduction in the structural fiscal deficit by 2019 would help stabilize the debt-to-GDP ratio in the near term and help reduce it to under 50 percent by 2020 (from 53 percent in 2015, albeit with a share of foreign-denominated debt that remains high at 65 percent). This path is consistent with large amortization payments—peaking at 4.7 percent of GDP in 2017 (text chart)—limited financing options, and the need to reduce external imbalances. Public debt dynamics remain sustainable under most shocks, with the shock to the exchange rate the most severe in view of a large share of foreign-denominated debt (DSA Annex II).

Debt and Amortization
(In percent of GDP)



Source: Tunisian authorities.

11. Fiscal consolidation over the medium term is expected to proceed gradually, anchored by wide consensus on tax and civil service reforms which are essential to improve budget composition (Section C and MEFP ¶9). The consolidation should help create space for contingencies, including from a more depreciated exchange rate, and allow for a sizable increase in public investment. Risks to the planned adjustment include spending pressures from interest groups, tax yields falling short on account of slower growth, and additional transfers to ailing SOEs (¶24, Box 5).

12. Higher security spending reduces the pace of adjustment envisaged at the time of the 2016 budget (MEFP ¶11). Staff agreed with the authorities to adjust the pace of fiscal consolidation in 2016 to account for one-off security related expenditures necessary to strengthen their anti-terrorism efforts. As a result, the structural fiscal deficit for 2016 is 0.4 percent of GDP higher than originally budgeted, but still consistent with the medium-term adjustment path. Revenue loss from lower oil production and weaker economic activity as well as higher pension transfers are expected to be mostly offset by substantial savings on energy subsidies (resulting from lower oil prices and partial adjustment in domestic energy products) and higher revenues from surpluses from refineries, the sale of the telecom license, and reduced unallocated spending (text table).

Tunisia: Selected Fiscal Indictors, 2015–21 1/
(In percent of GDP)

	2015	2016		2017	2018	2019	2020	2021
	Prel.	Budget		Proj.				
Revenue	23.0	24.2	23.9	24.1	24.4	24.9	24.8	24.8
Of which : Tax revenue	21.6	22.5	21.7	22.2	22.5	22.9	22.8	22.8
Expenditure and net lending	28.5	28.2	28.5	28.0	28.1	27.3	26.9	26.6
of which : Wages and salaries	13.5	14.1	14.1	13.8	13.8	12.7	12.0	11.7
Transfers and subsidies	5.7	5.0	4.9	4.5	4.3	4.4	4.4	4.4
Capital expenditure	4.6	5.0	5.0	5.5	5.9	6.5	7.0	7.2
Net lending	0.8	-0.1	-0.1	0.1	0.1	0.1	0.1	0.1
Of which: Public banks' recapitalization	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Central government overall deficit (-) (excl. grants)	-5.5	-4.0	-4.6	-3.9	-3.7	-2.4	-2.0	-1.8
Structural fiscal balance	-4.3	-3.6	-4.0	-3.3	-2.8	-2.1	-1.9	-1.8
Central government debt	53.2	54.6	54.6	54.5	53.1	50.9	48.7	46.4

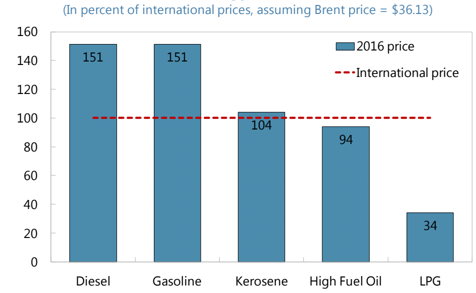
Sources: Tunisian authorities; and IMF staff estimates.

1/ Nominal GDP has been revised down from 2012–14, reflecting final numbers of the national accounts publication by the National Institute of Statistics.

13. **Containing the wage bill remains an immediate priority to ensure fiscal sustainability, pending the design of a comprehensive civil service reform.** Rationalizing promotions and performance bonuses (savings of 0.2 percent of GDP) were necessary to keep the wage bill at the originally budgeted level in 2016 (MEFP ¶11), thereby helping offset additional wage increases recently granted to security forces (0.2 percent) on top of past agreements with unions reflected in the current budget (0.7 percent of GDP). Staff acknowledged the difficult situation facing security forces at this juncture, but noted that increasing salaries would endanger fiscal sustainability while reducing space for priority spending required to meet the needs of the unemployed. Staff and the authorities both agree that recourse to the public sector cannot be the solution to reduce high unemployment, with the wage bill already at 14 percent of GDP (63 percent of tax revenues).

14. **The introduction of an automatic fuel-price adjustment mechanism will help sustain energy subsidy reforms.** The five percent decline in retail fuel prices last January increased households' disposable income and will be followed in July by the implementation of a new automatic price adjustment mechanism, which is expected to ensure full cost recovery and appropriate tax collection. The authorities argued that the symmetric mechanism and associated smoothing formula should initially be implemented on a quarterly basis (MEFP ¶22), but agreed with staff that monthly adjustments starting in January 2017 are necessary to ensure it can be sustained in case of large fluctuations in international oil prices.

Energy Prices
(In percent of international prices, assuming Brent price = $36.13)

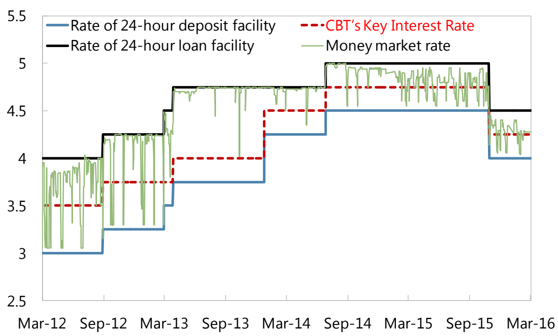


Sources: Tunisian authorities; and IMF staff calculations.

Monetary and exchange rate policies

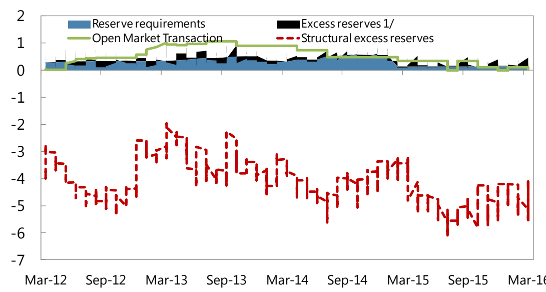
15. The authorities are committed to a prudent monetary policy. Continued declines in inflation, moderate credit growth, and economic activity well below potential justify the current monetary policy stance (implying a positive real interest rate of 1 percent), which is further reinforced by limited inflationary pressures from the latest bouts of wage increases. Staff reiterated the importance of maintaining a positive real interest rate to anchor inflation expectations and manage possible depreciation pressures. It supported the CBT's readiness to reverse its rate cut of October 2015 should underlying inflationary pressures pick-up (MEFP ¶14).

Interest Rates
(In percent)



Source: Tunisian authorities.

Structural Liquidity Deficit of Banking System
(In billions of dinars)



Sources: Tunisian authorities; and IMF staff estimates.
1/ This item captures spare liquidity arising from BCT injections, rather than proper excess reserves.

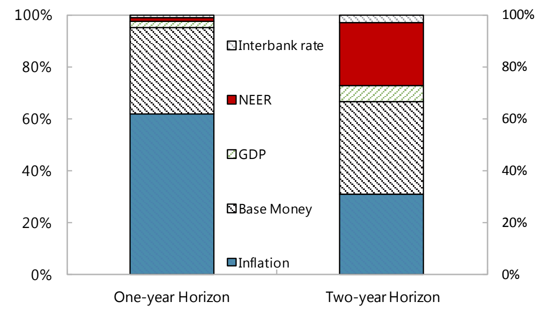
16. A gradual move towards a full-fledged inflation targeting framework is planned for the medium term. The authorities agreed to continue targeting NDA to maintain money supply growth consistent with the inflation objective until pre-requisites for inflation targeting are fully in place (Box 3). Improved liquidity forecasts and strengthened collateral framework will strengthen the monetary transmission channels and banks' liquidity management (MEFP ¶15). Improving the communication of the CBT's objectives and policy commitments, as well as greater exchange rate flexibility and a risk-based supervision framework—are also important for moving towards a full-fledged inflation targeting framework.

17. Enhanced central bank independence will improve monetary policy making. The adoption of the new central bank law grants greater CBT autonomy—including by forbidding third parties from interfering with the CBT mandate—and provides clarity of objectives, an important pre-requisite to inflation targeting. The new law also improves the monetary policy framework by setting up a full-fledged lender of last resort that clearly separates emergency liquidity operations from monetary policy ones. Staff regretted deviations from best practices included in the law—such as government presence in the CBT Board and lack of outright prohibition on receiving specific instructions from the government—and urged the authorities to consider further amendments in the future to ensure compliance with best principles. The establishment of a yield curve will also help improve the monetary transmission mechanism.

Box 3. Tunisia: Monetary Base and Inflation

Reserve money remains an important driver of inflation. Staff analysis indicates that a third of inflation variability at a two-year horizon is due to changes in the supply of base money, under the direct control of the CBT. Changes in the policy rate help only marginally in explaining changes in inflation, even at longer horizons. Monetary aggregates remain a relevant indicator for assessing the monetary policy stance in Tunisia, and the ceiling on NDA accumulation can still help the CBT communicate its monetary policy stance to market participants. The policy rate, in turn, will become a more important indicator over time as interbank and capital markets deepen.

Variance Decomposition Of CPI Inflation /1



1/ Refers to the relative contribution to inflation variability of shocks to selected variables at a specific time horizon. The estimated contributions are derived from a vector error correction model using quarterly data from 1997 to 2015.

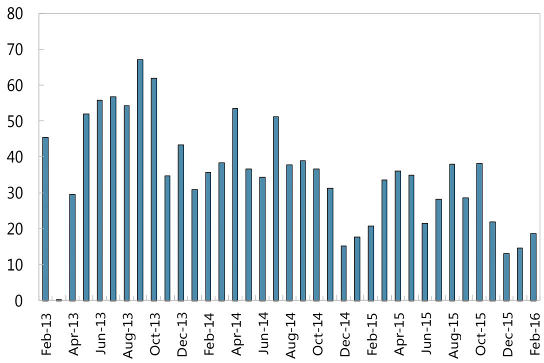
Source: IMF staff estimates.

18. **Simplification of the existing capital account regulations and the modernization of the FX liquidity framework will strengthen exchange rate policy.** Staff welcomed steps taken to reduce ex-ante controls on capital account transactions, eliminate the ceiling for foreign holdings of government debt, and grant greater powers to banks for FX transfers. The implementation of the recent FX auction mechanism helps improve FX liquidity management (MEFP ¶17). Staff called for further improving the FX operational framework through regular holdings of these auctions, which should be clearly pre-announced. Staff agreed with the authorities that a move towards full capital account convertibility would only be appropriate for the medium term once pre-requisites are met (MEFP ¶18).

19. **These measures, together with the planned reduction in CBT's interventions, would reduce dinar overvaluation and improve liquidity.** With the dinar continuing to depreciate in a crawl-like manner within a two percent band, staff estimates the real effective exchange rate to be overvalued (6–13 percent). Greater exchange rate flexibility[1] would help rebuild buffers, increase competitiveness and support monetary policy. Staff welcomed the explicit commitment by the CBT to limit interventions to only smoothing excessively large fluctuations, with a set ceiling for net FX sales (MEFP ¶18-19). Lower interventions, currently below 20 percent of the FX market (text chart), would complement other measures on the FX framework and improve liquidity management by reducing banks' refinancing needs.

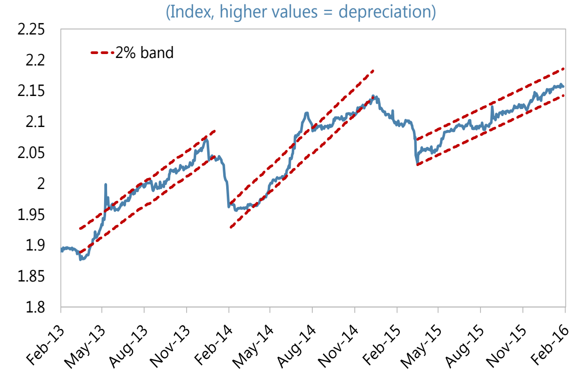
[1] Balance sheet effects from greater exchange rate flexibility are limited for the financial sector by commercial banks' ability to hedge. For the public sector, a large exchange rate depreciation would raise public debt ratios and increase external debt service, but exposure is limited by longer-term maturity of the debt, mostly owed to multilaterals. The impact on the non-financial sector's balance sheet will be attenuated by a windfall from resident foreign currency deposits (for more details, see Box 2 of IMF Country Report No 14/123).

Share of CBT Sales in the Foreign Exchange Market
(In percent)



Source: Tunisian authorities.

Tunisian Dinar to Euro-US$ Basket Exchange Rate
(Index, higher values = depreciation)



Source: IMF staff calculations. Weights based on currency of trade transactions.

Exchange Rate Assessment Using CGER Panel Estimates 1/
(In percent)

	Underlying CA	CA Norm	REER
EREER approach 2/	...	...	6.4
MB approach 3/	-4.5	-2.3	9.1
ES approach 4/	-4.5	-2.3	9.1

1/ Overvaluation (+); undervaluation (-)
2/ Based on an elasticity of the CA/GDP wrt th -0.24
3/ In 2021 corrected from program adjustment.
4/ Stabilizing NFA at 14.4 percent of GDP (2010 levels).

Source: IMF staff estimates

Macro Balance Approach Using EBA
(In percent)

CA Projected 2016	-7.7	CA Gap	-5.7
CA Norm	-2.3	Contribution of identified Policy Gaps	0.1
		Unexplained residual	-5.8
CA Fitted	-2.4		
REER misalignment 1/	13.1		

1/ Overvaluation (+); undervaluation (-)

Source: IMF staff estimates

C. Reforming Public Institutions

20. Reforming public institutions is the cornerstone of the authorities' medium-term program to boost inclusive growth. Increasing the efficiency of public services, improving the composition of the budget to increase pro-growth expenditures, and safeguarding fiscal sustainability are critical components of the authorities' strategy (MEFP ¶19). Achieving these goals requires a comprehensive civil service reform, the rationalization of energy subsidies, stronger public financial management, an improved social safety net, and equity-friendly revenue mobilization.

21. Modernizing the public administration has been identified by all stakeholders as a key priority to improve public service delivery and support growth (Box 4). Staff welcomed plans for a comprehensive civil service reform, which will be laid out in a time-bound strategy by September 2016 (structural benchmark, SB). The strategy will cover several aspects detailed in the authorities' vision, notably the creation of a "Special Statute for High Level Civil Servants" that seeks to attract qualified candidates, the application of stricter recruitment criteria, improved evaluation and promotion processes, and better alignment of pay structures with performance (including through rationalizing existing allowances). As part of the strategy, the authorities are committed to contain wage increases and finalize functional reviews of four ministries (end-December SB), which should improve efficiency and quality of services, paving the way to redeploying human resources where they are needed the most (including in the interior regions). This could allow for a reduction in the workforce—possibly accelerated through incentives for targeted voluntary departures in

2018—that helps the authorities meet their objectives of improving public service delivery and reducing the wage bill to 12 percent of GDP by 2020 (MEFP ¶20).

22. Implementation of the civil service reform strategy will imply containing the wage bill increase in 2017. The growing wage bill—driven by a 23 percent increase in employment and a 37 percent rise in average wages since the revolution—is unsustainable. Staff welcomed the authorities' commitment to limit the increase of the wage bill in 2017 to the expected inflation rate which, in view of past agreed wage increases, implies the need to identify savings of about 0.6 percent of GDP in 2017. Specific options to be considered at the time of the 2017 budget, which should be in line with the overall reform strategy, could include streamlining bonuses and allowances, further reducing turnover and promotions, and extending the hiring freeze (MEFP ¶20).

23. Reforming energy subsidies in a sustainable manner while strengthening the existing social safety net is necessary to improve budget composition over the longer term. Following the reform of fuel subsidies—to be implemented in July 2016 (¶14)—the authorities plan a gradual increase of electricity tariffs to cost-recovery levels, accompanied by lifeline tariffs that will continue to protect the most vulnerable (MEFP ¶22). In addition to existing cash transfer schemes, whose coverage and importance increased over the past two years, a better-targeted social safety net would be introduced in June 2017, with the introduction of a unique social identification number and a new database on vulnerable households (end-March 2017 SB) (MEFP ¶24).

24. The financial viability of the public pension system should be promptly restored (MEFP ¶24)**.** The public sector retirement and social security fund (CNRPS) is in deficit, requiring budget transfers of about 0.4 percent of GDP in 2016. Staff reiterated the importance of accelerating the tri-partite National Social Dialogue on pension reform with the aim of restoring CNRPS's financial viability. A comprehensive long-term solution could include changes in contribution parameters and benefits, and should be consistent with civil service reform proposals.

25. Strengthening the monitoring and performance of State-Owned Enterprises (SOEs) is necessary to improve service delivery and reduce fiscal risks. Staff welcomed the government adoption of a strategy to improve governance and ensure SOEs can operate on a commercial basis and reduce their substantial losses (Box 5). Staff also supported the authorities' plans to create an independent agency overseeing SOE restructuring, including public banks, but noted potential difficulties in avoiding duplications among existing ministerial structures (MEFP ¶21). The mission encouraged the authorities to conclude performance contracts for the five largest SOEs (SB), which should include indicators on managerial and financial performance. The monitoring of cross-arrears between SOEs and the central administration, expected to start in 2016, is a key first step towards improving SOE financial performance. The production of a fiscal risks statement that highlights SOE risks and possible mitigation measures is necessary to strengthen transparency and guide policies.

Box 4. Civil Service Reform in Tunisia—Possible Options to Contain the Wage Bill

Reducing the wage bill to a size comparable to pre-revolution levels requires high quality reforms of public sector employment and wages. Successful reforms from other countries suggest combining short-term measures to limit salaries with more sustainable reforms. Country experiences show that a successful reform effort requires broad-based political consensus, and consistency with the medium-term fiscal framework and pension reform. Possible reform options could include:

Short-Term Measures:

- **A freeze on wages.** For Tunisia, the impact of this measure would likely be limited by increases agreed with unions through 2017. A wage freeze, particularly for lower categories of civil servants, could help reduce the existing disparity with the private sector (e.g., an 18.5 percent wage premium and low compression ratio).

- **Streamlining bonuses and allowances.** There are 37 types of specific allowances and more than 140 special allowances in the civil service in Tunisia—these have doubled since 2011 and differ by function and ministry. They represent about 60 percent of the average salary.

- **Hiring freeze.** The Tunisian government has already announced a three-year hiring freeze, with the exception of ongoing regularization of past contractual workers agreed in the aftermath of the revolution. Extending the freeze for a long time may contribute to distorting the structure of the civil service, which has already lost many of the high level skilled workers.

- **Voluntary separation of public workers.** This would likely be associated with a severance payment, which will increase short-term costs. This option would need to be carefully designed to ensure consistency with the recent decision to increase the retirement age in Tunisia so as to help make the pension system more viable.

Sustainable Reforms

- **Rationalizing the size and structure of government.** A review of employment would be needed to identify areas of duplication, overlap, and rigidities in the context of the priorities for public service delivery and planned decentralization.

- **Tightening the link between pay and performance.** Linking pay increases to performance provides incentives to workers for improving efficiency and productivity. This could also involve equalizing pay between different budget units or aligning wages with private sector comparators as well as increasing salary differentiation among categories (compression ratio) to promote productivity.

Other considerations. Reform of the civil service in Tunisia would need to go hand in hand with the reform of public enterprises, which have been used in the past as a source of public employment creation with limited transparency and efficiency.

26. **Strengthening public financial management and transparency will be critical to improve the efficiency of public services and reduce fiscal risks.** The authorities' vision include a three-pronged approach:

- **Public Financial Management.** The organic budget law, to be adopted by Parliament this year (SB), will improve the budget preparation and execution process, facilitate the collection of budgetary information, introduce a new budgetary functional classification, and simplify control and audit procedures (MEFP, ¶25). It will also help complete the rollout of performance budgeting and, together with the new procurement code and project prioritization, help accelerate public investment execution, particularly in rural areas. Coordination among agencies

and with state owned enterprises will also be critical to improve cash management and forecasting (¶25).

- **Debt Management.** A medium-term debt strategy will be finalized by end-2016, with help from the World Bank (SB), will help ensure the proper mix of foreign/domestic borrowing, optimal maturity structure and rollover management, and cost-effective issuance strategies coordinated with cash management. A centralized debt agency to be set up next year will help the authorities implement their strategy (MEFP ¶26). The agency will also be managing the share of sizeable state guarantees (about 12 percent of GDP). Staff recommended the publication of debt auctions calendars on a quarterly basis and the issuance of short-term debt to help develop financial markets. Staff also stressed the need for consistent reporting of domestic and external debt across public institutions and consolidating management of all debt types (multilateral, bilateral, and commercial) into the newly created unit.

- **Strengthening anti-corruption efforts.** The establishment by end-December 2016 (SB) of a high-level anti-corruption entity—whose independence and budgetary autonomy are guaranteed by the Constitution—will protect citizens against state abuses and set clear rules for conflicts of interests. Other priorities on this front include the introduction of a whistle blowing platform and stronger financial transparency requirements for high-level public officials (MEFP ¶27). With help from Fund TA, the authorities are strengthening their AML/CFT framework by introducing a risk-based approach and strengthening their assessment of banks' due diligence on new customers.

- **Improving data transparency.** The publication of a "citizen budget" and an electronic government platform illustrate the authorities' commitment to greater transparency. Efforts to improve data collection, production and dissemination by the national statistical agency are also a step in that direction. Reducing delays in data compilation and publication is necessary to monitor socio-economic developments and informing policymakers in a timely manner.

27. Work is underway to boost revenue in a fair, efficient, and transparent manner. The tax reforms included in the 2015-16 budgets—halving the difference in offshore-onshore corporate taxation, rationalizing customs duties, lowering of excessive excise rates (e.g., alcohol), improving presumptive taxation, and reducing VAT exemptions by 0.5 percent of GDP—represent the first wave of reforms towards a more efficient and equitable tax system. This will be complemented in an overall strategy (prior action) that: (i) broadens the VAT tax base by removing exemptions and simplifying the VAT from three to two rates (6 and 18 percent); (ii) improves the progressivity of the personal income tax; (iii) further reduces the difference in on-shore and off-shore corporate taxation while increasing dividend taxation to improve equity, eliminate tax arbitrage and preserve revenue neutrality; (iv) simplifies the taxation for small enterprises; and (v) reduces earmarked taxation. Once adopted, it would be important to complement the tax strategy through legislative action. In addition, existing tax incentives should be rationalized and tax administration strengthened by moving towards an integrated tax administration, starting as a priority with a Large Taxpayer Unit regrouping tax functions (MEFP ¶23).

Box 5. Reforming Non-financial SOEs in Tunisia

State-Owned Enterprises (SOEs) play an important role in Tunisia's economy. Ninety three non-financial SOEs operate in 17 sectors, of which the most important ones are in industry and energy, transport, water and agriculture. SOEs employ 180,000 people (5 percent of Tunisia's active population), with employment increasing by 50 percent since 2011. The largest 28 enterprises represent more than 70 percent of this employment.

Fiscal implications of SOE operations are high and rising:

- On a consolidated basis, **non-financial SOEs registered a 4.4 percent of GDP deficit** in 2013,[1] with half of the enterprises operating in the red, led by *Société tunisienne de l'électricité et du gaz (STEG), Société des transports de Tunis (Transtu)*, *Tunisair*, and the *Tunisian Chemical Group*. This deficit represents a three-fold increase from 2010. At the same time, transfers to public enterprises also increased from about 2 percent of GDP in 2010 to about 7 percent of GDP in 2013 (reduced more recently thanks to the decline in international energy prices).
- **Liabilities are high but hard to quantify:** Guaranteed external debt averages close to 10 percent of GDP (about a third of Tunisia's external PPG debt). SOE debt to the banking system is about 5 percent of GDP, while the magnitude of the total stock of domestic debt is not known (including because of lack of consolidation across public enterprises and central government on-lending operations).

A weak governance framework—aggravated by lack of transparency—contributed to the poor performance of SOEs. The performance of SOEs in Tunisia is hampered by lack of managerial autonomy (e.g., no independent executive board). Social objectives (e.g., employment) frequently dominate their operations—often without clear mandates and accountability. Also, lack of publication, long delays in producing balance sheets, and lack of consolidated accounts weaken monitoring operations (despite numerous control bodies).

An ambitious strategy to revamp SOEs has been designed, centering on the creation of a centralized technical body under the Ministry of Finance or PM office to monitor SOEs and oversee their restructuring. The unit would design performance contracts for SOE managers and be able to veto financial assistance if performance indicators are not met. The authorities also plan to strengthen the role of SOEs' Executive Boards, improve manager selection and control and audit mechanisms, and enforce the reporting and publication requirements. The role of the State in so many sectors of the economy would also be revisited.

Prioritization is key. Monitoring and design of performance contracts is set to start on a pilot basis with large SOEs. This endeavor would require significant resource requirements (both in terms of staffing and cooperation across departments). Accompanying changes in regulations would occur in parallel.

[1] 2014 data is under preparation.

Tunisia: Tax Package Over the Medium Term and Potential Yields
(Percent of GDP)

	2016		Estimated gains over the medium term	
	Million of dinars	Percent of GDP	Million of dinars	Percent of GDP
Tax package: First set of reforms included in the 2016 budget	439.0	0.5		
VAT	395.0	0.5		
Base expansion: Reduction tax exemptions	495.0	0.6		
Reduction withholding tax from 50 percent to 25 percent	-50.0	-0.1		
Impact of Customs duties harmonization	-50.0	-0.1		
Customs tariffs				
Tariff harmonization (reduction from seven to two)	-316.0	-0.4		
Excise taxes				
Increase in fuel taxation in fuel price mechanism	360.0	0.4		
Tax package: Outstanding reform proposals			994.7	1.1
Direct Taxation			-165.0	-0.2
Personal income tax			-215.0	-0.2
Simplification of number of brackets			315.0	0.3
Increase of income tax threshold from TD1500 to to TD5000			-730.0	-0.8
Elimination of deductions for professionnal services			200.0	0.2
Corporate income tax			50.0	0.1
Decrease of CIT Rate for onshore sector to 20 percent in 2018			...	...
Increase dividend taxation to 10 percent			50.0	0.1
Indirect Taxation			1,159.7	1.3
VAT			820.0	0.9
Rationalization of VAT rates (6,12,18) to 6 percent and 18 percent			320.0	0.3
Further reduction of tax exemptions			500.0	0.5
Customs duties				
Eliminate Preferential treatment regime (tax at current rates)			416.7	0.5
Excises			123.0	0.1
Reduction of list of products subject to excises			-77.0	-0.1
Increase rates for tobacco products while liberalizing retail prices [3/]			200.0	0.2
Other taxes				
Reduction of Earmarked Special Funds (and rationalization on spending side of Funds)			-200.0	-0.2

Sources: Tunisian authorities; USAID; and IMF staff estimates and projections.

D. Promoting Financial Intermediation

28. **Important steps have been taken towards establishing a modern banking system, subject to strong supervision and competition**. Reforms under the previous SBA—the recapitalization of two large public banks and a strengthened regulatory and supervisory framework—have paved the way towards a more stable and efficient banking sector, supportive of financial intermediation and private sector development. The adoption of all banking legislation (bankruptcy, banking and central bank laws) by May 2016 is a crucial step forward as these laws will set the stage for a considerable improvement in banks' ability to resolve bad loans; they will also make available more modern tools—including a lender of last resort facility and a deposit guarantee

scheme—to ensure the stability and efficiency of the financial sector (MEFP ¶29) and boost private sector credit, which has remained relatively low (77 percent of GDP at end-2015).

29. Nevertheless, vulnerabilities persist. Overall capital adequacy has improved to 12.2 percent in end-December 2015, but one public bank capital ratios still fall short of regulatory requirements. Banks continue to rely on central bank refinancing, with one large bank's liquidity ratio below prudential norms. Non-performing loans remain high and may deteriorate further once the freeze on tourism loan classifications—introduced after the Sousse attack—expires next year. Weaker economic activity, including from an anemic tourism sector (about 25 percent of NPLs), and smaller intermediation margins could put additional pressure on bank soundness and profitability.

30. Staff supported the authorities' strategy aimed at strengthening the financial sector and promoting financial inclusion. The authorities' strategy—which will be overseen by a Financial Sector Steering Committee (FSSC) chaired by the MoF—include strengthening banking sector resilience, improving banking sector regulation and governance, expanding CBT supervisory functions, and improving financial inclusion. Staff called for the FSSC to ensure not only coordination but also effective delivery of the reforms and regular communication with the public.

31. Strengthening banking sector resilience requires continued progress on public bank restructuring. The updated business plans, expected to be approved by banks' boards by May 2016 (prior action), build on prudent assumptions that aim at a rapid resolution of NPLs, including through write-offs (MEFP ¶30) while ensuring compliance with all prudential standards throughout the restructuring period (such write-offs should avoid sales of NPLs to public banks' own subsidiaries). Performance contracts will be signed by June (SB) to ensure the right incentives are in place for bank management, with key indicators to be monitored on a consolidated basis (MEFP ¶30) by the newly established state-ownership agency. Staff welcomed the authorities' intention to encourage the entry of strategic or technical partners by privatizing part of its stakes in the three main public banks, and to divest its remaining minority shares in private banks.

32. Resolution of NPLs is essential to ensure a successful bank restructuring. Staff and the authorities agreed on removing the legal barriers that hinder the capacity of banks to actively resolve their NPLs through: (i) new implementing decrees of the recently adopted bankruptcy law along with a review of the regulatory framework for insolvency practitioners; (ii) putting public banks on an equal footing with private banks by empowering them to write-off NPLs; (iii) simplifying write-off rules; and (iv) allowing credit recovery companies to contact their clients to incentivize repayments of debts. The introduction of dedicated internal structures in public banks to deal with NPLs will also help facilitate debt recovery. Staff encouraged the central bank to assess the possibility of out-of-court settlements to facilitate debt renegotiations, which is being planned with technical support from the World Bank.

33. The progress made in strengthening the regulatory and supervisory environment should be consolidated. Key measures include:

- **Passage of the banking law.** The banking law, to be adopted by parliament in early May 2016, includes a proper banking resolution framework and a deposit guarantee scheme, which will help boost confidence in the banking system and brings Tunisia closer to best international standards. However, staff noted that MoF presence in the banking resolution committee should be limited only to systemic cases as the use of public funds in the resolution of non-systemic banks is not warranted; the authorities disagreed.

- **Implementation of the CBT's five-year plan and steps towards a proper risk-based supervisory system.** Moving towards introducing internal risk rating systems, the use of a risk-based supervision manual (to be completed) as a systematic reference for supervisors (SB), and full automation of reporting by banks will help strengthen supervisory standards and limit risks to financial sector stability. Staff welcomed the forthcoming hiring of ten new supervisors, and urged additional recruitment to ensure adequate resources for the proper and timely assessment or risks, including through on-site general inspections in the seven largest private banks (SB). A new reporting to be obtained as of end-June will help assess whether consolidated supervision should be introduced earlier than in 2018, the current target under the authorities' plans.

34. The authorities have launched several initiatives to boost financial inclusion (¶31). Access to finance is limited, according to World Bank estimates, to 36 percent of the adult population. The policies to be implemented during the program include:

- **Development of private credit bureaus**, which will complement the CBT's "Centrale de Risques" with more exhaustive data collection that will eventually lead to a better risk analysis, and will facilitate lending to non-connected clients.

- **Revising the law on excessive lending rates**. The main objective of this law is to protect borrowers from excessive rates, but low ceilings and no consideration of loan size or of the nature of borrowers led to the exclusion of many households and SMEs from access to finance. The authorities recognize that this regulation should be improved by increasing the cap on lending rates for individuals and SMEs from the current limit of 20 percent more than the average lending rate to at least 33 percent (end-December 2016 SB) while revising the existing framework to adapt to different borrower types. Identifying the appropriate ceilings by type is considered by the authorities as an essential prerequisite before considering staff proposal to eliminate the ceiling for large enterprises.

- **Strengthening financing for microfinance and SMEs**. The government plans to regroup the existing 289 microcredit associations—of which more than half do not comply with the regulatory framework—into 24 institutes (one per region) that will be governed by a new microfinance strategy. The restructuring of several public institutions specialized in development financing into a regional bank is expected to increase efficiency and open new financing opportunities in lagging regions. Staff urged caution in setting this bank, which should only work as an intermediary in partnership with existing banks where traditional financial services would not be viable, refraining from duplicating existing commercial financial service providers.

E. Improving the Business Climate

35. Removing long-standing structural obstacles to private sector development is a critical element of the authorities' strategy. Changing the existing development model—which is based on pervasive state intervention that led to an economy dependent on low-value added exports, excessive regulation, and limited competition—requires swift implementation of the recently approved legislation. In particular, implementation decrees for the competition law should reduce delays for anti-trust hearings and increase sanctions for anti-competitive behavior; and the implementation of the approved PPP law will first focus on two pilot projects and include a framework to evaluate the feasibility and fiscal risks of new PPPs (MEFP ¶32).

36. The new investment code and the simplification of procedures will improve the business environment. The new investment code, expected to be adopted by September 2016 along with its implementing decrees (MEFP ¶32), will reduce barriers to entry and protect investor rights. Importantly, tax incentives currently included in the investment code will be removed and any new incentive will be incorporated in the tax code, avoiding duplications and ensuring consistency with the authorities' tax strategy and policy priorities. The simplification of about 530 tax, customs, and business formalities completed over the past two years are expected to reduce the administrative burden faced by businesses and increase government efficiency. The completion of the impact analysis of this simplification will guide the authorities' action plan on remaining procedures (MEFP ¶33).

37. Labor market reforms will proceed gradually. The authorities continue to build consensus amongst stakeholders to finalize a national employment strategy that addresses skills mismatches, hiring/firing policies, worker protection, and public/private sector compensation. Staff urged the authorities to accelerate work in this area with technical assistance from the International Labor Organization. In the interim, the authorities plan to focus on active labor market programs for youth and marginalized regions and reform vocational training in line with the new strategy in this area (MEFP ¶34).

PROGRAM MODALITIES

38. Tunisia will face significant balance of payments needs in the next four years. A four-year arrangement under the EFF (May 11, 2016–May 10, 2020) would be appropriate to meet those needs (projected at US$11 billion over the next four years), strengthen reserves above 100 percent of the Fund's risk-weighted metric, and support the authorities' efforts to reduce the structural impediments weakening the external position and growth. Access of 375 percent of quota (SDR 2.046 billion, or US$2.8 billion) is justified based on the needed reserve coverage (Box 6). Disbursements under the proposed arrangement will be evenly phased. The first installment will be at program approval and the remaining purchases contingent on completing semi-annual reviews.

39. Donors and market access are expected to cover most of the remaining financing needs. Staff has worked in close collaboration with the World Bank, European Union, European Bank of Reconstruction and Development, African Development Bank and Tunisia's key bilateral partners in coordinating donor activity to support the authorities' reform agenda and meet their financing needs. Accordingly, external financing needs are fully covered for the first year of the program, with donors expected to provide US$2 billion (including with third-country guarantees enabling market access of about US$500 million). Good prospects exist for adequate financing for the remainder of the program, including through market access (with no third-country guarantee in 2017) and firm commitments on donor assistance that will be linked to the reform priorities underlying the authorities' five-year development plan.

Tunisia: Official External Financing, 2016–17

(Millions of US dollars)

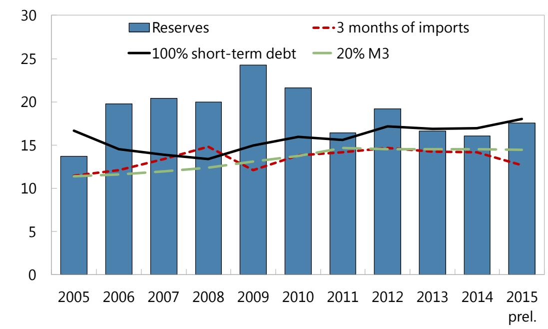
	2016					2017				
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year
Official External Financing	75.0	551.0	999.0	1,361.0	2,985.9	475.0	1,143.2	75.0	893.2	2,586.4
Project loans	65.0	65.0	65.0	65.0	260.0	75.0	75.0	75.0	75.0	300.0
Multilateral donors	-	476.0	419.0	1,281.0	2,175.9	400.0	568.2	-	318.2	1,286.4
AFDB	-	-	200.0	300.0	500.0	-	-	-	-	-
AMF (Arab Monetary Fund)	-	-	-	-	-	-	-	-	-	-
IMF (budget support starting 2017)	-	317.0	-	317.0	633.9	-	318.2	-	318.2	636.4
World Bank Group	-	50.0	-	500.0	550.0	400.0	-	-	-	400.0
European Union	-	109.0	219.0	164.0	492.0	-	250.0	-	-	250.0
Bilateral donors	-	-	-	-	-	-	-	-	-	-
Financial Market Access and other	10.0	10.0	515.0	15.0	550.0	-	500.0	-	500.0	1,000.0
Sukuk and other market financing	-	-	-	-	-	-	500.0	-	500.0	1,000.0
Market issuance with US Treasury guarantee	-	-	500.0	-	500.0	-	-	-	-	-
Loan Transfers to SOEs	10.0	10.0	15.0	15.0	50.0	-	-	-	-	-
Budget Grants	-	-	47.7	45.4	93.1	-	150.0	-	0.9	150.9

Sources: Tunisian authorities and IMF staff estimates.

Box 6. Tunisia: Reassessing Reserve Adequacy

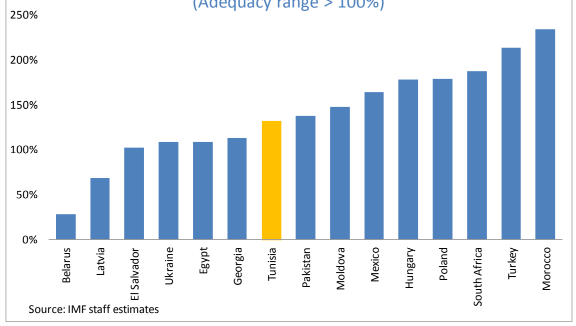
Reserve coverage improved in 2015, boosted by the January issuance of a US$1 billion Eurobond, and multilateral and bilateral disbursements. Over the medium term, greater exchange rate flexibility—and continued donor funding—is expected to correct for an overvalued exchange rate, gradually improving gross reserves and covering over four months of imports throughout the medium term. Under this scenario, reserves exceed common benchmarks, such as the three-month import coverage, 100 percent of short-term debt, and 20 percent of money supply. However, reserves are still relatively low compared to most emerging economies.

Traditional Metrics of Reserve Coverage
(In percent of GDP)



Sources: Tunisian authorities; and IMF staff calculations.

Reserves / Three Months Of Imports, 2015
(Adequacy range > 100%)

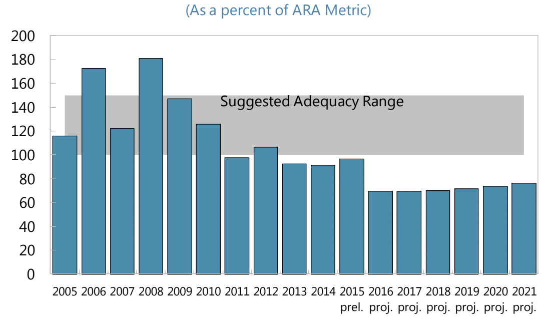


Source: IMF staff estimates

Reserves also remain below the range suggested by the IMF composite Adequacy Reserve Assessment (ARA) metric. The ARA metric for emerging countries comprises four components reflecting potential drains on the balance of payments. For Tunisia, these components (and their relative weights) are export income (10 percent), broad money (10 percent), short-term debt (30 percent), and other liabilities (20 percent). Using the unadjusted Reserves Adequacy Metric (no capital controls and fixed exchange rate regime for 2016 onwards), reserves would fall short of the suggested adequacy range of 100–150 percent.

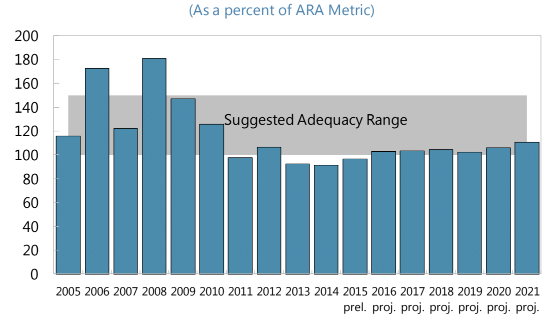
Adjusting the ARA metric to account for existing capital controls improves Tunisia's reserve adequacy. Theoretical and empirical studies have suggested that capital controls could reduce debt and equity outflows as well as reduce the probability of exchange rate market pressure. For the ARA metric, this translates into halving the weights on broad money and other liabilities to reflect lower risk of resident and non-resident assets flight, respectively (see IMF 2014 for more details).[1] Applying this to Tunisia suggest an improvement in its reserve coverage, with reserves crossing the bottom threshold of the satisfactory ARA adequacy range starting 2016 and gradually improving over the medium term under a Fund-supported program.[2]

Reserves Adequacy (Unadjusted 1/)
(As a percent of ARA Metric)



Sources: Tunisian authorities; and IMF staff calculations.
1/ The unadjusted metric assumes no capital controls throughout and a fixed exchange rate regime in 2016 onwards.

Reserves Adequacy (Adjusted 1/)
(As a percent of ARA Metric)



Sources: Tunisian authorities; and IMF staff calculations.
1/ The adjusted metric assumes a floating exchange rate regime and lifting of capital controls in 2019 onwards.

[1] IMF (2014) "Assessing Reserve Adequacy—Specific Proposals", IMF Board Paper SM/14/334, Washington, D.C.
[2] The graph below reflects reserves including Fund disbursements under the proposed EFF.

40. With the exception of the second tranche, Fund resources will be used for budgetary financing. For 2016, the first tranche at program approval will be made available to the budget to hedge against lingering uncertainties about the exact timing of donor disbursements in the course of 2016. Large amortization payments and protracted fiscal needs from 2017 onwards call for using IMF resources for fiscal support. All use of Fund resources for budget support will be governed by a Memorandum of Understanding regarding the respective responsibilities of the Ministry of Finance and the CBT for servicing charges and obligations to the Fund.

41. The program will be monitored through semi-annual reviews, based on: (i) quantitative performance criteria focused on fiscal, monetary and external objectives; (ii) indicative targets on domestic arrears and social spending; (iii) structural benchmarks focused on reforming the financial sector, budget policy and public institutions, and the business climate (MEFP, Tables 1-2). Prior actions in the banking sector and on the tax strategy were undertaken by the authorities to signal commitment to the reform agenda (Box 7).

42. Tunisia has the capacity to repay the Fund. Tunisia has a strong record of payments to the Fund, and standard indicators of Fund exposure remain low: (i) the stock of outstanding Fund credit would peak in 2020 at 5.7 percent of GDP, and 14.1 percent of exports of goods and services, before gradually declining; and (ii) obligations to the Fund remain modest and peak at 6.4 percent of gross reserves (1.3 percent of GDP) in 2018 (Table 10). Total external debt is projected to peak in 2018 at below 75 percent of GDP, and public debt will stabilize below 55 percent of GDP at its peak, albeit vulnerable to exchange rate risks and a combined macro-fiscal shock. Even under conservative assumptions on tourism and remittances flows, external debt is expected to start declining by the end of the program whereas public debt will decline to under 50 percent of GDP (Table 8, DSA Annexes).

43. The proposed program carries considerable risks (Box 2). Increased security tensions represent the main risk as it could shift policymakers' focus away from economic reforms and increase investors' wait-and-see attitude. Public disillusionment over high levels of unemployment, electoral campaigning ahead of the municipal elections, or a weakened political support for the government's reform agenda could slow politically and socially sensitive reforms. A rebound in oil prices and further deterioration of the external economic environment could weaken growth and add pressures on the fiscal and external position. Delays in reform implementation could also postpone donor disbursements and create a financing shortfall.

44. Several program features mitigate existing risks. Program design builds early momentum towards the most critical reforms, which are expected to catalyze significant donor support, both technical and financial. The authorities' strong commitment to reform, the creation of the high-level reform implementation committee at the Prime Minister's office, and the broad political consensus built around the five-year plan are important risk-mitigating factors. Six-month Reviews, with interim visits, would allow for early remedial actions in case of program slippages.

45. An updated safeguards assessment is being finalized. The external audit arrangements continue to be sound and financial statements are published on a timely basis. While progress has

been made by the adoption of the new central bank law, new amendments are needed—particularly on greater autonomy(¶17)—in order to align the law with best international practices.

Box 7. Tunisia: Extended Fund Facility

Access: SDR 2.045625 billion (375 percent of quota, equivalent to about US$2.865 billion)

Length: 48 months, starting May 2016

Phasing: There are eight program reviews and nine disbursements. Disbursements will be even-phased (see Table 9).

Quantitative Performance Criteria

- Ceiling on the primary balance of the central government, cash basis and excluding grants
- Ceiling on net domestic assets of the central bank; Ceiling on current primary expenditures
- Floor on net international reserves of the central bank

Continuous Performance Criteria

- Ceiling on the accumulation of new external debt payment arrears by the central government

Quantitative Indicative Targets

- Floor on social spending; Ceiling on the accumulation of new domestic arrears

Prior Actions

- Approval, by banks' boards, of the updated business plans for all three public banks.
- Adoption, by the Assembly, of the People's Representatives (ARP), of the CBT law, the banking law, and the bankruptcy law in line with good international practices.
- Adoption, by the Council of Ministers, of the comprehensive tax reform strategy, in line with the principles of fairness and efficiency agreed with IMF staff.

Structural Benchmarks

- Approval, by the Board of Directors of public banks (STB, BH, and BNA), of performance contracts in line with their new restructuring plans, June 2016
- Approval, by the Council of Ministers, of a comprehensive strategy on civil service reform, September 2016
- Signature of performance contracts for the five largest public enterprises, September 2016
- Adoption of the implementation decrees for the new law on competition, law on PPPs, and new investment code, September 2016
- Increase of the cap on lending rates to, at least, the 2009 level, December 2016
- Systematic use, by the supervisors, of the new manual on risk-based supervision, December 2016
- Completion of the functional review of four ministries (Health, Education, Finance, and Infrastructure), December 2016
- Publication, in the official journal, of the organic budget law, December 2016
- Establishment of a Large Taxpayers Unit to include formal responsibility for major tax and enforcement functions (return processing, taxpayer advisory services, and audit), December 2016
- Adoption of a medium-term debt strategy, December 2016
- Creation of an independent, high anti-corruption authority, December 2016.

STAFF APPRAISAL

46. Tunisia's economy has shown resilience but continues to face important challenges. Social and security tensions dampen immediate prospects for recovery despite a more favorable external economic environment and low international oil prices. External imbalances persist, budget composition has worsened, and the financial sector does not provide sufficient support to the economy. These vulnerabilities underlie the importance of forcefully tackling the long-standing structural weaknesses of Tunisia's economy.

47. Strong policy action is needed to address critical constraints on growth and consolidate macroeconomic stability. The Fund-supported program—built on the authorities' five-year vision—is appropriately focused on consolidating macroeconomic stability and promoting a more inclusive growth. To underpin these goals, early and decisive action is needed on key structural reforms that may be difficult politically and socially but will yield the largest gains in terms of economic opportunities, create jobs and help establish a virtuous cycle of renewed confidence and higher inclusive economic growth. Inaction or delays in the implementation would be costly as they would risk undermining macroeconomic stability maintained so far, and disappointing the aspirations of the Tunisian people.

48. Staff welcomes the authorities' commitment to put debt firmly on a downward path. Further reduction of the structural fiscal deficit would ease financing constraints, reduce external imbalances, and ensure fiscal sustainability. A reduction of current spending and greater revenue mobilization—including through a more progressive and efficient tax system and a wider tax base via further reductions of exemptions—will create space for priority investment and better-targeted social spending. It will also require moving towards an integrated tax administration.

49. Civil service reform is needed to improve public service delivery and underpin fiscal consolidation. Recent increases in public sector employment and wages are unsustainable. Staff welcomes the authorities' commitment to conduct functional reviews of ministries, align the increase in the 2017 wage bill to inflation, and reduce the wage bill to 12 percent of GDP by 2020. All these elements are part of the comprehensive civil service reform aimed at increasing the efficiency of public services. The soon-to-be adopted civil service reform strategy should ensure the success of the reform and sustainability of the fiscal position, including through clearly stating the need to avoid unnecessary hiring in the already large public sector and refrain from additional wage increases.

50. Energy subsidy reform needs to be accompanied by programs to protect the most vulnerable. Staff welcomes the lowering of fuel prices and the planned introduction of an improved automatic price mechanism, which should be implemented on a monthly basis to ensure close alignment with international prices. Further rationalization of electricity subsidies is welcome, as is the introduction of a lifeline tariff for the poor. The introduction of a new social identification number and a new database on vulnerable households will pave the way for a better-targeted social

safety net. In the meantime, human development and social assistance programs should be protected, as signaled by the inclusion of an indicative floor on social spending in the program.

51. Fiscal risks will need to be carefully monitored. Large losses and weak governance in SOEs are important vulnerabilities. The introduction of an SOE monitoring agency and new performance contracts are urgently needed to mitigate risks. The financial viability of the public pension system should be restored. A medium-term debt strategy and close cooperation among agencies on cash and debt management will improve program monitoring, transparency, and policy coordination.

52. Efforts to strengthen governance should be accelerated. The implementation of a new organic budget law will improve data dissemination, budget preparation and execution, and government accountability. Anti-corruption efforts and further strengthening of statistical data will help reduce fiscal risks, and inform sound policies.

53. Monetary policy should remain prudent. Staff welcomes the authorities' readiness to raise interest rates should inflationary pressures materialize. Enhanced central bank independence, following the adoption of the new central bank law, the establishment of an emergency liquidity framework, and better communication of the CBT objectives will improve the monetary transmission channels and facilitate the transition to an inflation targeting framework.

54. Greater exchange rate flexibility will strengthen reserve buffers and gradually reduce dinar overvaluation. Reduced FX interventions, regular FX auctions, and a deeper FX market—made possible by recent relaxation of restrictions on FX use by banks—will help promote greater exchange rate flexibility and improve banks' liquidity management. This is critical in view of the high external current account deficits and rising external debt.

55. Moving forward on banking sector reforms is essential to reduce lingering fragilities and boost financial inclusion. Strengthening banking sector resilience requires continued progress on public bank restructuring, a proper resolution framework, and a risk-based supervision system that is enhanced by on-site inspections and has adequate resources. Public banks should make all efforts to stay above regulatory requirements, and remedial actions in case of breach should be swift and decisive. Developing credit bureaus, relaxing existing caps on lending rates, and developing microfinance institutions will increase access to finance—a key constraint to growth.

56. Improvements in Tunisia's business climate are necessary to deliver more sustainable growth. The adoption of the competition and PPP laws, and of their implementation decrees, will enhance the private sector's role in the economy. The new investment code and more simplified procedures will reduce red tape and help ensure a level playing field for investors. The continued gradual reduction of the dichotomy between onshore and offshore corporate tax rates will help clarify policy intention to investors while reducing regional disparities. Streamlining tax incentives is also essential to reduce distortions.

57. Program risks are high. A worsening of the security situation, social unrest, political uncertainty, and opposition by vested interests are the main risks to program implementation. External shocks could also undermine economic reforms. Steadfast reform implementation and continued efforts to build consensus on reforms—manifest in the elaboration of the forthcoming government's five-year plan—can help mitigate these risks. Continued policy dialogue and program monitoring will reduce risks further.

58. In view of Tunisia's balance of payment and budget needs, the strong policies proposed by the authorities and their readiness to swiftly address unforeseen shocks, staff supports the authorities' request for a 48-month EFF for the amount of SDR 2.046 billion (375 percent of quota).

Table 1. Tunisia: Selected Economic and Financial Indicators, 2012–17

	2012	2013	2014	2015	2016	2017
				Pre.	Proj.	
Production and income (percent change)						
Real GDP	3.9	2.4	2.3	0.8	2.0	3.0
GDP deflator	5.0	4.3	5.2	4.9	5.1	3.3
Consumer price index (CPI), average	5.1	5.8	4.9	4.9	3.9	3.9
Consumer price index (CPI), end of period	5.9	5.7	4.8	4.1	4.0	3.9
Gross national savings (in percent of GDP)	16.1	14.4	14.0	12.9	14.1	15.3
Gross investment (in percent of GDP)	24.4	22.7	23.2	21.8	21.8	22.3
Central government (percent of GDP, unless indicated otherwise 1/						
Total revenue (excluding grants)	24.0	24.9	25.4	23.0	23.9	24.1
Total expenditure and net lending	29.8	32.4	29.7	28.5	28.5	28.0
Central government overall balance (excluding grants)	-5.8	-7.5	-4.3	-5.5	-4.6	-3.9
Central government overall balance (excluding grants, cash basis)	-5.5	-9.8	-5.4	-4.7	-4.6	-3.9
Structural fiscal balance 2/	-5.7	-6.4	-4.3	-4.3	-4.0	-3.3
Change in the structural fiscal balance (+: improvement)	-2.4	-0.7	2.1	0.0	0.3	0.7
Central government debt (foreign and domestic)	45.5	44.5	49.0	53.2	54.6	54.5
Foreign currency public debt (percent of total debt)	61.6	59.6	62.6	62.6	68.0	68.6
Total external debt						
External debt (US$ billions)	24.0	26.0	26.7	26.7	29.3	30.7
External debt (in percent of GDP)	52.9	57.0	61.4	63.5	69.0	71.4
Debt service ratio (percent of exports of GNFS)	12.1	9.5	8.4	10.2	12.8	16.7
Money and credit (percent change)						
Credit to the economy	8.8	6.8	9.4	6.4	7.1	7.3
Broad money (M3 of the financial system)	8.4	6.6	7.8	5.3	6.5	6.8
Velocity of circulation (GDP/M2)	1.46	1.45	1.45	1.46	1.47	1.46
External sector (percent change)						
Exports of goods, f.o.b. (in $)	-4.6	0.3	-1.9	-15.9	-2.6	5.8
Imports of goods, f.o.b. (in $)	2.1	-0.5	1.8	-18.4	-4.3	3.9
Exports of goods, f.o.b. (volume)	1.6	-0.7	-2.9	-2.8	1.6	5.5
Import of goods, f.o.b. (volume)	9.0	-0.5	2.1	-1.7	3.5	2.1
Trade balance (in percent of GDP)	-13.6	-12.8	-14.0	-11.5	-10.4	-10.1
Current account (in percent of GDP)	-8.3	-8.4	-9.1	-8.9	-7.7	-7.0
Foreign direct investment, net (in percent of GDP)	1.5	1.1	2.3	2.5	2.1	2.2
Terms of trade (deterioration -)	0.2	1.1	1.4	4.2	3.7	-1.5
Official reserves						
Gross official reserves (US$ billions, e.o.p)	8.7	7.7	7.7	7.6	8.3	8.5
In months of next year's imports of goods and services, c.i.f.	3.9	3.4	4.2	4.3	4.6	4.5
Memorandum items:						
GDP at current prices (TD millions)	70,354	75,152	80,816	85,491	91,658	97,495
GDP at current prices (US$ billions)	45.0	46.3	47.6	43.6	44.0	44.4
Real effective exchange rate (percent change, depreciation -) 3/	-1.49	-1.90	-0.20	...	...	...
Interest rate (money market rate, in percent, e.o.p)	3.3	4.8	4.7	...	...	...
Stock market TUNINDEX (12/31/1997=1000)	4,580	4,381	4,674	...	...	...

Sources: Tunisian authorities; and IMF staff estimates and projections.

1/ Excludes the social security accounts.

2/ Excludes banking recapitalization costs and one-off arrears payments for energy subsidies. Different figures from sixth SBA review account for updated output gap estimation.

3/ Information Notice System.

Table 2. Tunisia: Balance of Payments, 2013–21

(In millions of U.S. dollars)

	2013	2014	2015	2016					2017					2018	2019	2020	2021
			Projections														
	Annual	Annual	Annual	Q1	Q2	Q3	Q4	Annual	Q1	Q2	Q3	Q4	Annual				
Current account	-3,879	-4,341	-3,891	-827	-984	-854	-725	-3,390	-790	-936	-779	-608	-3,113	-2,789	-2,632	-2,568	-2,325
Trade balance	-5,930	-6,670	-5,029	-993	-1,252	-1,358	-974	-4,577	-973	-1,233	-1,354	-940	-4,500	-4,244	-4,266	-4,388	-4,369
Exports	17,049	16,733	14,073	3,510	3,597	3,070	3,535	13,712	3,703	3,796	3,256	3,746	14,501	15,154	15,952	16,696	17,401
Energy	2,591	2,204	1,013	165	155	151	145	616	197	186	180	174	737	811	874	929	976
Non-energy	14,458	14,529	13,061	3,345	3,441	2,920	3,390	13,096	3,506	3,610	3,076	3,572	13,765	14,342	15,078	15,767	16,425
Of which: Nonfood	12771	13176	11017	2,834	2,929	2,571	2,967	11300	2,976	3,078	2,713	3,132	11899	12387	13013	13576	14106
Imports	-22,979	-23,403	-19,102	-4503	-4849	-4428	-4509	-18,290	-4676	-5030	-4610	-4687	-19,001	-19,398	-20,219	-21,084	-21,771
Energy	-4,172	-4,348	-2,742	-529	-529	-541	-465	-2,064	-616	-617	-631	-544	-2,407	-2,646	-2,895	-3,151	-3,400
Non-energy	-18,807	-19,055	-16,361	-3,974	-4,320	-3,888	-4,044	-16,225	-4,060	-4,413	-3,979	-4,143	-16,594	-16,752	-17,324	-17,932	-18,371
Of which: Nonfood	-16,625	-17,035	-14,452	-3,441	-3,832	-3,409	-3,543	-14,224	-3,466	-3,868	-3,444	-3,584	-14,361	-14,461	-15,005	-15,576	-15,978
Services and transfers (net)	2,051	2,329	1,138	166	269	504	248	1,187	183	298	574	332	1,387	1,455	1,635	1,820	2,044
Nonfactor	1,621	1,442	363	25	68	234	14	341	18	67	244	16	346	325	314	283	256
Of which: Tourism	1,983	2,136	1,200	229	285	415	288	1,217	249	310	452	314	1,326	1,418	1,536	1,636	1,742
Factor Services and Transfers (net)	430	887	775	141	200	271	234	847	165	231	330	316	1,042	1,130	1,320	1,538	1,788
Of which: Workers' remittances	2,290	2,347	1,908	422	446	575	470	1,913	430	455	586	479	1,950	1,985	2,043	2,148	2,259
Interest payments on external debt	-571	-583	-566	-151	-155	-175	-118	-599	-167	-138	-160	-101	-566	-525	-466	-429	-387
Capital and financial account	3,628	4,888	4,274	82	894	1,429	1,731	4,135	737	1,031	318	1,173	3,258	3,127	3,177	3,324	2,952
Capital account	115	300	173	-4	-3	44	44	81	-3	147	-3	-3	136	57	56	56	56
Financial account	3,513	4,588	4,101	85	897	1,385	1,688	4,055	740	885	321	1,176	3,122	3,071	3,120	3,268	2,897
Direct investment and portfolio (net)	1,139	1,097	1,106	176	237	224	304	944	177	241	228	309	958	975	1,031	1,096	1,265
Medium- and long-term loans (net)	1,683	2,269	2,279	-321	346	850	1,099	1,973	349	316	-233	581	1,013	907	772	775	731
Disbursement	3,205	3,515	3,487	210	684	1,130	1,499	3,522	607	1,273	203	1,019	3,102	2,444	2,455	2,111	2,047
Amortization	-1,521	-1,245	-1,208	-531	-338	-280	-400	-1,549	-258	-957	-436	-438	-2,089	-1,537	-1,683	-1,336	-1,316
Short-term capital	691	1,222	716	166	185	2	166	737	171	191	227	171	761	794	1,166	1,260	750
of which: change in NFA of commercial banks	-248	670	161	31	70	51	55	209	20	64	48	53	185	187	72	62	63
Valuation changes	...	...	-15	65	129	91	115	400	43	136	100	112	390	396	152	137	150
Errors and omissions 1/	-714	-577	-394	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Overall Balance	-965	-29	-11	-745	-90	575	1,006	745	-53	96	-462	565	145	339	545	756	627
Changes in gross reserves (+ = accumulation)	-965	-29	-26	-745	-90	575	958	745	-53	96	-462	555	145	339	545	756	627
of which: IMF (net)	150	1046	299	0	317	-17	300	599	-17	243	-100	193	319	120	253	142	-133
Memorandum items:																	
Current account balance/GDP (percent)	-8.4	-9.1	-8.9	-1.9	-2.2	-1.9	-1.6	-7.7	-1.8	-2.1	-1.8	-1.4	-7.0	-6.2	-5.5	-5.1	-4.4
Reserves (in billions of US$)	7.7	7.7	7.6	6.9	6.8	7.4	8.3	8.3	8.3	8.4	7.9	8.5	8.5	8.8	9.4	10.1	10.7
Reserves in months of imports of goods and services 2/	3.4	4.2	4.3	3.8	3.7	4.0	4.6	4.6	4.4	4.5	4.2	4.5	4.5	4.5	4.6	4.7	4.8
Reserves/total short term external debt (percent) 3/	117.0	111.9	121.4	108.2	106.6	114.8	132.3	132.3	129.0	129.5	121.8	130.3	130.3	132.1	132.9	135.7	136.6
External medium- and long-term debt (billions of US$)	19.4	19.8	20.4	20.6	21.0	21.9	23.0	23.0	23.4	23.8	23.6	24.2	24.2	25.2	26.3	27.3	28.1
External medium- and long-term debt/GDP (percent)	42.6	45.6	48.5	46.0	47.9	50.6	54.1	54.1	54.1	56.3	56.3	57.9	56.3	57.9	57.2	55.9	54.3
External short-term debt (billions of US$)	6.6	6.8	6.3	6.4	6.4	6.4	6.3	6.3	6.4	6.5	6.5	6.5	6.5	6.7	7.0	7.5	7.9
External short-term debt/GDP (percent)	14.4	15.8	15.0	14.3	14.6	14.9	14.8	14.8	14.9	15.2	15.2	15.3	15.2	15.3	15.3	15.3	15.2
Debt service ratio (as percent XGS, including IMF)	9.5	8.4	10.2	16.0	11.2	11.3	9.7	12.8	9.5	23.8	14.0	11.6	16.7	13.9	13.1	9.6	8.7
Imports (percent of GDP)	49.68	49.16	43.83	39.85	43.76	40.53	41.96	41.53	41.13	45.04	41.83	43.20	42.80	43.16	42.61	41.88	40.78
Exports (percent of GDP)	36.86	35.15	32.29	31.06	32.45	28.10	32.90	31.14	32.57	34.00	29.54	34.53	32.67	33.71	33.62	33.17	32.59
National GDP in USD	46,253	47,605	43,581	11,301	11,082	10,926	10,746	44,041	11,368	11,167	11,021	10,849	44,391	44,948	47,450	50,337	53,388

Sources: Tunisian authorities; and IMF staff estimates and projections.
1/ Differs from zero in current and future years because of stocks valuation effects.
2/ End-of-year reserves over next year imports.
3/ Short-term defined as one year or less.

Table 3. Tunisia: External Financing Needs, 2012–21

(In millions of U.S. dollars)

	2012	2013	2014	2015	2016					Projections 2017					2018	2019	2020	2021
		Year	Year	Year	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year	Year	Year	Year	Year
Total financing requirements	10,886	11,607	12,155	11,944	7,685	7,849	7,714	7,429	11,244	7,427	8,282	7,650	7,354	11,510	10,834	10,989	10,952	11,101
Current account deficit	3,738	3,879	4,341	3,891	827	984	854	725	3,390	790	936	779	608	3,113	2,789	2,632	2,568	2,325
Amortizations	2,038	1,534	1,242	1,207	531	338	280	403	1,554	258	957	436	437	2,088	1,537	1,683	1,336	1,316
Central government 1/	1,227	1,036	628	597	103	188	154	225	670	142	725	327	283	1,477	1,067	1,304	992	990
Central Bank 2/	0	0	97	85	334	15	25	30	404	23	29	24	29	105	44	4	0	0
Corporate 3/	811	498	517	525	94	136	101	148	480	93	202	85	126	506	426	374	344	326
Short-term debt 4/	5,110	6,193	6,572	6,846	6,327	6,527	6,581	6,300	6,300	6,379	6,390	6,434	6,309	6,309	6,508	6,675	7,049	7,460
Total financing sources	10,886	11,606	12,155	11,944	7,685	7,849	7,714	7,429	11,241	7,427	8,282	7,650	7,354	11,510	10,834	10,989	10,952	11,101
Direct investment and portfolio (net)	1,539	1,139	1,097	1,106	176	237	224	304	944	177	241	228	309	958	975	1,031	1,096	1,265
Disbursements	3,351	3,179	3,505	3,474	210	684	1,130	1,464	3,487	607	1,273	203	1,017	3,100	2,444	2,455	2,111	2,047
Central government 1/	2,849	1,664	2,802	2,761	74	551	999	1,018	2,642	475	1,143	75	891	2,584	1,936	1,936	1,578	1,500
Central Bank 2/	0	639	0	25	0	0	0	317	317	0	0	0	0	0	0	0	0	0
Corporate 3/	502	875	703	689	136	133	131	129	529	132	130	128	126	516	507	518	533	547
Short-term debt	6,193	6,572	6,846	6,300	6,379	6,390	6,434	6,309	6,309	6,408	6,428	6,480	6,508	6,508	6,675	7,049	7,460	7,870
Other flows net (incl. drawdown in commercial banks NFA)	933	-248	679	1,051	175	448	501	310	1,246	183	435	277	75	1,090	1,079	1,000	1,042	546
Drawdown in gross reserves	-1,130	965	29	12	745	90	-575	-958	-745	53	-96	462	-555	-145	-339	-545	-756	-627
Financing gap	0	0	0	0	0	0	0	0	3	0	0	0	0	-1	0	0	0	0
Of which: Multilateral (excluding IMF), bilateral and budget grants		126	795	1,370	0	159	467	1,009	1,635	400	400	0	1	801	0	0	0	0
Financial Market Access and other		284	1,083	83	10	10	515	15	550	0	500	0	500	1,000	0	0	0	0
Fund credits, net 5/	0	150	1,046	301	0	317	-17	300	599	-17	243	-100	193	319	120	253	142	-133
Purchases	0	150	1,046	301	0	317	0	318	634	0	318	0	318	636	637	638	320	0
Repurchase	0	0	0	0	0	0	-17	-17	-34	-17	-75	-100	-125	-318	-517	-385	-178	-133
Memorandum items:																		
Gross international reserves (in millions of U.S. dollars)	8,655	7,689	7,660	7,648	6,903	6,812	7,388	8,346	8,346	8,293	8,388	7,926	8,481	8,481	8,820	9,365	10,121	10,748
Government rollover rates (in percent)	232	222	446	467	72	293	650	594	442	334	158	23	315	175	182	148	159	152
Corporate rollover rates (in percent)	62	176	136	131	144	98	130	87	110	143	64	151	100	102	119	138	155	168

Sources: Tunisian authorities; and IMF staff projections.

1/ Central government includes IMF money going to budget support

2/ Central Bank includes IMF money going to BOP support

3/ Includes public and private entreprises.

4/ Stock of short-term debt outstanding at end of previous year

5/ Under the proposed schedule of purchases during the EFF.

Table 4a. Tunisia: Central Government Fiscal Operations, 2012–18

(In millions of dinars)

	2012	2013	2014	2015	2016					2017	2018
				Annual	Annual	Q1	Q2	Q3	Q4		
				Est.				Proj.			
Total revenue and grants	17,517	18,812	20,860	19,941	22,107	5,170	5,250	5,650	6,037	23,793	25,579
Revenue	16,888	18,702	20,494	19,649	21,910	5,170	5,250	5,550	5,940	23,464	25,417
Tax revenue	14,864	16,333	18,580	18,487	19,860	4,975	4,700	5,000	5,185	21,607	23,435
Direct taxes	6,090	7,118	8,168	7,816	8,149	2,101	1,718	2,120	2,210	8,872	9,475
Trade taxes	715	729	809	825	523	171	110	110	132	654	802
VAT	4,376	4,449	5,106	5,057	5,686	1,309	1,478	1,421	1,478	6,368	7,053
Excise	1,598	1,547	1,685	1,773	2,277	543	569	569	596	2,554	2,728
Other taxes	2,086	2,490	2,812	3,016	3,225	851	825	780	769	3,160	3,377
Nontax revenue	2,024	2,320	1,910	1,158	2,046	194	550	550	752	1,852	1,978
Of which: ETAP and STIR 1/	...	...	759	526	504	...	...	...	...	...	...
Grants	629	110	366	292	197	0	0	100	97	329	162
Total expenditure and net lending	20,949	24,362	24,007	24,340	26,097	6,827	5,641	6,276	7,353	27,250	29,262
Total expenditure	21,299	24,363	23,587	23,672	26,157	6,784	5,671	6,286	7,416	27,150	29,161
Current expenditure	16,608	20,639	20,093	19,729	21,584	5,815	4,771	5,394	5,604	21,788	23,018
Wages and salaries	8,655	9,608	10,541	11,542	12,960	3,694	3,000	3,150	3,116	13,471	14,394
Of which: one-off civil service reform costs	-	-	-	-	-	-	-	-	-	-	*505*
Of which: Ministry of Defense and Interior	...	... .	...	*2,752*	3,100	...	...	...	...	3,223	3,346
Goods and services	1,167	1,200	1,489	1,682	2,168	476	400	608	684	1,939	2,114
Interest payments	1,268	1,411	1,516	1,641	1,860	626	421	436	377	2,035	1,992
Transfers and subsidies	5,518	7,539	6,546	4,864	4,496	1,019	950	1,200	1,327	4,343	4,519
CGC (Food)	1,242	1,450	1,417	1,530	1,600	391	300	400	509	1,633	1,698
Energy subsidies (gross) 1/	2,689	4,434	3,112	918	166	0	50	50	66	194	209
Other (including transfer to CNRPS)	1,587	1,655	2,017	2,416	2,730	628	600	750	752	2,516	2,612
Other expenditure (non-allocated)	-	880	-	-	100	-	-	-	100	-	-
Capital expenditure	4,692	3,725	3,495	3,943	4,573	969	900	892	1,812	5,362	6,143
Net lending	-351	-1	420	669	-60	43	-30	-10	-63	100	101
Of which: Public banks' recap. and restructuring	*41*	-	-	*647*	-	-	-	-	-	-	-
Central government overall balance (excluding grants)	-4,061	-5,660	-3,513	-4,692	-4,187	-1,657	-391	-726	-1,413	-3,787	-3,845
Central government overall balance (including grants)	-3,431	-5,550	-3,147	-4,400	-3,990	-1,657	-391	-626	-1,316	-3,457	-3,683
Float 2/	211	-1,698	-824	702	-	757	-965	-200	409	-	-
Central government overall balance (excluding grants, cash basis)	-3,849	-7,358	-4,337	-3,990	-4,187	-900	-1,356	-926	-1,004	-3,787	-3,845
Central government overall balance (including grants, cash basis)	-3,220	-7,248	-3,971	-3,698	-3,990	-900	-1,356	-826	-907	-3,457	-3,683
Financing, net	3,220	7,248	3,971	3,698	3,990	900	1,356	826	907	3,457	3,683
Foreign	2,524	1,080	3,711	4,268	4,155	-59	750	1,773	1,691	2,434	2,015
Drawings	4,450	2,742	4,783	5,441	5,555	150	1,139	2,095	2,170	5,681	4,485
Amortization	1,926	1,662	1,072	1,173	1,400	209	389	323	479	3,247	2,470
Domestic financing	1,297	4,527	1,464	-611	-165	959	606	-947	-784	1,024	1,668
Debt	657	510 0	990	590	400	59	628	680	-967	684	136
Drawings	1,582	1,843	3,268	2,381	2,300	764	750	750	37	2,000	2,136
Amortization	925	1,333	2,277	1,792	1,900	705	122	70	1,004	1,316	2,000
Non-debt	-281	3,427	232	-934	-565	901	-22	-1,627	184	340	1,532
Government Deposits (+ = drawing / - = accumulation)	-675	2,948	140	-1,004	-765	901	-122	-1,627	84	140	1,332
Privatization proceeds and sale of confiscated assets 3/	394	479	92	70	200	-	100	-	100	200	200
Memorandum items:											
Central government primary balance (excluding grants, cash basis)	-2,582	-5,947	-2,822	-2,349	-2,327	-274	-935	-490	-627	-1,752	-1,853
Structural fiscal balance 4/	-4,035	-4,844	-3,496	-3,711	-3,691	...	...	...	...	-3,254	-2,864
Central government debt 5/	31,987	33,479	39,560	45,490	50,045	...	...	...	...	53,162	55,313
Nominal GDP	70,354	75,152	80,816	85,491	91,658	...	...	...	...	97,495	104,116

Sources: Tunisian authorities; and IMF staff estimates.

1/ Energy subsidies used to be accounted as expenses net of revenue streams from utilities and fuel companies. The series has been revised to report gross flows of revenues from the commercialization of fuel of Entreprise Tunisienne d’Activités Pétrolières (ETAP) and from operational surplus of Société Tunisienne des Industries de Raffinage (STIR). Revenues beyond 2016 are not

2/ Difference between the cash and accrual central government overall deficit data calculated at the end of the period. For actual data, this line also includes payments for which payment has been ordered but the corresponding amounts have not been withdrawn from the treasury accounts. A negative sign implies higher cash spending than ordered (i.e. higher required financing).

3/ Includes mostly the sale of confiscated assets.

4/ Excludes banking recapitalization costs and one-off arrears payments for energy subsidies.

5/ Gross debt.

Table 4b. Tunisia: Central Government Fiscal Operations, 2012–21

(In percent of GDP)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
			Prel.	Est.			Proj.			
Total revenue and grants	24.9	25.0	25.8	23.3	24.1	24.4	24.6	25.0	25.0	25.0
Revenue	24.0	24.9	25.4	23.0	23.9	24.1	24.4	24.9	24.8	24.8
Tax revenue	21.1	21.7	23.0	21.6	21.7	22.2	22.5	22.9	22.8	22.8
Direct taxes	8.7	9.5	10.1	9.1	8.9	9.1	9.1	9.2	9.2	9.2
Trade taxes	1.0	1.0	1.0	1.0	0.6	0.7	0.8	0.9	0.9	0.9
VAT	6.2	5.9	6.3	5.9	6.2	6.5	6.8	7.0	6.9	6.9
Excise	2.3	2.1	2.1	2.1	2.5	2.6	2.6	2.6	2.6	2.6
Other taxes	3.0	3.3	3.5	3.5	3.5	3.2	3.2	3.2	3.2	3.2
Nontax revenue	2.9	3.1	2.4	1.4	2.2	1.9	1.9	2.0	2.0	2.0
Of which: ETAP and STIR *1/*	…	…	0.9	0.6	0.5	…	…	…	…	…
Grants	0.9	0.1	0.5	0.3	0.2	0.3	0.2	0.1	0.1	0.1
Total expenditure and net lending	29.8	32.4	29.7	28.5	28.5	28.0	28.1	27.3	26.9	26.6
Total expenditure	30.3	32.4	29.2	27.7	28.5	27.8	28.0	27.2	26.8	26.6
Current expenditure	23.6	27.5	24.9	23.1	23.5	22.3	22.1	20.8	19.8	19.4
Wages and salaries	12.3	12.8	13.0	13.5	14.1	13.8	13.8	12.7	12.0	11.7
Of which: One-off civil service reform costs	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.5*	*0.0*	*0.0*	*0.0*
Of which: Ministry of Defense and Interior	*2.7*	*2.9*	*3.1*	*3.2*	*3.4*	*3.3*	*3.2*	*3.1*	*3.0*	*2.8*
Goods and services	1.7	1.6	1.8	2.0	2.4	2.0	2.0	2.0	2.0	2.0
Interest payments	1.8	1.9	1.9	1.9	2.0	2.1	1.9	1.7	1.4	1.3
Transfers and subsidies	7.8	10.0	8.1	5.7	4.9	4.5	4.3	4.4	4.4	4.4
CGC (Food)	1.8	1.9	1.8	1.8	1.7	1.7	1.6	1.5	1.4	1.3
Energy subsidies (gross) 1/	3.8	5.9	3.9	1.1	0.2	0.2	0.2	0.2	0.2	0.2
Other (including transfer to CNRPS)	2.3	2.2	2.5	2.8	3.0	2.6	2.5	2.6	2.8	2.9
Other expenditure (non-allocated)	0.0	1.2	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Capital expenditure	6.7	5.0	4.3	4.6	5.0	5.5	5.9	6.5	7.0	7.2
Net lending	-0.5	0.0	0.5	0.8	-0.1	0.1	0.1	0.1	0.1	0.1
Of which: Public banks' recap. and restructuring	*0.1*	*0.0*	*0.0*	*0.8*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
Central overall government balance (-) (excluding grants)	-5.8	-7.5	-4.3	-5.5	-4.6	-3.9	-3.7	-2.4	-2.0	-1.8
Central overall government balance (-), (including grants)	-4.9	-7.4	-3.9	-5.1	-4.4	-3.5	-3.5	-2.3	-1.9	-1.7
Float 2/	0.3	-2.3	-1.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0
Central government overall balance (-), (excluding grants, cash basis)	-5.5	-9.8	-5.4	-4.7	-4.6	-3.9	-3.7	-2.4	-2.0	-1.8
Central government overall balance (-), (including grants, cash basis)	-4.6	-9.6	-4.9	-4.3	-4.4	-3.5	-3.5	-2.3	-1.9	-1.7
Financing, net	4.6	9.6	4.9	4.3	4.4	3.5	3.5	2.3	1.9	1.7
Foreign	3.6	1.4	4.6	5.0	4.5	2.5	1.9	1.3	1.2	1.0
Domestic	1.8	6.0	1.8	-0.7	-0.2	1.1	1.6	0.9	0.7	0.7
Of which: Bank recapitalization	0.6	0.6	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Of which: Privatization proceeds and sale of confiscated assets 3/	0.6	0.6	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Memorandum items:										
Central government primary balance (excluding grants, cash basis)	-3.7	-7.9	-3.5	-2.7	-2.5	-1.8	-1.8	-0.7	-0.6	-0.5
Structural fiscal balance 4/	-5.7	-6.4	-4.3	-4.3	-4.0	-3.3	-2.8	-2.1	-1.9	-1.8
Change in the structural fiscal balance (+: improvement)	…	-0.7	2.1	0.0	0.3	0.7	0.6	0.6	0.2	0.1
Central government debt 5/	45.5	44.5	49.0	53.2	54.6	54.5	53.1	50.9	48.7	46.4

Sources: Tunisian authorities; and IMF staff estimates.

1/ Energy subsidies used to be accounted as expenses net of revenue streams from utilities and fuel companies. The series has been revised to report gross flows of revenues from the commercialization of fuel of Entreprise Tunisienne d'Activités Pétrolières (ETAP) and from operational surplus of Société Tunisienne des Industries de Raffinage (STIR). Revenues beyond 2016 are not forecasted. A smoothing fuel mechanism is expected to be implemented on July 1, 2016, to bridge the gap between domestic and international prices; surplus dividends linked to this mechanism are not expected.

2/ Difference between the cash and accrual central government overall deficit data calculated at the end of the period. For actual data, this line also includes payments for which payment has been ordered but the corresponding amounts have not been withdrawn from the treasury accounts. A negative sign implies higher cash spending than ordered (i.e. higher required financing).

3/ Includes mostly the sale of confiscated assets.

4/ Excludes banking recapitalization costs and one-off arrears payments for energy subsidies.

5/ Gross debt.

Table 5. Tunisia: Monetary Survey, 2013–17

(In millions of dinars)

	2013	2014	2015 Q3	2015 Q4	2015 Annual	2016 Q1	2016 Q2	2016 Q3	2016 Q4	2016 Annual	2017
		Prel.	Proj.								
	(In millions of dinars)										
Net foreign assets (NFA)	3,865	2,173	1,404	1,679	1,679	572	-1,040	107	1,406	1,406	693
Foreign assets	15,027	16,764	16,441	17,856	17,856	16,100	15,967	17,227	19,351	19,351	20,054
Central bank	12,701	14,294	13,719	15,075	15,075	13,296	13,107	14,327	16,392	16,392	16,946
Foreign liabilities	-11,162	-14,591	-15,037	-16,177	-16,177	-15,528	-17,007	-17,121	-17,945	-17,945	-19,360
Central bank	-3,004	-5,043	-5,396	-5,991	-5,991	-5,377	-6,653	-6,617	-7,263	-7,263	-7,976
Net domestic assets (NDA)	50,684	56,628	58,484	60,213	60,213	61,371	63,717	63,321	64,527	64,527	69,691
Domestic credit	65,660	74,829	78,022	80,517	80,517	82,450	84,948	84,169	86,520	86,520	94,402
Credit to the government (net)	8,794	12,619	13,625	14,355	14,355	15,924	15,845	15,281	15,655	15,655	18,351
Central bank net credit	-175	1,242	1,233	688	688	1,951	2,394	767	1,191	1,191	2,776
Commercial banks	4,111	5,807	6,635	7,199	7,199	7,506	6,983	7,527	7,359	7,359	7,633
Other	4,858	5,570	5,757	6,468	6,468	6,467	6,467	6,987	7,105	7,105	7,942
Credit to the economy	56,866	62,210	64,397	66,162	66,162	66,526	69,103	68,888	70,865	70,865	76,052
Other items (net)	-14,976	-18,200	-19,538	-20,304	-20,304	-21,079	-21,230	-20,848	-21,993	-21,993	-24,712
Money plus quasi-money (M2)	51,686	55,908	56,892	58,821	58,821	58,895	59,387	60,098	62,472	62,472	66,690
Money (M1)	20,877	22,542	23,375	24,434	24,434	24,780	24,304	24,692	25,950	25,950	27,702
Currency	7,236	8,084	8,569	8,419	8,419	8,604	8,558	9,052	8,941	8,941	9,545
Demand deposits	13,641	14,458	14,806	16,015	16,015	16,175	15,746	15,640	17,009	17,009	18,157
Quasi-money	30,809	33,366	33,517	34,387	34,387	34,430	34,718	35,134	36,522	36,522	38,987
Long-term deposits (M3-M2)	2,863	2,893	2,996	3,071	3,071	3,048	3,290	3,329	3,461	3,461	3,695
Broad money (M3)	54,549	58,802	59,888	61,892	61,892	61,943	62,677	63,427	65,933	65,933	70,384
	(Annual rate of change in percent)										
Net foreign assets	-45.2	-43.8	-38.3	-22.8	-22.8	-82.4	-155.6	-92.4	-16.2	-16.2	-50.7
Net domestic assets	14.9	11.7	5.1	6.3	6.3	9.3	11.0	8.3	7.2	7.2	8.0
Domestic credit	13.2	14.0	7.3	7.6	7.6	11.0	12.1	7.9	7.5	7.5	9.1
Credit to government (net)	83.5	43.5	14.2	13.8	13.8	42.0	36.0	12.2	9.1	9.1	17.2
Credit to the economy	6.8	9.4	6.0	6.4	6.4	5.5	7.7	7.0	7.1	7.1	7.3
Money and quasi-money (M2)	7.0	8.2	3.2	5.2	5.2	4.2	5.5	5.6	6.2	6.2	6.8
Broad money (M3)	6.6	7.8	3.4	5.3	5.3	4.3	5.7	5.9	6.5	6.5	6.8
	(Annual growth rates, in percent of broad money)										
Net foreign assets	-6.2	-3.1	-1.5	-0.8	-0.8	-4.5	-4.9	-2.2	-0.4	-0.4	-1.1
Net domestic assets	12.8	10.9	4.9	6.1	6.1	8.8	10.6	8.1	7.0	7.0	7.8
Domestic credit	14.9	16.8	9.2	9.7	9.7	13.7	15.4	10.3	9.7	9.7	12.0
Credit to the government (net)	7.8	7.0	2.9	3.0	3.0	7.9	7.1	2.8	2.1	2.1	4.1
Credit to the economy	6.8	9.4	6.0	6.4	6.7	5.8	8.3	7.5	7.6	7.6	7.9
Other items (net)	-2.1	-5.9	-4.3	-3.6	-3.6	4.0	5.2	5.4	5.9	5.9	6.4
Memorandum items:											
GDP (in millions of dinars)	75,152	80,816	…	…	85,491	…	…	…	…	91,658	97,495

Sources: Tunisian authorities; and IMF staff estimates and projections.

Table 6. Tunisia: Central Bank Survey, 2013–17

(In millions of dinars)

	2013	2014	2015 Q3	2015 Q4	2015 Annual	2016 Q1	2016 Q2	2016 Q3	2016 Q4	2016 Annual	2017
Net Foreign Assets	9,696	9,251	8,324	9,084	9,084	7,919	6,454	7,710	9,129	9,129	8,970
Assets	12,701	14,294	13,719	15,075	15,075	13,296	13,107	14,327	16,392	16,392	16,946
of which: proceeds of FX swaps					606	606	606	606	606	606	606
Liabilities	3,004	5,043	5,396	5,991	5,991	5,377	6,653	6,617	7,263	7,263	7,976
Net Domestic Assets	1,382	1,688	3,579	1,924	1,924	3,220	4,887	3,498	2,191	2,191	2,341
Domestic credit (net)	3,493	4,358	6,413	4,897	4,897	6,958	8,491	6,893	5,996	5,996	7,004
Net credit to government 1/	-175	1,242	1,233	688	688	2,234	2,774	1,147	1,231	1,231	2,816
Credit to Banks	3,668	3,116	5,180	4,209	4,209	4,724	5,717	5,746	4,766	4,766	4,188
Other items net	-2,111	-2,669	-2,834	-2,973	-2,973	-3,737	-3,604	-3,394	-3,805	-3,805	-4,662
Reserve Money 2/	11,078	10,939	11,903	11,009	11,009	11,139	11,341	11,208	11,320	11,320	11,311
Memorandum items:											
FX swap operations					606	606	606	606	606	606	606
Total refinancing of banks by the CBT (except OMPs)					4,815	5,330	6,323	6,352	5,372	5,372	4,794

Sources: Central Bank of Tunisia; and IMF staff estimates.

1/ Includes subscription to IMF/AMF.

2/ Excludes deposits of other financial institutions, individuals, and nonfinancial enterprises.

Table 7. Tunisia: Financial Soundness Indicators of the Banking Sector, 2008–15

(In percent, unless otherwise indicated)

	2008	2009	2010	2011	2012	2013	2014	2015 Prel.
Regulatory capital to risk-weighted assets	11.7	12.2	11.6	11.9	11.8	8.2	9.4	12.2
Tier 1 capital to risk weighted assets	10.6	10.7	10.2	10.0	9.5	6.6	7.6	9.5
Capital to assets	8.1	8.5	8.4	8.5	7.8	5.6	6.2	7.9
Asset quality								
Sectoral distribution of loans to total loans								
Industry	31.3	30.0	30.5	28.6	27.9	27.8	27.2	27.3
Agriculture	3.6	3.4	2.9	2.9	2.8	2.8	2.8	2.6
Commerce	17.3	17.4	15.0	16.0	15.4	15.1	15.6	15.6
Construction	4.5	4.9	5.9	5.6	5.4	5.5	5.7	6.1
Tourism	9.1	8.2	7.3	7.3	6.9	6.5	6.1	6.1
Households	20.1	21.6	22.1	23.4	25.4	26.2	26.2	26.4
Other	14.3	14.4	16.3	16.3	16.2	16.0	16.4	15.9
FX-loans to total loans	3.9	4.5	5.3	5.1	4.8	4.8	5.5	5.8
Credit to the private sector to total loans	71.6	70.4	70.6	67.4	67.7	73.8	73.8	73.6
Nonperforming Loans (NPLs) to total loans	15.5	13.2	13.0	13.3	14.9	16.5	15.8	16.0
Specific provisions to NPLs	...	...	...	48.6	45.7	56.4	58.0	65.2
NPLs, net of provisions, to Tier 1 capital	71.1	57.9	60.3	66.2	86.3	111.8	89.9	70.2
Specific provisions to total loans	8.8	7.7	7.6	7.6	8.0	10.3	10.1	10.4
General provisions to total loans	...	...	...	0.4	0.5	0.5	0.6	0.6
Profitability								
Return on assets (ROA)	1.0	1.0	0.9	0.6	0.6	0.3	0.9	...
Return on equity (ROE)	11.2	11.7	10.2	5.9	7.2	3.0	11.2	...
Interest rate average spread (between loans and deposits)	3.6	3.5	3.5	3.0	3.0	3.3	3.1	3.0
Interest return on credit	7.0	6.4	6.2	5.7	5.4	5.9	6.4	6.3
Cost of risk as a percent of credit	1.4	1.2	1.7	1.2	1.2	1.9	1.1	...
Net interest margin to net banking product (PNB)	58.6	58.8	58.6	57.2	58.1	58.9	57.2	54.6
Operating expenses to PNB	45.4	47.2	46.5	51.1	50.3	47.3	48.5	48.3
Operating expenses to total assets	1.6	1.6	1.6	1.7	1.6	1.6	1.7	1.7
Personnel expenses to non-interest expenses	60.4	61.4	59.1	62.6	61.5	60.8	59.3	59.9
Trading and other non-interest income to PNB	21.7	22.1	21.8	22.5	20.9	21.6	22.4	23.9
Liquidity								
Liquid assets to total assets 1/	31.6	32.1	29.8	26.5	28.2	28.4	28.2	5.4
Liquid assets to short-term liabilities	124.0	119.1	104.1	89.4	89.2	92.6	96.6	80.0
Deposits to loans	98.9	100.9	94.6	87.4	89.5	89.6	88.8	87.4
Deposits of state-owned enterprises to total deposits	13.8	14.8	13.8	12.6	13.2	13.0	11.7	9.5
Sensitivity to market risk								
FX net open position to Tier 1 Capital	1.4	1.5	1.4	1.9	2.3	3.1	2.2	3.3

Source: Central Bank of Tunisia.

1/ The definition of the liquidity ratio was modified in 2015. Liquid assets now include only treasury bills and cash. Using the new definition, the end-December 2014 liquidity ratio would have been 6 percent.

Table 8. Tunisia: Illustrative Medium-Term Growth Scenario, 2011–21

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
					Proj.						
					(Change in percent)						
Real GDP growth	-1.9	3.9	2.4	2.3	0.8	2.0	3.0	3.7	4.3	4.7	4.5
Total consumption	4.5	4.6	3.3	3.6	2.5	3.1	1.2	3.3	2.9	3.5	3.7
Private consumption	4.1	4.4	3.0	4.0	1.8	1.1	2.3	3.1	4.9	4.6	4.1
Public consumption	6.1	5.2	4.3	2.6	4.8	10.1	-2.0	3.9	-3.8	-0.6	2.2
Investment	-21.4	5.3	-5.4	8.5	-2.9	4.5	5.0	7.0	7.5	8.7	8.5
Gross fixed capital formation	-12.7	6.1	0.2	-2.6	-2.5	4.5	5.0	7.0	7.5	8.7	8.5
Exports of goods and nfs 1/	-7.6	6.8	2.6	4.2	-2.8	1.6	5.5	6.1	5.0	4.7	4.6
Imports of goods and nfs 1/	3.5	8.3	4.9	2.6	-1.7	3.5	2.1	4.7	3.9	4.3	4.1
Inflation (annual average)	3.5	5.1	5.8	4.9	4.9	3.9	3.9	3.8	3.7	3.5	3.5
					(In percent of GDP)						
Gross national savings	15.7	16.1	14.4	14.0	12.9	14.1	15.3	16.6	18.0	19.2	20.8
Consolidated government 2/	4.1	2.0	-2.3	0.6	-0.4	0.8	2.2	2.6	4.5	5.1	5.5
Rest of the economy	11.6	14.2	16.6	13.5	13.3	13.2	13.2	14.0	13.5	14.1	15.3
Gross investment	23.1	24.4	22.7	23.2	21.8	21.8	22.3	22.8	23.5	24.3	25.2
Consolidated government	7.2	6.7	5.0	4.4	4.6	5.0	5.5	5.9	6.5	7.0	7.2
Rest of the Economy	15.9	17.7	17.8	18.8	17.2	16.7	16.8	16.9	17.0	17.3	18.0
Total consumption	84.4	85.0	86.8	87.8	88.9	88.3	87.9	87.5	86.5	85.4	84.5
Private consumption	66.4	66.8	68.1	69.1	69.4	67.6	68.0	67.6	68.0	67.8	67.2
Public consumption	18.0	18.2	18.6	18.7	19.4	20.7	19.9	19.9	18.4	17.6	17.2
Savings-investment gap	-7.4	-8.3	-8.4	-9.1	-8.9	-7.7	-7.0	-6.2	-5.5	-5.1	-4.4
Consolidated government	-3.1	-4.7	-7.2	-3.8	-5.0	-4.2	-3.4	-3.3	-2.0	-1.9	-1.7
Rest of the economy	-4.3	-3.6	-1.1	-5.4	-3.9	-3.5	-3.6	-2.9	-3.6	-3.2	-2.7
Memorandum items											
Nominal GDP at current prices (TD millions)	64,492	70,354	75,152	80,816	85,491	91,658	97,495	104,116	112,227	121,208	130,766
Central government debt in percent of GDP	43.1	45.5	44.5	49.0	53.2	54.6	54.5	53.1	50.9	48.7	46.4
External debt in percent of GDP	51.3	52.9	57.0	61.4	63.5	69.0	71.4	73.3	72.5	71.2	69.6
Central government balance in percent of GDP 3/	-3.6	-5.8	-7.5	-4.3	-5.5	-4.6	-3.9	-3.7	-2.4	-2.0	-1.8
Current account balance in percent of GDP	-7.4	-8.3	-8.4	-9.1	-8.9	-7.7	-7.0	-6.2	-5.5	-5.1	-4.4
Credit to the economy (yoy growth, percent)	13.4	8.8	6.8	9.4	6.4	7.1	7.3	8.1	8.3	8.6	8.0

Sources: Tunisian authorities; and IMF staff estimates.

1/ Goods and nonfactor services.

2/ Includes social security, excludes privatization receipts.

3/ Excluding grants and privatization.

Table 9. Tunisia: Schedule of Proposed Purchases under the Extended Fund Facility, 2016–20

Table 9. Tunisia: Schedule of Proposed Purchases under the Extended Fund Facility, 2016–20

Review	Availability Date	Action	Purchase: Millions of SDRs	Purchase: Percent of quota 1/	Total: Millions of U.S. dollars 2/
	May 16, 2016	Board approval of the EFF	227.292	41.7	316.971
First Review	September 30, 2016	Observance of end-June 2016 performance criteria, completion of the first review	227.292	41.7	316.971
Second Review	March 31, 2017	Observance of end-December 2016 performance criteria, completion of the second review	227.292	41.7	318.224
Third Review	September 30, 2017	Observance of end-June 2017 performance criteria, completion of the third review	227.292	41.7	318.224
Fourth Review	March 31, 2018	Observance of end-December 2017 performance criteria, completion of the fourth review	227.292	41.7	318.272
Fifth Review	September 30, 2018	Observance of end-June 2018 performance criteria, completion of the fifth review	227.292	41.7	318.272
Sixth Review	March 31, 2019	Observance of end-December 2018 performance criteria, completion of the sixth review	227.292	41.7	319.045
Seventh Review	September 30, 2019	Observance of end-June 2019 performance criteria, completion of the seventh review	227.292	41.7	319.045
Eighth Review	March 15, 2020	Observance of end-December 2019 performance criteria, completion of the eighth review	227.289	41.7	320.071
Total			2045.625	375.000	2,865.095

Source: IMF staff projections.

1/ Proposed new quota is SDR 545.2 million.

2/ Indicative amount based on the [program] exchange rate.

Table 10. Tunisia: Indicators of Fund Credit, 2014–21

	2014	2015	2016	2017	2018	2019	2020	2021
Existing and prospective Fund credit (millions of SDR)								
Disbursement	689	215	455	455	455	455	227	0
Stock	788	1003	1433	1660	1746	1926	2027	1932
Obligations	0	0	39	256	402	311	171	145
Repurchase	0	0	25	227	369	274	126	95
Charges	0	0	14	29	33	36	45	51
Stock of existing and prospective Fund credit								
In percent of quota	275.0	350.0	262.6	304.3	320.0	353.0	371.5	354.2
In percent of GDP	2.5	3.2	4.5	5.2	5.4	5.7	5.7	5.1
In percent of exports of goods and services	5.5	8.1	11.8	13.0	13.2	13.9	14.1	12.9
In percent of gross reserves	15.6	19.0	23.9	27.4	27.7	28.9	28.2	30.7
Obligations to the Fund from existing and prospective Fund arrangements								
In percent of quota	0.1	0.0	7.1	46.9	73.8	56.9	31.4	26.6
In percent of GDP	0.0	0.0	0.1	0.8	1.3	0.9	0.5	0.4
In percent of exports of goods and services	0.0	0.0	0.3	2.0	3.0	2.2	1.2	1.0
In percent of gross reserves	0.0	0.0	0.6	4.2	6.4	4.7	2.4	2.3

Source: IMF staff estimates.

Annex I. The 2013–15 SBA—Context, Design, and Outcomes

Background. The 2013-15 two-year SBA—which disbursed US$1.6 billion out of US$1.75 billion originally envisaged—was designed to assist Tunisia in maintaining its macroeconomic stability in the aftermath of the Arab Spring, while implementing an ambitious reform agenda aimed at supporting private sector development, tackling high unemployment, and reducing regional disparities. The program focused on building up fiscal and external buffers, improving the investment climate, and strengthening social safety nets. Addressing the critical vulnerabilities of the Tunisia's banking sector was a key objective of the program.

Context. The implementation of the program was complicated by a more protracted political transition process than expected, with frequent changes in governments, delayed elections and a strong legislative focus on the constitutional and political process. Policy implementation during the program was also hampered by social tensions (including strikes and work stoppages), and security tensions (starting with conflicts with Salafists, spillovers from the Libya crisis, political assassinations and, in 2015, the tragic terror attacks of Bardo, Sousse, and Tunis). Opposition by vested interests, including by some within the administration, resulted in the search for consensus taking longer than expected and reforms often turning out less ambitious than initially planned. The international economic environment—particularly growth in Europe—remained weak throughout the program, although the substantial decline in global oil prices starting in late 2014 represented a positive unexpected development.

Program design. The original ambitious program design was adapted to accommodate the exogenous nature of shocks, which were unexpected at the concept stage. Prior actions were used regularly during the program. Monitoring occurred through quarterly reviews, with a focus on timely structural reform implementation (hence the high number of benchmarks), which was seen at risk of slippage. Delays in achieving key reforms also led to combined reviews (first and second program reviews), halving of expected disbursement (5th Review) and delay in completing the review (9-month delay in completing the 6th Review, and program extension).

Program outcomes were mixed:

1. Macroeconomic outcomes—stability was maintained despite shocks, although vulnerabilities were not eliminated.

- **Growth**. Security incidents, work stoppages, and political uncertainty delayed the growth recovery. By 2015, real GDP was 10 percent lower than initially envisaged, and growth was four percentage points lower.

- **Inflation**. A reversal of the monetary policy loosening put in place in the immediate aftermath of the revolution as well as declining food/energy prices contributed to a decline in inflation, which remained in line with projections.

- **Current Account**. Low phosphate and energy exports and delayed recovery in manufactured exports, combined with high energy imports and a substantial drop in tourism flows contributed to the widening of the current account deficit.

- **Reserves** have stabilized at 2013 levels and above three months of imports coverage. Some delays in external disbursements, a worse than expected external environment, as well as continued FX interventions by the CBT contributed to a lower reserve level than originally programmed.

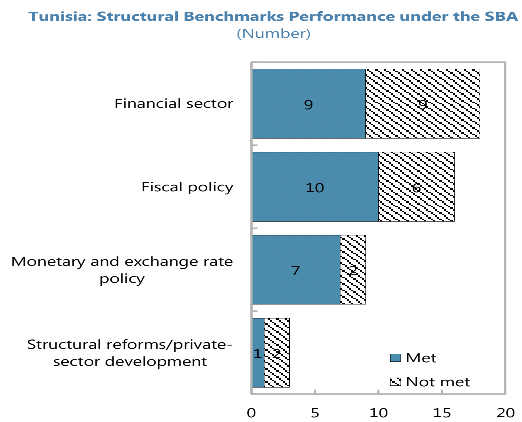
2. Macroeconomic policies—the fiscal deficit was reduced but at the cost of worsening composition.

- The **underlying fiscal stance** has improved for most of the program—with the structural fiscal balance improving even faster than initially envisaged (Annex Figure 2). The stance was appropriately loosened in 2015 to respond to the impact of terror attacks. Debt levels increased, reflecting increasing financing and one-off bank recapitalization costs consistent with program objectives. Overall, current primary spending moved in line with expectations as declining international oil prices helped reduce energy subsidies faster than programmed. Importantly, however, budget composition worsened as public investment reached historically low levels and the public sector wage bill rose steadily.

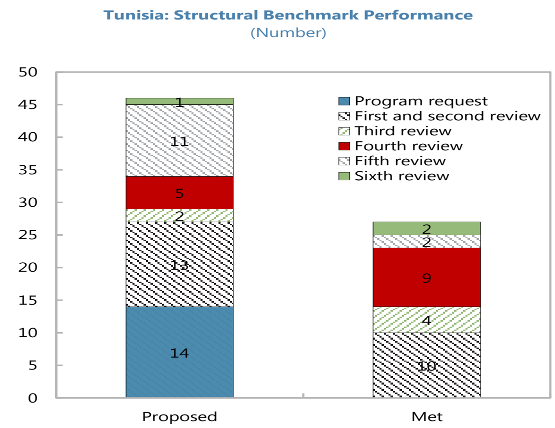
- **Monetary policy** was tightened through higher policy rates. The monetary policy framework was improved through the removal of caps on deposit rates, strengthened collateral requirements, and the introduction of a monetary policy committee. Caps on lending rates were however not eliminated.

- Some steps were taken towards **greater exchange rate flexibility**, by reducing CBT interventions (halved in the last year of the program, albeit with some increase following the terror attacks). Despite a 20 percent nominal depreciation vis-à-vis the US dollar since January 2014, the dinar remains overvalued in real terms. Progress was made towards introducing the weekly auction mechanism, which came into effect in early 2016.

3. Structural reforms—despite progress in banking reforms, there were delays, particularly for those that required parliamentary approval. In terms of structural benchmarks, 60 percent of the forty six introduced under the program were met (table and text charts).



Source: IMF Staff estimates



Source: IMF Staff estimates

- **Banking reforms.** Progress was made in addressing key vulnerabilities of the banking sector, with the restructuring of public banks—including through completing audits, recapitalizing two public banks, and initiating changes in the governance framework (including by unifying rules for public and private banks, and changes in management/Boards of banks). Advances were also made in strengthening regulations on loan classification, provisioning and liquidity, improving the design of bank reporting, and developing a bank rating system. However, the operational restructuring of public banks has yet to start, bank supervision still needs considerable strengthening, and the legal framework is not yet in line with international best practices.

- **Fiscal reforms.** (i) Progress was made in reducing energy subsidies and introducing early in the program a household compensation mechanism that could accompany an increase in domestic energy prices. (ii) National tax consultations led to the design of a comprehensive tax reform aimed at greater equity and efficiency, albeit its adoption is occurring in a piecemeal manner, which has yet to be clarified to investors. Customs modernization is ongoing while the tax administration modernization plan approved by a previous government has yet to be implemented. (iii) On PFM, changes in the procurement code and some simplification of control procedures have not yet produced their impact on accelerating the implementation public investment. Transparency during the program was improved through the introduction of a Treasury Single Account.

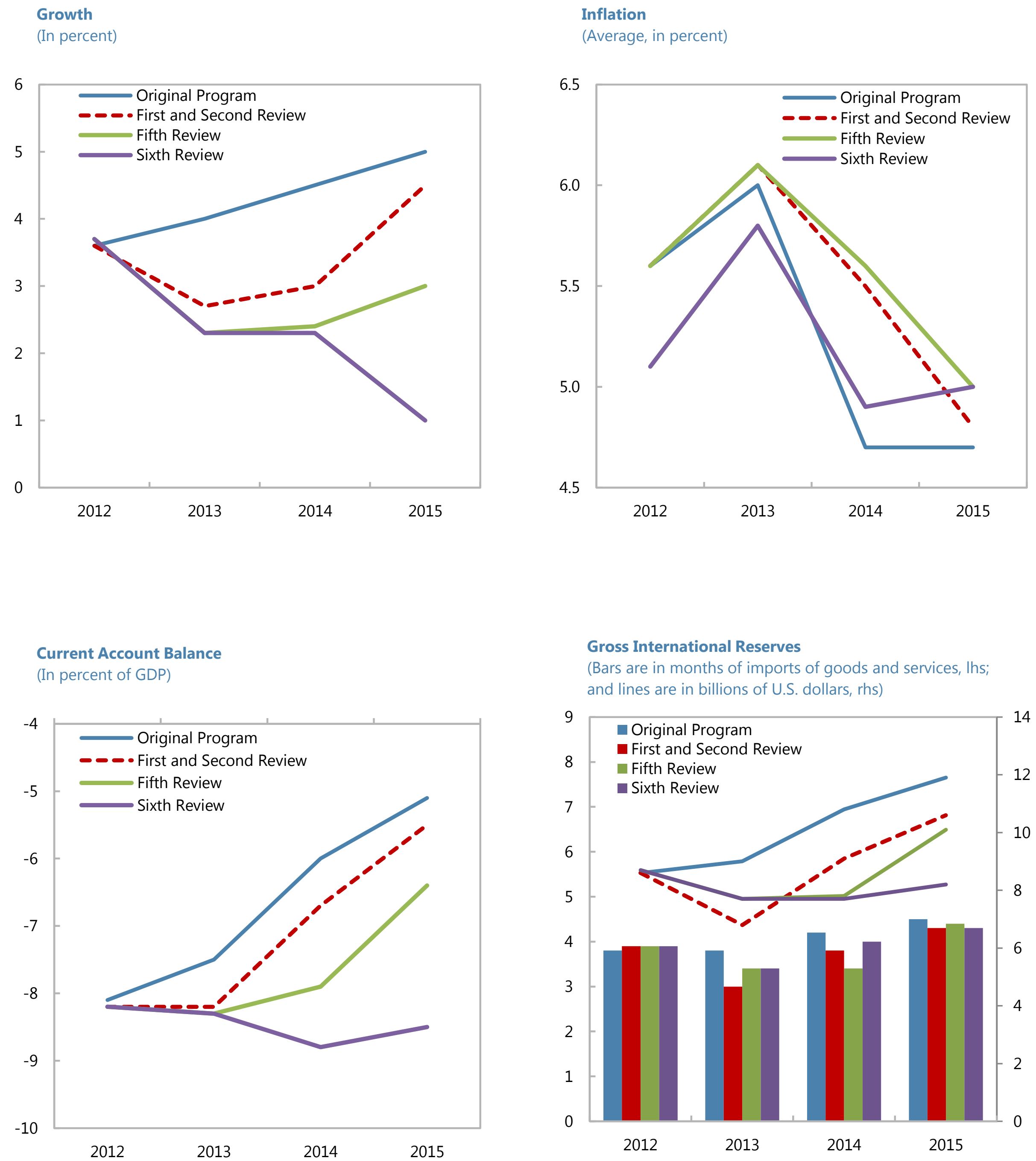
- **Business climate reforms**. Parliamentary delays postponed the adoption of key legislation critical to support growth, with the competition, PPP, and bankruptcy laws approved in September 2015, December 2015, and April 2016, respectively. The investment code (revised several times during the transition) is still pending parliamentary approval. Progress was made in simplifying administrative procedures in pilot ministries, which will need to be generalized.

- **Social protection mechanisms have strengthened.** The existing cash transfer system for the poor (PNAFN) has been expanded to cover 235,000 families (twice the level of 2010 and close to 60 percent of the estimated poor) and provide more cash (average transfer has tripled to about US$80 per month). A social electricity tariff was introduced to protect poorer households that

consume less than 100 kwh. These achievements will need to be consolidated in the establishment of a comprehensive better targeted social safety net.

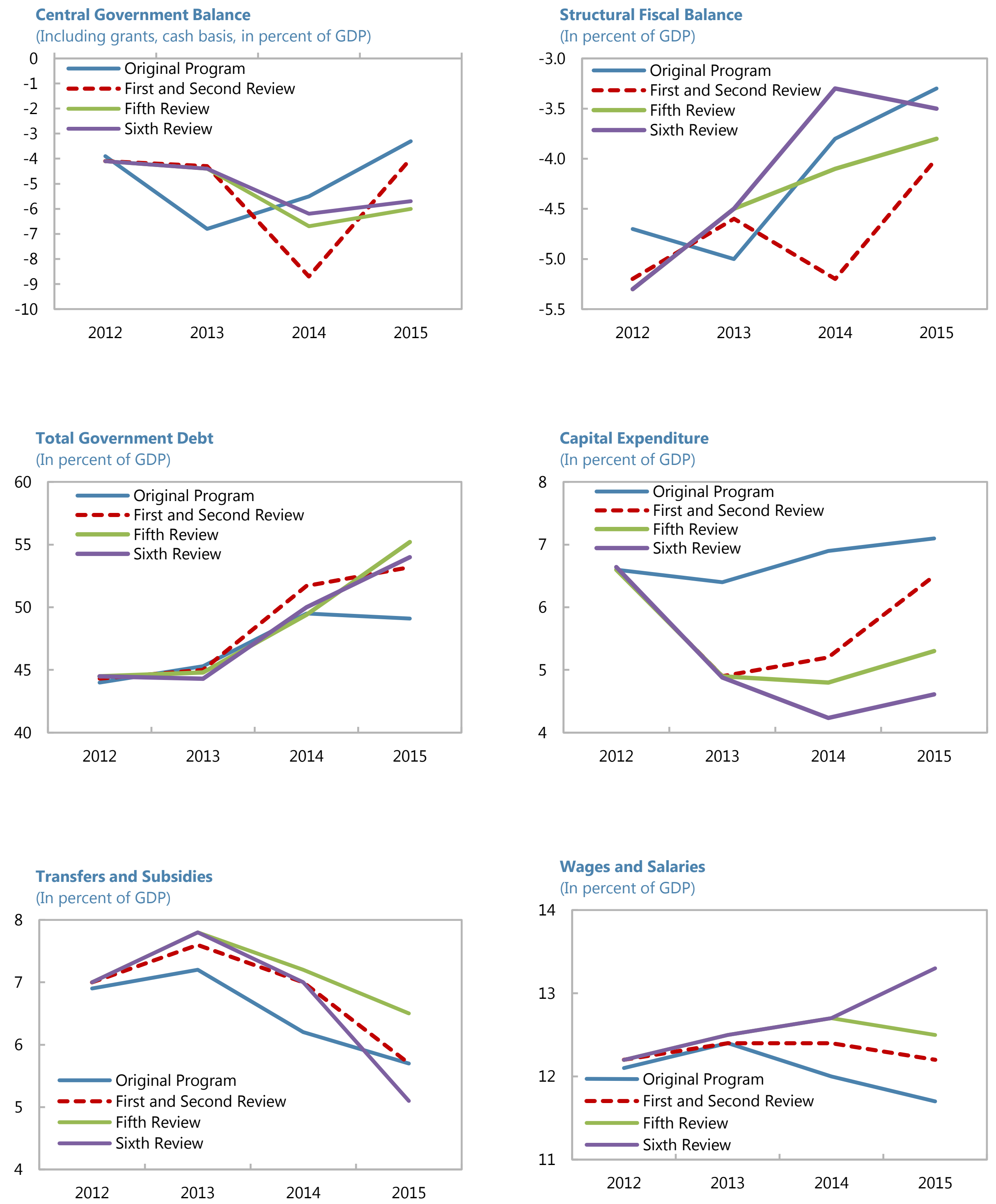
- **Labor market and pension reform.** Discussions with relevant stakeholders were initiated during the program period. Conditionality in this important area were left out from the program design as both the authorities and staff considered that reforms in this area could only be designed by a post-transition government.

Annex Figure 1. Tunisia: Key Indicators under the SBA Program, 2012–15



Sources: Tunisian authorities; and IMF staff estimates.

Annex Figure 2. Tunisia: Fiscal Performance under the SBA Program, 2012–15



Sources: Tunisian authorities; and IMF staff estimates.

Annex Table 1. Tunisia: Structural Benchmarks under the SBA Program

	Structural Benchmark	Proposed 1/	Completed 1/
	I. Financial sector		
1	Adoption by the Council of Ministers of the strategic vision of the government's future role in banks, on the basis of the preliminary results from the audit of public banks	R	1 & 2
2	Approval of the new reporting system architecture covering bank-related accounting, financial, and institutional functions	R	1 & 2
3	General on-site inspection of one major bank and inspection of the credit risks of four other banks	R	1 & 2
4	Presentation to the board of the CBT of a study concerning the impact on banks of liquidity ratio changes toward international standards	R	3
5	Submission to the Management of the Central Bank of Tunisia of a banking resolution framework in line with international practices	1 & 2	4
6	Submission to the Central Bank Board of a draft Central Banking law in line with international practices	1 & 2	4
7	Development and implementation of the new reporting system and bank classification system	1 & 2	Not met
8	Completion of the financial audit of the Banque Nationale Agricole (BNA)	3	5
9	Adoption by the Government of restructuring plans for the BH and STB	3	4
10	Creation of Asset Management Company (AMC) through the publication in the Official Journal of the Law on the AMC	4	Not met
11	Adoption by the Government of the BNA restructuring plan	4	Not met
12	Double the number of DGSB supervisors hired in 2013 and revise the CBT hiring criteria to facilitate the hiring of qualified personnel	4	Not met
13	All banks, including public banks, to comply with minimum solvency ratio required by the existing regulations (10 percent)	4	Not met
14	Designation of fit and proper Board members of the three public banks, with private sector experience	5	6
15	Adoption of recapitalization plans in line with sound international practices by the general assembly of the three public banks, following the criteria outlined in Annex 1 to the MEFP and based on the results of the audits	5	Not met
16	Approval by the Board of Directors of performance contracts in line with norms included in the bank restructuring plans for the STB, BH and BNA and subordinated to the approval of the respective recapitalization plans	5	Not met
17	Adoption by Parliament of the banking law (that includes a banking resolution framework) in line with sound international practices	5	Not met
18	Publication, on the Official Gazette, of the law governing the functioning of the AMC in line with sound international practices, as well as Government adoption of the related implementation decrees	5	Not met
	II. Fiscal policy		
1	Approval by the Council of Ministers of the corporate tax reform announcing the convergence of the tax rates of onshore and offshore sectors for 2014 and identification of countervailing measures to ensure a neutral impact on revenues	R	1 & 2
2	Adoption of a Ministry of Industry decree approving a new automatic fuel pricing formula	R	1 & 2
3	Submission to the Council of Ministers of a new targeted household support program to accompany the reform of generalized energy subsidies	R	4
4	Merge at the level of the large taxpayer unit the management, tax collection, and control of large enterprises	R	1 & 2
5	Finalize the audit of the electricity company (STEG) and of the petroleum refinery company (STIR)	R	3
6	Implementation by the Ministry of Finance of a plan to modernize tax administration	1 & 2	4

Annex Table 1. Tunisia: Structural Benchmarks under the SBA Program (concluded)

	Structural Benchmark	Proposed 1/	Completed 1/
	II. Fiscal policy		
7	Unification of government accounts into a Single Treasury Account (formulation to be revised for project loans)	1 & 2	4
8	Prepare a consolidated balance of 20 main public enterprises (2010-2012)	1 & 2	4
9	Government approval of a new tax code	1 & 2	5
10	Following national consultations on taxation, adoption of a tax reform plan covering direct and indirect taxes by the Council of Ministers	4	Not met
11	Parliamentary Approval of the 2015 budget	5	6
12	Creation of a new category of public accountants called "tax collectors"	5	Not met
13	Adoption by the Government of a strategy for a better monitoring of operations and financial performance of public enterprises	5	Not met
14	Signature of performance contracts for the 5 largest state-owned companies	5	Not met
15	Adoption by the government of a calendar for the total convergence of the tax rates of onshore and offshore sectors	5	Not met
16	Adoption of a tax reform plan covering direct and indirect taxes by the Council of Ministers	6	Not met
	III. Monetary and exchange rate policy		
1	Publication of a circulaire by the CBT that announces a haircut on all loans used as collateral for refinancing operations at the central bank	R	1 & 2
2	Ensure that the proportion of the refinancing volume at the CBT backed by government securities is at least 10 percent for each bank	R	1 & 2
3	Implementation of an electronic bank interlinking platform and launch of the Market Makers Agreement	R	3
4	Ensure that the proportion of the refinancing volume at the CBT that is backed by government securities is at least 20 percent for each bank	R	1 & 2
5	Presentation to the Central Bank board of the impact study for removing the upper limit for excessive rates for enterprises and to modify it for consumers	1 & 2	3
6	Implement an increase of the haircut for loans used as collateral for refinancing operations to at least 25 percent	1 & 2	4
7	Establishment of the lender of last resort facility	1 & 2	Not met
8	Ensure that the proportion of the refinancing volume at the CBT backed by government securities is at least 40 percent for each bank	1 & 2	4
9	Implementation of a weekly foreign exchange auction mechanism	1 & 2	Not met
	IV. Structural reforms/private-sector development		
1	Adoption of the Investment Code by the government (tax measures will be referred to in the tax code)	R	1 & 2
2	Decree for implementing the new investment code in line with the objective of protecting market access, reducing restrictions on investments, and rationalizing of incentives	1 & 2	Not met
3	Revision of the new investment code in line with the objective to protect market access, reduce investment restrictions, and rationalize exemptions	5	Not met

1/ corresponds to the review in which the structural benchmark was proposed or met. R: program request; 1 & 2: first and second review; 3: 3rd review; ...etc

Annex II. Tunisia: Public Debt Sustainability Analysis

Tunisia's debt level remains sustainable and lower than that of regional peers. Central government debt is expected to peak at 55 percent of GDP in 2016 before declining over the medium term under the fiscal path agreed under the program (the "baseline" scenario). Having peaked in 2015, gross financing needs are expected to average 7.2 percent of GDP through 2020, relying on long maturities and favorable conditions by official external creditors. Stress scenarios and the heat map confirm the sustainability of debt dynamics, but point to vulnerabilities related to the large proportion of foreign debt, including exchange rate risks, and permanently lower growth.[1]

Baseline and realism of projections[2]

- **Growth and prices.** Growth prospects have been revised down following weaker economic activity and the recent terrorist attacks, which had a severe impact on the tourism sector in particular and investors' confidence in general. Growth over the medium term is expected to recover to potential by 2019. Forecast errors are broadly in line with other countries, with past projections of growth tilted to the optimistic side, mainly driven by the large swing in 2011 GDP following the revolution. The track record of inflation forecasts remains in line with other countries, although inflation since 2011 has generally been higher than initially projected. Low commodity prices and a prudent monetary policy are expected to contain inflation below 4 percent over the medium term.

- **Debt level and fiscal adjustment.** The loosening of the fiscal stance to stimulate the economy after the 2015 terror attacks and weaker-than-originally-expected growth dynamics have contributed to increasing the debt-to-GDP ratio to an estimated 53.2 percent at end-2015 (from 45.5 percent in 2012). The programmed fiscal consolidation and the growth recovery beyond 2016 would help reduce the debt-to-GDP ratio to 50 percent by end-2020 (about 5.5 percentage points of GDP higher than the 2005–13 average). The three-year adjustment of the cyclically-adjusted primary balance (CAPB) is higher than three percent of GDP and in the top quartile, but due to the large adjustment from 2013–16. More importantly, the envisaged fiscal consolidation under the program will be measured by the structural fiscal balance—i.e., excluding economic cycles and one-off costs linked to bank restructuring and civil service reform—and is estimated at 2.2 percent of GDP, which places the expected path in the second quartile. The forward-looking three-year average cyclically-adjusted primary deficit is in the first quartile with a forecast of 4.4 percent of GDP in 2016, halving by 2021.

- **Sovereign yields.** Tunisia's effective interest rate is projected to decline to its lowest level in the next two years thanks to the large proportion of concessional or guaranteed debt, and the redemption of the 2017 Eurobond. However, projected market issuance in the outer years will start lifting effective rates in the medium term. Domestic yields might also increase

[1] See definition of central government in the Technical Memorandum of Understanding (¶17). State guarantees (12 percent of GDP) are excluded from the analysis on account of low probability of being called and the lag in data provision to the central government. Also see Box 5.

[2] The DSA framework is described at http://www.imf.org/external/np/pp/eng/2013/050913.pdf

in the next three years from the current moderate levels, before stabilizing in the medium term thanks to declining risk premium as reforms bear fruit.

- **Maturity and rollover.** Tunisia enjoys relatively long maturities in both foreign and domestic debt (with an average above three years for domestic debt). Gross public financing needs peaked in 2015 (9.4 percent of GDP) and will remain moderate. However, the high share of foreign currency-denominated public debt leaves debt vulnerable to exchange rate fluctuations.

Stress test and heat map

Public debt dynamics remain sustainable under all adverse shocks, but could deteriorate significantly relative to the baseline. Tunisia is most vulnerable to real exchange rate and real GDP growth shocks, reinforcing the call to implement structural reforms that support competitiveness and economic activity. The heat map highlights the need to monitor closely the composition of debt and contingent liabilities.

- Under most adverse scenarios, the public debt-to-GDP ratio would initially worsen to a maximum of between 55 and 65 percent of GDP and then decline to between 48 percent and 58 percent in 2021. Scenarios include: a failure to implement medium-term fiscal consolidation; shocks to growth or to the real interest rate; and the realization of a one-off 10 percent of GDP fiscal contingent liability, which could come in the form of callable state guarantees, public bank bailouts, or ailing SOEs.[3] However, the debt trajectory would remain sustainable even if 90 percent of these contingencies were called, as evidenced by the shock, although debt levels would increase.

- The most severe shocks point to higher but sustainable debt in the medium term. A one-time 30 percent real depreciation would increase the public debt-to-GDP ratio to about 65 percent before it declines to below 60 percent by 2021, because about 66 percent of public debt is denominated in foreign currency.

- A combined shock (to real growth and the primary balance) would raise public debt to 78 percent of GDP by 2018 before declining to 72 percent by the end of the outlook while a contingent liability shock will raise the public debt to 69 percent in 2018 before declining to 63 percent in 2021. The results of the asymmetric fan chart (see below), also reinforces the need for fiscal adjustment to prevent debt approaching an unsustainable level.

Tunisia's relatively high reliance on foreign debt is a weakness, making it more vulnerable to market perceptions and to volatile private sector flows. Contingent liabilities could also increase financing needs above the high early warning threshold. On the upside, public debt is generally of long maturity and, provided fiscal consolidation continues as envisaged, debt dynamics will remain favorable.

[3] The one-off 10 percent of GDP shock to contingent liabilities reflects an additional three percent of GDP in bank recapitalization costs and the realization of about 7 percent of GDP of government's contingent liabilities from public enterprises (these represent about 70 percent of government's existing contingent liabilities).

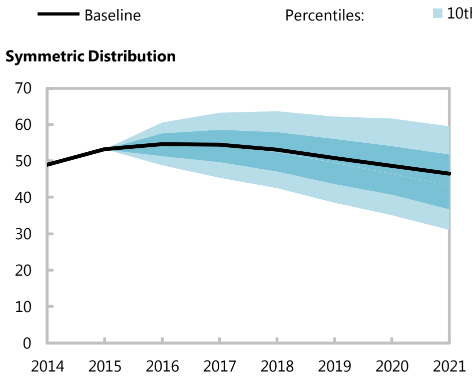
Tunisia Public DSA Risk Assessment

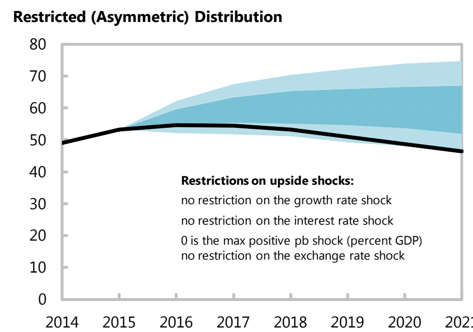
Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

Evolution of Predictive Densities of Gross Nominal Public Debt

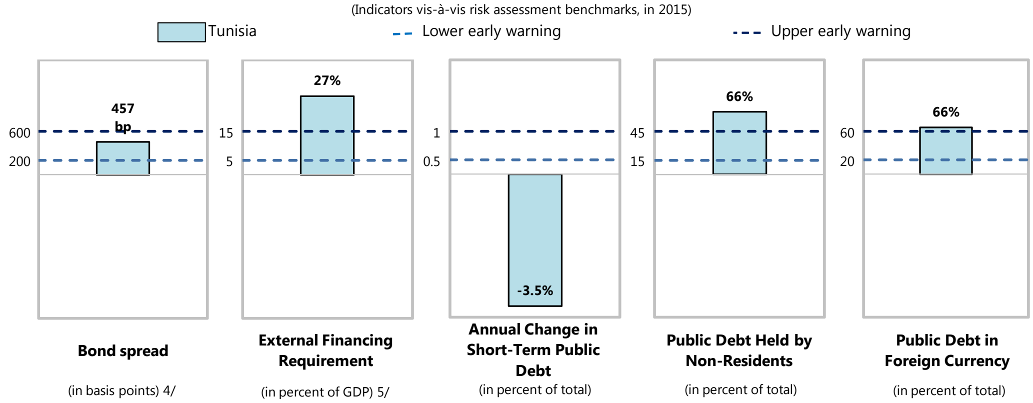
(in percent of GDP)





Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2015)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

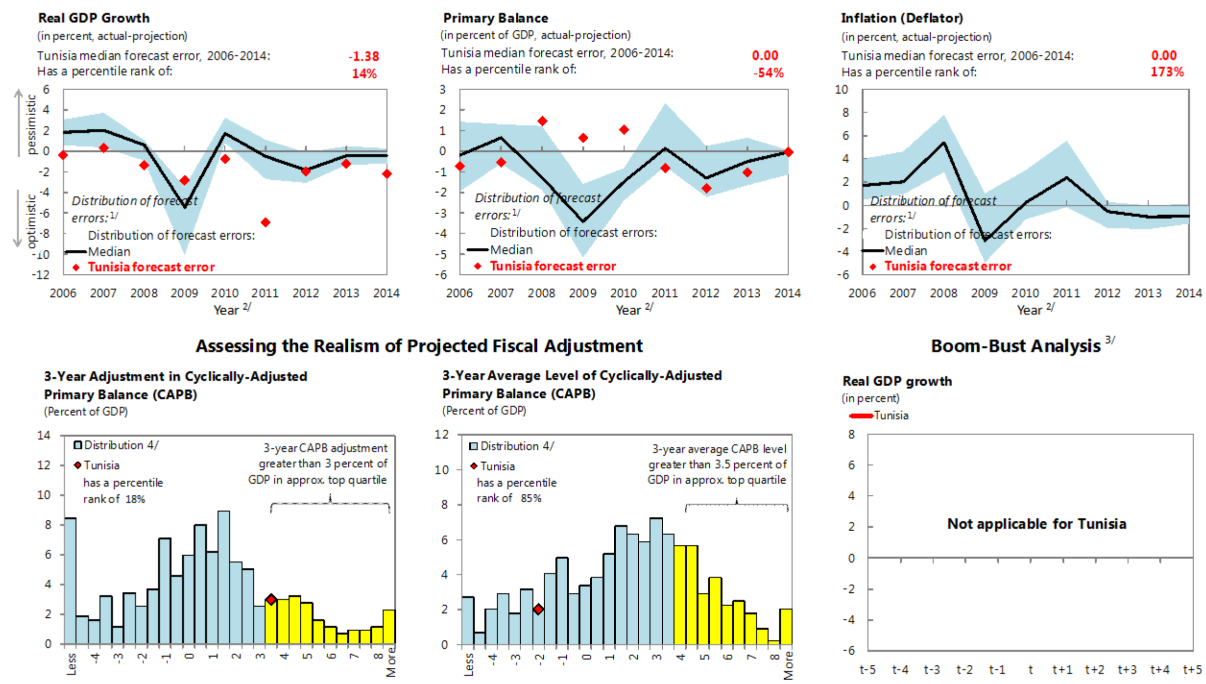
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over U.S. bonds, an average over the last 3 months, 14-Jan-16 through 13-Apr-16.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Tunisia Public DSA – Realism of Baseline Assumptions

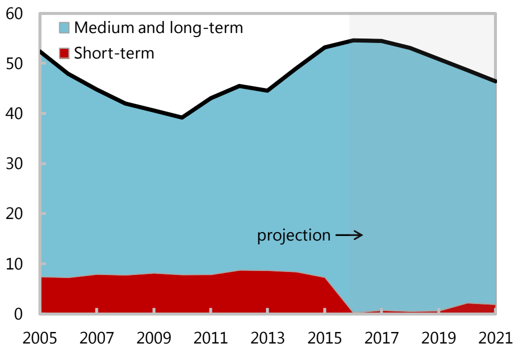


Source : IMF Staff.
1/ Plotted distribution includes program countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Not applicable for Tunisia, as it meets neither the positive output gap criterion nor the private credit growth criterion.
4/ Data cover annual observations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

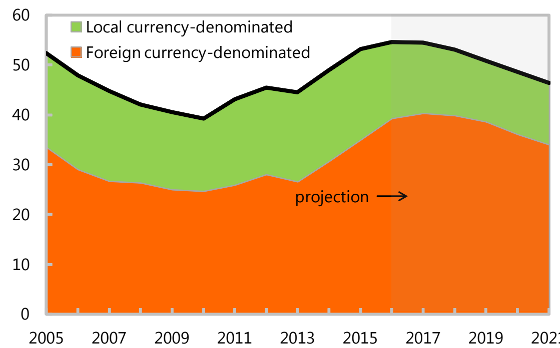
Tunisia Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



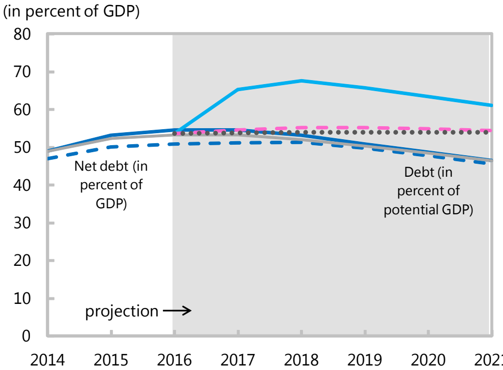
By Currency
(in percent of GDP)



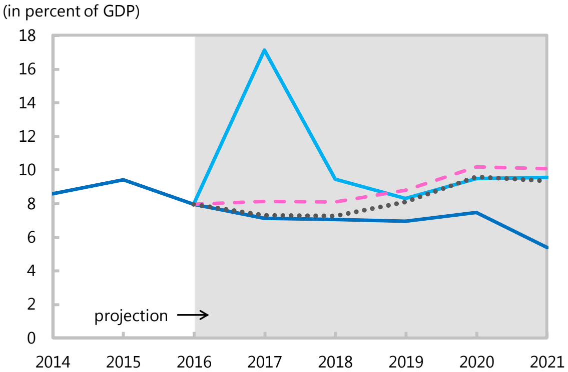
Alternative Scenarios

Baseline
Historical
Constant Primary Balance
Contingent Liability Shock

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

Baseline Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	2.0	3.0	3.7	4.3	4.7	4.5
Inflation	5.1	3.3	3.0	3.3	3.2	3.2
Primary Balance	-2.3	-1.5	-1.6	-0.6	-0.5	-0.4
Effective interest rate	4.1	2.5	0.8	1.2	1.8	2.3
Constant Primary Balance Scenario						
Real GDP growth	2.0	3.0	3.7	4.3	4.7	4.5
Inflation	5.1	3.3	3.0	3.3	3.2	3.2
Primary Balance	-2.3	-2.3	-2.3	-2.3	-2.3	-2.3
Effective interest rate	4.1	2.4	0.8	1.3	2.0	2.6

Historical Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	2.0	3.0	3.0	3.0	3.0	3.0
Inflation	5.1	3.3	3.0	3.3	3.2	3.2
Primary Balance	-2.3	-1.5	-1.5	-1.5	-1.5	-1.5
Effective interest rate	4.1	2.4	1.0	1.6	2.5	3.3
Contingent Liability Shock						
Real GDP growth	2.0	0.6	1.3	4.3	4.7	4.5
Inflation	5.1	2.7	2.4	3.3	3.2	3.2
Primary Balance	-2.3	-11.0	-1.6	-0.6	-0.5	-0.4
Effective interest rate	4.1	2.7	1.8	2.1	2.6	3.0

Source: IMF staff.

Tunisia Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

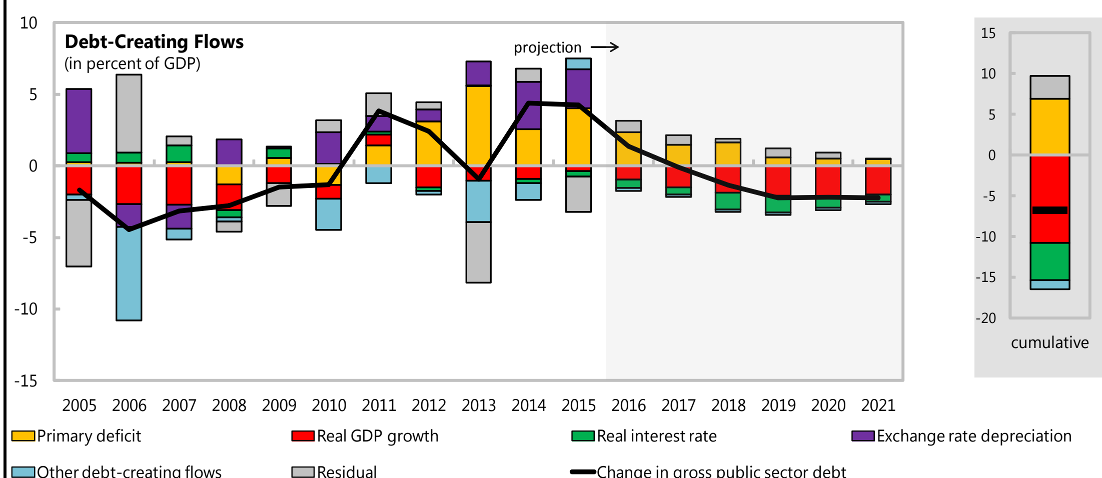
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators [1]

	Actual			Projections						As of April 13, 2016		
	2005-2013 [2]	2014	2015	2016	2017	2018	2019	2020	2021	Sovereign Spreads		
Nominal gross public debt	44.4	49.0	53.2	54.6	54.5	53.1	50.9	48.7	46.4	EMBIG (bp) 3/		434
Public gross financing needs	6.7	8.6	9.4	8.0	7.1	7.0	6.9	7.5	5.4	5Y CDS (bp)		467
Real GDP growth (in percent)	3.4	2.3	0.8	2.0	3.0	3.7	4.3	4.7	4.5	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	4.1	5.2	4.9	5.1	3.3	3.0	3.3	3.2	3.2	Moody's	Ba3	Ba3
Nominal GDP growth (in percent)	7.6	7.5	5.8	7.2	6.4	6.8	7.8	8.0	7.9	S&Ps	...	...
Effective interest rate (in percent) [4]	4.9	4.5	4.1	4.1	2.5	0.8	1.2	1.8	2.3	Fitch	BB-	BB

Contribution to Changes in Public Debt

	Actual			Projections							
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021	cumulative	debt-stabilizing
Change in gross public sector debt	-1.1	4.4	4.3	1.4	-0.1	-1.4	-2.2	-2.2	-2.2	-6.8	primary
Identified debt-creating flows	-0.8	3.5	6.7	0.6	-0.7	-1.6	-2.9	-2.6	-2.3	-9.5	balance [9]
Primary deficit	1.0	2.5	4.0	2.3	1.5	1.6	0.6	0.5	0.4	6.9	-2.7
Primary (noninterest) revenue and grants	23.6	25.8	23.3	24.1	24.4	24.6	25.0	24.9	24.9	147.9	
Primary (noninterest) expenditure	24.6	28.4	27.3	26.4	25.9	26.2	25.6	25.4	25.3	154.8	
Automatic debt dynamics [5]	-0.2	2.1	2.0	-1.6	-2.0	-3.1	-3.3	-2.9	-2.5	-15.4	
Interest rate/growth differential [6]	-1.2	-1.2	-0.8	-1.6	-2.0	-3.1	-3.3	-2.9	-2.5	-15.4	
Of which: real interest rate	0.3	-0.3	-0.4	-0.6	-0.5	-1.2	-1.1	-0.7	-0.5	-4.6	
Of which: real GDP growth	-1.5	-0.9	-0.4	-1.0	-1.5	-1.9	-2.1	-2.2	-2.0	-10.8	
Exchange rate depreciation [7]	1.0	3.3	2.7	...	...	...	...	...	...	...	
Other identified debt-creating flows	-1.6	-1.1	0.7	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-1.1	
CG: Privatization Proceeds (negative)	-1.1	-0.1	-0.1	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-1.1	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8]	-0.2	0.9	-2.5	0.8	0.7	0.2	0.6	0.4	0.0	2.8	



Source: IMF staff.

1/ Public sector is defined as central government.

2/ Based on available data.

3/ Long-term bond spread over U.S. bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi (1+g)$ and the real growth contribution as $-g$.

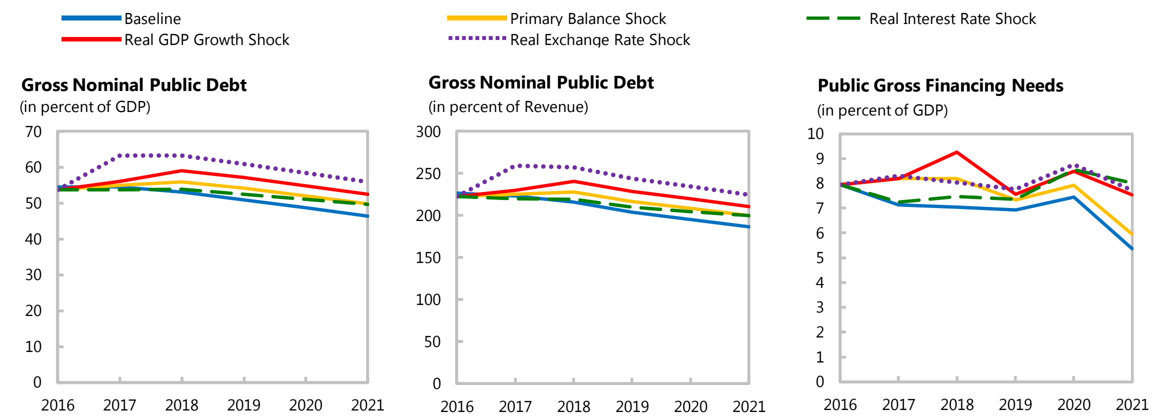
7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

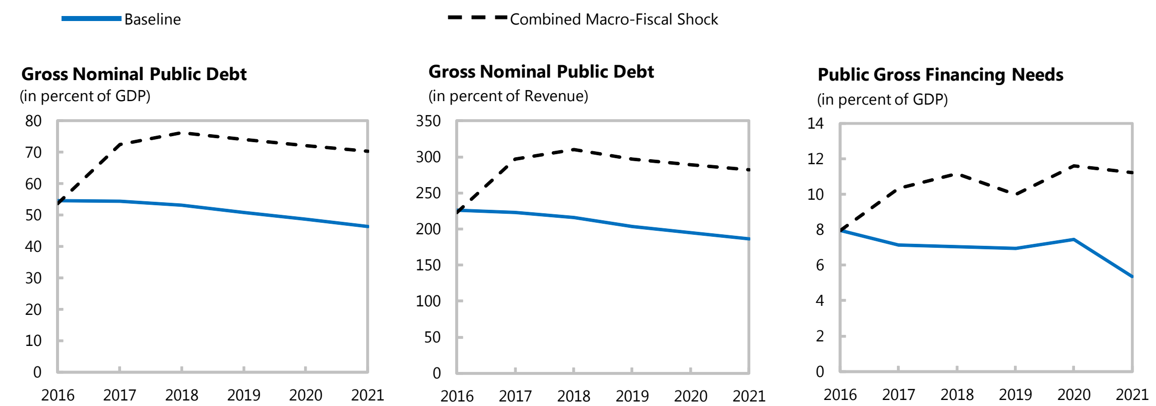
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Tunisia Public DSA - Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2016	2017	2018	2019	2020	2021
Real GDP growth	2.0	3.0	3.7	4.3	4.7	4.5
Inflation	5.1	3.3	3.0	3.3	3.2	3.2
Primary balance	-2.3	-2.6	-2.8	-0.6	-0.5	-0.4
Effective interest rate	4.1	2.4	0.9	1.4	2.0	2.5
Real Interest Rate Shock						
Real GDP growth	2.0	3.0	3.7	4.3	4.7	4.5
Inflation	5.1	3.3	3.0	3.3	3.2	3.2
Primary balance	-2.3	-1.5	-1.6	-0.6	-0.5	-0.4
Effective interest rate	4.1	2.4	1.2	2.1	3.3	4.3
Combined Shock						
Real GDP growth	2.0	0.6	1.3	4.3	4.7	4.5
Inflation	5.1	2.7	2.4	3.3	3.2	3.2
Primary balance	-2.3	-2.6	-3.2	-0.6	-0.5	-0.4
Effective interest rate	4.1	3.0	1.4	2.3	3.4	4.3

Real GDP Growth Shock	2016	2017	2018	2019	2020	2021
Real GDP growth	2.0	0.6	1.3	4.3	4.7	4.5
Inflation	5.1	2.7	2.4	3.3	3.2	3.2
Primary balance	-2.3	-2.2	-3.2	-0.6	-0.5	-0.4
Effective interest rate	4.1	2.4	0.8	1.4	2.0	2.4
Real Exchange Rate Shock						
Real GDP growth	2.0	3.0	3.7	4.3	4.7	4.5
Inflation	5.1	13.3	3.0	3.3	3.2	3.2
Primary balance	-2.3	-1.5	-1.6	-0.6	-0.5	-0.4
Effective interest rate	4.1	3.0	0.8	1.2	1.8	2.3

Source: IMF staff.

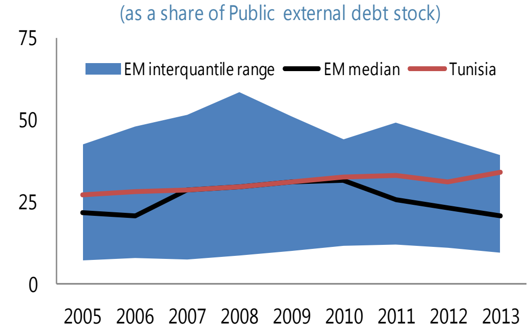
Annex III. Tunisia: External Debt Sustainability Analysis

Tunisia's external debt has been rising since 2011. External debt declined sharply from over 61 percent of GDP in 2002 to 49 percent of GDP at end-2010. Four years after the 2011 revolution, however, external debt-to-GDP ratios climbed from 51 percent in 2011 to around 64 percent by end 2015, reflecting higher fiscal and current account deficits following a series of external shocks and rising social pressures. Most of the new debt commitments are either with official creditors or backed by a third party guarantee, with the exception of a US$1 billion Eurobond issued in January 2015.

Under baseline projections,[1] external debt would increase to 69 percent of GDP in 2016, peak at 73.3 percent in 2018, before declining gradually over the medium term. External debt-to-GDP is expected to increase from around 64 percent in 2015 to 69 percent in 2016, driven by US-guaranteed market access and continued official financing. The external debt-to-GDP ratio is expected to gradually increase reaching a peak of 73.3 in 2018, driven by multilateral financing—including the Fund's EFF—and international market access. It is then expected to gradually decline to around 70 percent over the medium term by end-2021, following favorable current account dynamics (Annex III Table 1).

The external debt-to-GDP ratio remains resilient to most types of adverse external shocks except for a large exchange rate depreciation shock. Tunisia's relatively low level of external debt as well as its profile (low average interest rate and relatively long maturity and large proportion of concessional debt, see text chart) makes it robust to most shocks, with the exception of a large real exchange rate depreciation shock. Specifically, external DSA results suggest that the external debt-to-GDP ratio would remain below 80 percent of GDP throughout the projection period under all but one shock scenario. For example, a combined negative shock to real interest rate, growth and the current account would raise the debt ratio to around 76 percent of GDP compared to 70 percent of GDP under the baseline by end-2021. However, a sharp real depreciation (one-time 30 percent) of the exchange rate in 2017 relative to the baseline would raise the external debt ratio to around 104 percent of GDP in 2018 before declining to about 99 percent by end-2021 (Annex III. Figure 1).

Public external concessional debt stock
(as a share of Public external debt stock)



Sources: Calculations based on WB International Debt Statistics.

[1] For more details, see IMF (2008) "Staff Guidance Note on Debt Sustainability Analysis for Market Access Countries," IMF Board Paper SM/08/221.

Annex III. Table 1. Tunisia: External Debt Sustainability Framework, 2011–2021

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2011	2012	2013	2014	2015			2016	2017	2018	2019	2020	2021	Debt-stabilizing non-interest current account 6/
Baseline: External debt	51.3	52.9	57.0	61.4	63.5			**69.0**	**71.4**	**73.3**	**72.5**	**71.2**	**69.6**	**-5.6**
Change in external debt	2.5	1.6	4.1	4.4	2.1			5.5	2.5	1.8	-0.7	-1.3	-1.7	
Identified external debt-creating flows (4+8+9)	4.7	5.8	4.5	5.2	12.2			4.3	2.8	1.5	0.4	-0.3	-1.0	
Current account deficit, excluding interest payments	6.0	6.9	7.2	7.9	7.6			6.3	5.7	5.0	4.6	4.2	3.6	
Deficit in balance of goods and services	2.7	9.2	9.3	11.0	10.7			9.6	9.4	8.7	8.3	8.2	7.7	
Exports	53.9	49.4	47.7	45.6	40.0			38.6	40.2	41.1	40.9	40.2	39.4	
Imports	56.6	58.6	57.1	56.6	50.7			48.2	49.5	49.9	49.2	48.3	47.1	
Net non-debt creating capital inflows (negative)	-0.8	-3.4	-2.5	-2.3	-2.5			-2.1	-2.2	-2.2	-2.2	-2.2	-2.4	
Automatic debt dynamics 1/	-0.4	2.4	-0.2	-0.4	7.1			0.2	-0.7	-1.4	-2.0	-2.3	-2.3	
Contribution from nominal interest rate	1.5	1.5	1.2	1.2	1.4			1.4	1.3	1.2	1.0	0.9	0.7	
Contribution from real GDP growth	0.9	-2.0	-1.3	-1.2	-0.5			-1.3	-2.1	-2.6	-3.0	-3.2	-3.0	
Contribution from price and exchange rate changes 2/	-2.8	2.9	-0.1	-0.4	6.2			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets 3/	-2.2	-4.2	-0.4	-0.8	-10.1			1.1	-0.4	0.3	-1.1	-1.1	-0.7	
External debt-to-exports ratio (in percent)	95.1	107.1	119.4	134.8	158.8			178.8	177.9	178.0	177.5	177.3	176.7	
Gross external financing need (in billions of US dollars) 4/	10.4	10.9	11.6	12.2	11.9			11.2	11.5	10.8	11.0	11.0	11.1	
in percent of GDP	22.8	24.2	25.1	25.5	27.4	10-Year	10-Year	25.5	25.9	24.1	23.2	21.8	20.8	
A. Scenario with key variables at their historical averages 5/								**69.0**	**68.5**	**68.5**	**69.6**	**70.8**	**72.6**	**-2.9**
Key Macroeconomic Assumptions Underlying Baseline						Historical Average	Standard Deviation							
Real GDP growth (in percent)	-1.9	3.9	2.4	2.3	0.8	3.0	2.4	2.0	3.0	3.7	4.3	4.7	4.5	
GDP deflator in US dollars (change in percent)	6.0	-5.4	0.2	0.7	-9.2	0.3	6.1	-0.9	-2.1	-2.4	1.2	1.3	1.5	
Nominal external interest rate (in percent)	3.1	2.9	2.4	2.2	2.1	3.1	0.7	2.2	1.9	1.7	1.5	1.3	1.1	
Growth of exports (US dollar terms, in percent)	11.0	-9.9	-0.8	-1.8	-19.7	3.0	16.6	-2.5	4.9	3.8	4.9	4.3	3.9	
Growth of imports (US dollar terms, in percent)	6.4	1.9	0.0	2.0	-17.9	5.2	16.0	-3.9	3.5	2.0	4.2	4.2	3.3	
Current account balance, excluding interest payments	-6.0	-6.9	-7.2	-7.9	-7.6	-4.2	3.2	-6.3	-5.7	-5.0	-4.6	-4.2	-3.6	
Net non-debt creating capital inflows	0.8	3.4	2.5	2.3	2.5	2.8	1.1	2.1	2.2	2.2	2.2	2.2	2.4	
B. Bound Tests														
B1. Nominal interest rate is at historical average plus one standard deviation								**69.0**	**71.7**	**73.7**	**73.2**	**72.1**	**70.6**	**-5.4**
B2. Real GDP growth is at historical average minus one standard deviations								**69.0**	**72.6**	**75.6**	**75.9**	**75.5**	**74.7**	**-4.8**
B3. Non-interest current account is at historical average minus one standard deviations								**69.0**	**73.0**	**76.5**	**77.2**	**77.3**	**76.9**	**-6.0**
B4. Combination of B1-B3 using 1/2 standard deviation shocks								**69.0**	**72.7**	**75.9**	**76.3**	**76.1**	**75.5**	**-5.4**
B5. One time 30 percent real depreciation in 2016								**69.0**	**101.4**	**104.0**	**103.0**	**101.1**	**98.8**	**-8.0**

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

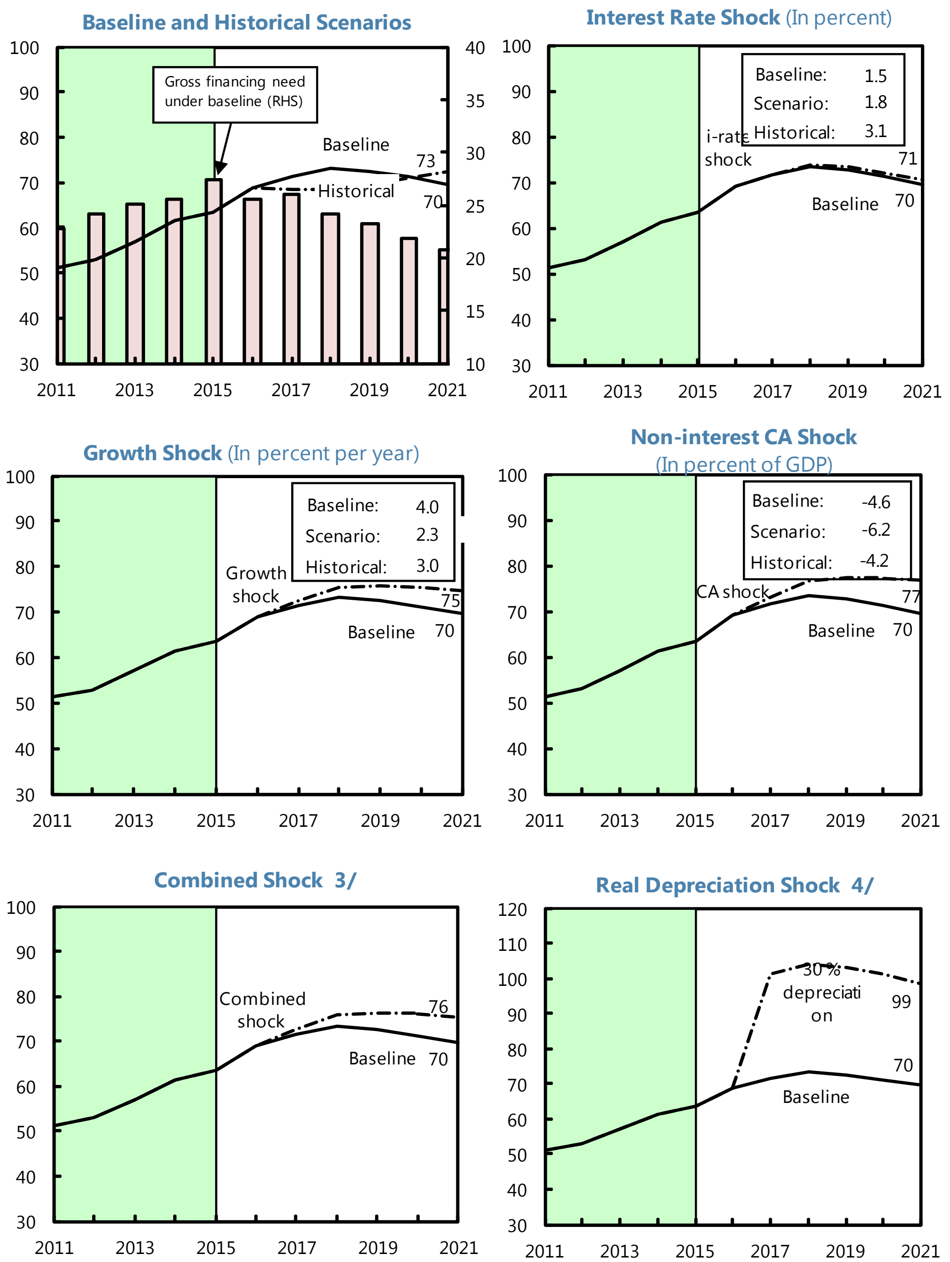
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Annex III. Figure 1. Tunisia: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: IMF, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks (except for growth which is a 3/4th standard deviation). Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2017.

Appendix I. Letter of Intent

Tunis, May 2, 2016

Madam Christine Lagarde
Managing Director
International Monetary Fund
700 19th Street, NW
Washington, DC 20431
USA

Madam Managing Director:

1. Since January 14, 2011, Tunisia's path has been remarkable in many ways. The election of a constituent assembly in October 2011, whose work culminated in the approval of a new constitution in January 2014, opened the way towards a new democratic era. The legislative and presidential elections held in October 2014 and the naming of a government supported by a large parliamentary majority have been milestones marking this political transition. Finally, the fact that the 2015 Nobel Peace Prize was awarded to the Tunisian National Dialogue Quartet highlighted and recognized the efforts made by all parties in building a pluralistic democracy in Tunisia. This path is all the more remarkable in that it has been accompanied by several exogenous shocks, in particular continued weak growth in the euro zone (our main trading partner), the deteriorating security situation in Libya, worsening social tensions, and the repercussions of the recent cowardly and barbaric terrorist attacks.

2. The IMF stand-by arrangement approved in June 2013, which has just ended, provided major financial support for carrying out economic reforms to maintain macroeconomic stability, in spite of a difficult regional and global environment, and so that the necessary policies could be put in place as a foundation for further growth. Thus, work has continued in pursuing fiscal consolidation and keeping the inflation rate under control, foreign-exchange reserves have been stabilized, and risks to financial stability have been lessened in the wake of the restructuring of public banks. However, several sources of vulnerability remain: unemployment remains stubbornly high, external imbalances persist, the wage bill weighs heavily on government expenditure, banking sector vulnerability continues, and the business climate is not sufficiently attractive to bring in the investment flows needed to create more jobs.

3. Meeting the challenges that Tunisia faces will require a transformation of the current development model, in order to reduce the vulnerabilities in our economy and meet the Tunisian people's aspirations to achieve stronger, more inclusive growth. Accordingly, the government has developed an economic vision, coupled with a national program of major reforms to enable Tunisia's growth potential to flourish in the next five years. This vision will be spelled out in detail in

the 2016–20 five-year plan which will be submitted to the Assembly of the People's Representatives (ARP) in June 2016; it will serve as the foundation for the economic and reform program that we are committed to carrying out, and we will present it at an international conference to be held in the coming months.

4. We are requesting support from the International Monetary Fund through an Extended Fund Facility for a four-year program in the amount of SDR 2.045625 billion (375 percent of quota, or about US$2.8 billion). The main objective of the new arrangement is to restore Tunisia's economic growth in order to create more jobs and reduce unemployment. The new arrangement will also help Tunisia pursue prudent macroeconomic policies, further reduce the economy's vulnerability to exogenous shocks, and foster more inclusive development in keeping with the aspirations of the Tunisian people. We also hope to build buffers to respond in the event of exogenous shocks, especially in view of the fragile regional security environment. The program will demonstrate our determination to pursue adequate policies and will serve as a catalyst to attract investment and financial support from other development partners.

5. The memorandum on economic and financial policies (MEFP), hereto annexed, sets out the principal elements of the program of reforms and policies that the government and the central bank intend to carry out during the period 2016 to 2019. It also describes macroeconomic objectives, structural reforms, and indicators that pertain to the first year of the program. We are determined to devote our fullest efforts to implementing our program, while remaining aware of the difficulties associated with the national, regional, and international contexts.

6. The progress we make in carrying out our program will be monitored through semi-annual reviews based on prior actions, quantitative criteria, and structural benchmarks as described in the accompanying MEFP and the technical memorandum of understanding (TMU). There will be eight such reviews to examine the progress made in carrying out the program and to agree on any corrective measures necessary to achieve program objectives. The first two reviews of Tunisia's performance under the Extended Fund Facility must be completed no later than December 31, 2016, and June 30, 2017, respectively.

7. We are convinced that the policies described in the accompanying MEFP are adequate for achieving the objectives of our economic program. We will remain vigilant and stand ready to take any further measures that might prove necessary to achieve those objectives. We will consult with IMF staff on the adoption of such measures, and prior to any revision of the macroeconomic policies described in the MEFP, in accordance with the IMF's policies on such consultations. All information and data required for program monitoring will be reported to IMF staff.

8. In accordance with the usual provisions of an arrangement of this kind, we have assessed the central bank's safeguards. In this connection, we have also put in place a technical memorandum of understanding between the Central Bank of Tunisia and the Ministry of Finance to clarify responsibilities associated with financial obligations with respect to IMF resources which, in the case of budget support, will be held by the Central Bank of Tunisia pending their utilization.

9. We authorize IMF staff to publish this letter of intent together with its attachments (MEFP, Tables 1 and 2) and the accompanying IMF staff report.

Sincerely yours,

/s/
Chedly Ayari
Governor of the Central Bank of Tunisia

/s/
Slim Chaker
Minister of Finance

Attachment I. Memorandum on Economic and Financial Policies

1. The Tunisian government has drawn up an economic program that aims at generating stronger and more inclusive growth to support job creation. This program is supported by an action plan on major reforms that will be part the forthcoming five-Year Development Plan 2016-20. This memorandum describes the macro-critical elements of the IMF-supported government program over a four-year period under an Extended Fund Facility (EFF) arrangement.

ECONOMIC CONTEXT

2. Tunisia's economy has shown great resilience in withstanding internal and external shocks. Although weak, growth remained positive in 2015 at 0.8 percent, mainly due to exceptionally high olive-oil production and the decline in global energy prices. However, difficulties in Tunisia's regions, uncertainty related the last phase of the political transition, ongoing social tensions, and above all, deadly terrorist attacks have weighed heavily on economic activity. Inverting the downward trend in investment, which continued in 2015, poses a major challenge.

3. Significant internal and external imbalances remain. The authorities have started a fiscal consolidation process, driven by revenue improvements. However, the composition of public expenditure worsened and public debt increased significantly, especially costly foreign borrowing (accounting for 63 percent of total debt). Headline inflation continues its decline, with core inflation (excluding food and energy) at a relatively high level but expected to drop in the coming months. Despite a significant improvement in the trade balance, due mainly to exceptionally strong agricultural exports and, to a lesser degree, falling world commodity prices, the current-account deficit remained stuck at about 8.9 percent of GDP (close to the 2014 level) because of declining tourism and remittance inflows. Disbursements from the AfDB and the World Bank and proceeds from an international bond issuance helped stabilize foreign exchange reserves at US$7.6 billion in 2015, a level that covers more than four months of imports.

4. Longstanding structural challenges limit Tunisia's growth potential. Binding growth constraints include: limited access to finance for small and medium enterprises (SMEs), a heavy regulatory burden, lengthy authorization processes, investment restrictions or tax incentives, lack of competition, inefficient government institutions, and depressed public investment. In addition, major external shocks have limited annual growth to 1.5 percent in the past five years, a level that is too low to reduce unemployment. The weak performance of state-owned enterprises' (SOEs) further dampens growth and their inefficiency acts as an additional drain on government finances.

Medium-term macroeconomic outlook

5. The government's economic program aims to restore economic growth and gradually correct external and internal imbalances. It calls for fiscal consolidation to stabilize and eventually reduce public debt, rebalancing of the budget towards high-priority investment expenditure, prudent monetary policy, greater exchange rate flexibility, and structural reforms. The

implementation of these reforms should re-start growth and cushion the impact of factors that weigh upon Tunisia's economy, especially those related to social and security tensions.

6. Tunisia's economic performance is expected to gather pace over the medium term. Growth in 2016 will remain modest (2 percent), but structural reforms, the easing of investors' wait-and-see attitude, and the reduction of social tensions should strengthen growth to an average of 4 percent (2017 to 2020). The overall downward inflationary trend should continue, assisted by prudent monetary policy. Fiscal consolidation will gradually reduce the structural budget deficit (i.e., deficit corrected for the economic cycle and excluding bank recapitalizing and civil service reform costs) by 2.2 percentage points of GDP by 2019, thereby stabilizing public debt at 51 percent of GDP. Tighter fiscal policy, combined with the gradual correction of the dinar's over-valuation and a recovery in Europe, should reduce the current-account deficit to 4.4 percent of GDP in the medium term. A stronger current account, a rebound in foreign direct investment following improvements to the business climate, and a significant volume of external financing will keep foreign exchange reserves above 100 percent of the Fund's ARA (assessment of reserve adequacy) index. This level covers more than four and half months of imports from 2016 onwards.

OBJECTIVES AND STRATEGY UNDER THE PROGRAM

7. Our economic and reform program aims primarily to transform Tunisia's economy so that it can generate more inclusive growth and create jobs. Our program is based on four pillars: (i) consolidating macroeconomic stability, a prerequisite for economic growth; (ii) reforming government institutions to improve service delivery, increase transparency, and reallocate public expenditure with a view to reducing regional and social inequalities; (iii) reforming the banking sector so that it can adequately support growth; and (iv) developing the private sector to create jobs, which is our highest priority.

8. Our reform agenda is comprehensive, requiring dialogue, consensus, and closer coordination among the main stakeholders in the Tunisian economy. We have therefore set up a unit in the Prime Minister's office to oversee economic reforms. It will have full coordination powers to ensure that reforms are carried out within the agreed timeline.

F. Consolidating Macroeconomic Stability

Fiscal policy

9. The cornerstone of medium-term fiscal policy is to reduce public debt to a sustainable level while rebalancing the composition of the budget towards priority spending that can generate inclusive growth. Our medium-term debt sustainability objective is to bring the overall fiscal deficit (excluding grants) to the equivalent of 2.4 percent of GDP by 2019 and stabilize the debt-to-GDP ratio at 51 percent. These projects include one-off costs related to civil service reform during the program's duration. Establishing a more equitable and effective tax system and reducing the wage bill to the equivalent of 12.7 percent of GDP by 2019 should create the necessary fiscal

space to increase investment to 7 percent of GDP. An increase of social transfers is also envisaged as part of a new social safety net.

10. The 2016 budget law initiates a fiscal consolidation process that reduces financing constraints, while reflecting urgent needs associated with security and social tensions. Accordingly, it had called for a structural fiscal deficit—corrected for the economic cycle and excluding bank recapitalizing costs—of approximately 3.6 percent of GDP. This deficit takes into account the impact of wage increases and new wage "agreements", a 16 percent increase in capital expenditure, a reduction in energy subsidies, and the implementation of the first phase of the tax reform (reducing exemptions and rationalizing customs duties).

11. A slight deviation from the budget target is envisaged in 2016 to address new needs arising from new security requirements and recent economic developments. Since the beginning of the year, we have faced additional, unforeseen costs of 1.2 percent of GDP, mainly due to security expenditures (0.4 percent of GDP), increases in security personnel (0.3 percent of GDP), expenditures on other goods and services (0.1 percent of GDP), and a transfer to the pension system (related to the delay in approving legislation which extends the retirement age) (0.4 percent of GDP). The impact of these costs—exacerbated by the decline in tax revenue (1.0 percent of GDP) and nontax revenue (0.3 percent of GDP) from the contraction of economic activity and the fall in oil prices—will only be partially offset by the reduction in energy subsidies (0.5 percent of GDP) and a profit transfer of 0.4 percent of GDP from the STIR (Tunisian Refineries Corporation) arising from lower global oil prices, the sale of 4G mobile telephone licenses (0.4 percent of GDP), lower unallocated expenditure (0.2 percent of GDP), and a rationalization of promotions and performance bonuses that keeps the wage bill in line with the budgeted level (0.3 percent of GDP). As a consequence, the structural fiscal deficit for 2016 will be 0.4 percent of GDP higher than implied by the budget.

12. We remain committed to taking additional measures to correct any deviation from our fiscal targets, including reducing current expenditures that have been a source of budget overruns in the past. Investment and social expenditures (excluding energy subsidies) will be protected and will not be constrained by our fiscal consolidation strategy.

13. Substantial budget support will be necessary to meet our financing needs. The 2016 budget will receive donor support from the World Bank (US$550 million), the African Development Bank (US$500 million), and the European Union (US$492 million in financing and US$96 million in grants). We also plan a bond issue of US$500 million in international markets with a guarantee from the United States' government. In light of the high cost of borrowing in international markets, greater use of the domestic debt market is also planned (approximately 2.3 billion dinars), although we will limit issuance to avoid crowding out private-sector credit. We request that the first disbursement of the IMF's Extended Fund Facility be allocated to the government's budget to alleviate expected cash-flow pressures during the first half of the year.

Monetary policy

14. The Central Bank of Tunisia (CBT) has recently pursued an accommodative monetary policy. The slowdown in private sector credit, a widening output gap (2.5 percent in 2015), and a downward inflationary trend led the central bank to lower its policy rate by 50 basis points in October 2015. Nevertheless, we are ready to tighten monetary policy to prevent any resurgence of inflationary pressures, particularly should core inflation increase because of a depreciating dinar or higher wages. Higher policy rates would also support positive real interest rates, which is one of the central bank's main objectives.

15. Reform of the monetary policy framework is ongoing. To anchor inflation expectations, we plan to gradually move towards a credible inflation-targeting framework in the medium term, once the prerequisites for the transition are met. The priorities are as follows:

- **Approval of the new CBT statutes.** To strengthen central bank independence, a new central banking law was approved by the Assembly of the People's Representatives (ARP) in April 2016 (prior action). That law confirms price stability as the central bank's overriding objective. A greater focus on communication will also be important to enhance the monetary policy framework.

- **Lender of last resort.** The implementation of a lender-of-last-resort (LOLR) facility by September 2016 will allow a differentiation of urgent liquidity operations from monetary policy ones. A framework agreement for loans granted under the LOLR was established in April with Fund technical assistance (TA). This mechanism will also contain risks to the central bank's balance sheet and delineate the justification for bank financing needs, which remain high (nearly 4.7 billion dinars, excluding FX swaps, at the end-March 2016). In tandem with that reform, we intend to sharpen the qualitative criteria used to rate refinancing collateral (including a revision of the proportion of treasury bills which may be used for that purpose) and, by June 2017 (with TA from the Fund), introduce ratings instruments to strengthen the existing haircut system, including for government securities.

- **Strengthening the monetary policy framework.** We initiated in April 2016 the drafting of a manual for monetary policy operations with TA from the Bank of France and Fund staff. With an expected implementation date of June 2017, the manual will streamline several texts that currently govern money market operations (intervention tools, operations, counterparties and eligible assets, penalties, discretionary measures) into a single manual for monetary policy operations. It will also tighten our collateralization system. By December 2016, our liquidity forecasting should improve thanks to the implementation of a system to analyze deviations from forecasts and adjust liquidity allocations.

- **Developing the interbank market,** based on four pillars: (i) introduction of a fixing system for interbank rates in December 2016; (ii) development of a yield curve by 2017, including the use of separate auctions by maturity; (iii) diversification of liquidity management instruments to include repurchase agreements; and (iv) introduction of interest-rate hedging instrument by June 2017.

16. Until a stronger monetary policy framework is in place, the program will retain a ceiling on the central bank's net domestic assets as a performance criterion. In coordination with Fund staff and depending on the progress made towards moving to an inflation-targeting framework, this criterion could be modified in future reviews to include a monetary policy consultation clause (MPCC). Using this clause will require that the pre-requisites for a credible inflation-targeting framework are in place (including a more flexible exchange rate).

Exchange-rate policy

17. The change underway in the operational framework of the foreign exchange market will encourage market deepening and allow for greater exchange rate flexibility. The regular foreign-exchange auction system, introduced in February 2016 with Fund TA, will help promote competitive bidding for foreign exchange, improve operational transparency, and reduce operational risk. The mechanism, in which nine banks are participating (90 percent of the market), will contribute to greater exchange rate flexibility and will further reduce our market interventions (already reduced from an average of 37 percent of the market in 2014 to 24 percent in the fourth quarter of 2015). The recent circular, which severs the link between interbank, trade, and financial operations, will further stimulate activity in the foreign exchange market. The circular also grants more flexibility to cover exchange and interest rate risk (forwards, swaps, and options) and for registered intermediaries to convert foreign bank drafts into foreign exchange (instead of converting only into dinars).

18. More exchange rate flexibility is essential to improve competitiveness, conserve the central bank's international reserves, and facilitate external adjustment. In addition to the ongoing measures listed above, we intend to make the exchange rate market more flexible by:

- **Limiting central bank interventions** in the foreign-exchange market to smooth out excessive fluctuations. Holding FX auctions will allow the exchange rate to be determined by market forces, among others. To that end, we are firmly committed to limiting net foreign-exchange sales, and that only if the market cannot supply the necessary foreign exchange. A more flexible exchange rate will help gradually correct the overvaluation of the dinar and improve alignment with macroeconomic fundamentals. We also plan to buy foreign exchange when market conditions permit;

- **Gradually making foreign exchange regulations more flexible as prerequisites are met.** The CBT Board of Directors has approved measures to encourage capital mobility over the medium term. Among these measures, which are key to facilitating investment and economic operations, are the following: (i) reducing ex-ante controls by the CBT with respect to capital operations and replacing them with ex-post controls; (ii) eliminating the cap on the amounts that foreigners can buy of government securities or securities issued by resident companies; (iii) removing all caps on foreign borrowing by domestic credit institutions and export-only companies, and raising the cap for all other enterprises (to 10 million dinars); and (iv) making foreign exchange operations more flexible by delegating certain transfer procedures to banks.

G. Reforming Government Institutions

19. The government is firmly committed to reforming government institutions. One of our high-priority objectives is to make the public administration more productive and to improve service delivery to citizens and enterprises. Better governance will also help sustain growth. Reforms to the civil service, public-sector enterprises, tax policy and administration, pension funds, and social safety nets are essential to improve the efficiency and effectiveness of public services and to enhance the management of government expenditure and government debt. Fighting corruption will be part of all our reforms (see below).

20. Restructuring the civil service remains a top priority to improve the efficiency and effectiveness of the public administration and contain the wage bill. By September 2016, we will adopt a civil service reform strategy aimed at (i) redefining the government's functions, duties, and responsibilities, (ii) establishing statutes for the senior civil service in addition to the ongoing revision of general status, (iii) redeploying officials between ministries and regions to optimize government activities according to needs, (iv) reducing staff numbers (including by voluntary separations and no replacement of those who leave), (v) updating the civil service recruitment process, (vi) reviewing the salary and benefits structure, and (vii) redefining civil service performance evaluation and career paths. This strategy, consistent with our objective of reducing the wage bill to the equivalent of 12 percent of GDP in 2020 (53 percent of tax revenues) will be adopted by the Council of Ministers by end-September 2016 (structural benchmark). Broad discussions initiated at the national employment conference in March 2016 will help develop a consensus on the main objectives and components of the strategy. The strategy will set out the main reform areas, specific action plans, deadlines, expected results, and the government entities responsible for implementation of each action. Although specific measures remain to be determined, we are committed to ensuring implementation by:

- **Maintaining the hiring freeze** in all ministries through the next three years, with the exception of urgent needs for security and defense personnel. This measure will also be assessed over the next two years to ensure that the large number of retiring civil servants from 2018 onward will not create staffing distortions and a lack of experienced personnel in public administration;

- **Containing the increase in the 2017 wage bill to no more than the rate of inflation**, i.e., 4 percent. This goal implies taking measures to cut spending equivalent to 0.6 percent of GDP. These measures will be established in the 2017 budget, and may include a menu of options, among them the harmonization and rationalization of benefits and performance bonuses and the suspension of promotions.

- **Facilitating the redeployment of staff to regions outside the capital.** Carrying out this measure will require a review of ministries' functions and responsibilities. The reviews for four ministries (the Ministries of Health, Education, Finance, and Infrastructures), which account for over half of all the country's civil servants, will be completed by December 2016 (structural benchmark). By December 2016, the government intends to review the legal framework for redeploying civil servants and other government personnel to help implement the results of the

functional reviews. In 2017, functional reviews will also cover all other ministries beyond the first four, which will define duties and responsibilities, recruitment requirements, staff reallocation, and budget cost structure of each ministry.

- **Developing a voluntary separation program.** In parallel with our redeployment efforts, we will examine the possibility of carrying out a voluntary separation program beginning in 2018. Technical and financial assistance from our development partners will be requested to support us in this effort.

21. Strengthening the oversight of state-owned enterprises (SOEs) and restructuring them will improve the quality of their service delivery and ensure their financial viability over the medium term. The strategy we adopted in October 2015 is based on promoting good governance in the public sector and fully acknowledges the government as a shareholder. It also strengthens internal governance and supports financial restructuring of SOEs. To that end, we will establish by January 2017 an agency to manage the government's corporate shareholdings, oversee SOE restructuring programs (including the banks in which the government has equity stakes), and overhaul their governance. All the other bodies that have up to now reported to the Prime Ministry or the Ministry of Finance and who are responsible for overseeing SOEs under restructuring will be grouped together under a supervision and coordination committee. In the meantime, we will finalize performance-based contracts that will rely on management and financial indicators for the five largest public-sector enterprises—STEG (Société Tunisienne de l'Électricité et du Gaz), STIR, the Office des Céréales (National Grain Board), Tunisair, and the Régie Nationale des Tabacs (National Tobacco Company) (end-September 2016 structural benchmark). We will also produce a list of all arrears between SOEs and the State by December 2016 and between all SOEs by June 2017. In addition, the internal governance of SOEs will be strengthened by professionalizing their boards of directors, starting with the five largest. In parallel with these reforms, the government's shareholdings will be reviewed in order to identify nonstrategic sectors and sectors where the government's stake could be divested.

22. Reforming energy subsidies will enable us to lock in savings from the drop in world oil prices and create the necessary fiscal space to cover high-priority expenditures. The first part of this reform centers on establishing a symmetrical, automatic adjustment formula for petroleum products (gasoline, diesel fuel), which will be adopted in May 2016. This mechanism will be implemented in stages starting from July 2016 on a quarterly basis, then increasing onwards to a monthly basis from January 2017, to be gradually extended to other petroleum products (natural gas, kerosene). The new pricing scheme will accompany the establishment of new minimum social-protection safety nets (see below). The second part of the reform will focus on electricity subsidies, with rates to be reviewed in 2017 (while maintaining a lifeline tariff to protect disadvantaged segments of society) and eliminating subsidized tariffs for all manufacturing and industrial sectors (as was the case for cement plants in 2014).

23. An adequate tax system, together with a modern tax administration, is crucial for promoting inclusive growth. We plan to achieve this objective by:

- A **tax policy reform** aimed at strengthening revenue collection and the fairness and transparency was initiated through the rationalization of VAT exemptions, reduction in the number of customs tariff rates, and closing the gap in corporate taxation between on-shore and off-shore businesses. To clearly communicate our vision to the public, the full strategy—including the harmonization of VAT rates, a further reduction of exemptions, a more progressive personal income tax (IRPP) with lower rates for low-income people, and revised allowances and deductions, together with the timetable for implementing these reforms—is expected to be approved by the Council of Ministers in May 2016 (prior action) and subsequently published.

- **A modern, efficient, and fair tax administration.** A new tax administration in line with international practices will be designed over the next 12 months with the aim of establishing an integrated and modern tax administration system within the next three to five years. In the short term, the Large Taxpayer Unit (LTU, which collects about 55 percent of tax revenues) will be reformed by December 2016 (structural benchmark) to include formal responsibility for major tax and enforcement functions (return processing, taxpayers advisory services, and audit). The LTU will also be responsible for closely monitoring and reporting on the arrears of large taxpayers using monthly information from the Public Accounting and Collections Directorate (DCPR), thereby ensuring that the largest taxpayers fully meet their tax obligations. In addition, a pilot medium-sized taxpayer office (MTO)—modeled on the reformed LTU model—will be established in the greater Tunis area by June 2017. Three other MTOs will be established throughout the country in 2017–18. In parallel, we will continue to work on implementing risk-based and selective audit programs across all segments of taxpayers, increase our efforts to identify and bring into compliance taxpayers currently in the informal sector, and improve services to compliant taxpayers.

24. Our economic reforms will be accompanied by a better targeted social protection system. To support the most vulnerable, a sustainable, effective, efficient, and transparent social protection system is essential. Once implemented, the scope of the system can be broadened quickly. Our main priorities are:

- A **targeted social safety net** based on data containing information on vulnerable families with limited incomes, which will be finalized by March 2017 (structural benchmark) using the findings of field surveys conducted in 2016. This system will be based on a new, unique social identifier which will be finalized once the lists of social assistance program beneficiaries have been cross-checked, with the aim of eliminating the fragmentation of social-protection safety nets. We intend to expand the coverage of this unique social identifier beyond vulnerable families with limited income to those registered in the existing social security system (8.3 million people) and beneficiaries of reduced-rate health care cards, which will help us define a new well-targeted social safety net by June 2017.

- A **pension scheme** that is more comprehensive and financially viable, to ensure people's security in retirement. Initially, adopting a voluntary increase in the retirement age in 2016 should smooth out short-term imbalances in the National Retirement and social Security Fund (CNRPS), which has no available cash reserves and will post an annual deficit of 0.4 percent of

GDP. Discussions within the National Council on Social Dialogue—which will be established in May 2016 once the national assembly has approved its creation—are planned in order to completely overhaul the system by 2017, reestablishing the CNRPS' financial viability. The key elements of the reform will focus on reviewing the parameters for calculating pensions (e.g., the replacement rate), the rate of contributions, and benefits. Developing this strategy will take into account the guidance defined by the reform of the civil service.

25. More effective public financial management is needed to increase transparency and good governance and assure the efficiency and effectiveness of public services. Our actions will focus on three main areas:

- **A new organic budget law.** This law, to be published in the official gazette in December 2016 (structural benchmark), will ensure that the budget is better designed. It will provide additional budget information (new functional classification), allow for tighter control on expenditures, and simplify budget execution and monitoring procedures. It will also entrench performance-based budgeting, with 18 ministries (85 percent of the budget) already preparing their budgets according to the new classification and a multiyear framework.

- **Cash-flow management.** Coordination will be strengthened between the Directorate General of Debt, the Treasury, and other units in the Ministry of Finance to improve cash flow management. This will be supported by monitoring a Treasury Single Account (TSA) that would only regroup sub-accounts that relate to central government. The management of TSA operations will benefit from Fund TA.

- **Reform of the public investment framework** to make it more effective and help accelerate public investment to 7 percent of GDP by 2020. The overhaul of the procurement system has started to show results with a 76 percent increase in new contracts awarded in 2015. At the same time, increased flexibility in reallocating investment expenditures from stalled to viable projects has helped improve the execution rate on investments to 90 percent in 2015. We will continue to identify constraints on, and introduce flexibility in, the execution of investment projects, especially in the most marginalized areas. Better planning, monitoring and follow-up in the regions will go hand in hand with the redeployment of staff, a main element of the civil service reform. Our priorities include identifying high-priority projects to be included in the 5-year development plan, simplifying procedures, accelerating the establishment of an evaluation and monitoring system for government projects at the regional and national levels, and reducing land-deed constraints.

26. Our debt management will be strengthened throughout the program. With TA from the World Bank, we will finalize a medium-term debt strategy by the end of December 2016 (structural benchmark) with the aim of strengthening debt management and minimizing costs, optimizing the composition of domestic and external debt, and ensuring debt sustainability. In coordination with the capital market development strategy, we will finalize an action plan by June 2016 to establish a debt management agency in 2017, which will have the authority to analyze fiscal risks and financing options. The agency will also closely monitor risks arising from guarantees (currently equivalent to

about 12 percent of GDP). To help deepen the domestic market, we will publish the timetable of regular auctions of government securities with three months' advance notice. We will also examine the possibility of issuing short-term treasury bills.

27. Stepping up the fight against corruption and increasing transparency will help the government fulfill its accountability responsibility to citizens and contribute to a better understanding of the reform impact. Improving electronic access to information and public services and reforming statistics are critical.

- **Reforming the anti-corruption framework.** The government is currently drafting a law to be approved no later than December 2016 (structural benchmark) to set up an independent "high-level constitutional body to fight corruption and promote good governance," which will be adequately resourced with criminal investigatory powers and access to relevant information to perform its functions. In the meantime, the government will issue a decree strengthening the oversight powers of existing "good governance units". Three additional laws are under preparation: (i) protection for whistleblowers (citizens who report corruption cases in government services), (ii) conflicts of interest in the public sector, and (iii) financial disclosure of net worth by senior government officials. The government will also continue to strengthen the AML/CFT framework to address corruption risks, specifically by implementing enhanced customer due diligence measures for domestic politically exposed persons in line with the FATF standard, and strengthening AML/CFT supervision" helped by the work of two commissions set up by the new August 2015 Anti-Terrorism and Money Laundering law

- **Reforming the system for data production, dissemination, and access.** In December 2015, a citizens' budget was published online for the first time. Tunisia has joined the "open government initiative", and the Ministry of Finance recently put the Mizaniatouna portal online to disclose budget performance. A draft organic law on access to information was voted by the ARP in March 2016, with its implementation decrees to be finalized by September 2016. This law will establish and facilitate access to government data. Moreover, a national e-Gov plan will bring government services in a unified portal online.

- **Reforming the statistics system.** Eurostat has completed a comprehensive diagnosis of our statistics system, and efforts to strengthen our national accounts statistics (both yearly and quarterly) are under way. Our reform strategy is aimed at consolidating the governance of the statistics system, modernizing the production of statistics, and maintaining quality standards. Our strategy will require substantial capacity-building for the National Bureau of Statistics (INS), a new National Statistics Charter, and the drafting of a new statistics law (in lieu of the 1999 law)—to be presented to the government in December 2016—to guarantee the independence of published statistics. It will strengthen the CBT's statistical and analytical capacities, including for the consolidation and modernization of monetary and balance-of-payments statistics. We are also committed to publish within agreed timelines the statistics required in support of industrial and employment policies, or for establishing national accounts. In this regard, the five-year household consumption survey will be completed in June 2016 and published no later than December 2016.

H. Financial Sector Policy

28. The soundness of the banking sector has improved, but vulnerabilities remain. Three public banks have recently been recapitalized, increasing the solvency ratio of the sector as a whole from 9.4 percent in December 2014 to 12.2 percent in December 2015. All the banks (except for the Banque Franco Tunisienne and a large public bank (BNA)) were in full compliance with the 10 percent regulatory minimum at end-2015. Credit growth slowed to 5.8 percent at end-February 2016. Deposit growth in 2015 was half that of 2014 (November to October), which affected liquidity and caused excessive recourse to central bank refinancing, particularly in the case of one public bank that was not in compliance with the minimum liquidity ratio. With respect to nonperforming loans, in spite of some progress in resolving them, they remain high at about 16 percent of total loans, but covered to 65 percent by provisions.

29. We have pursued our reform program to stabilize and strengthen the banking sector. To coordinate future reform commitments, a committee chaired by the Minister of Finance has been set up in April 2016, bringing together various stakeholders involved in financial sector reforms. The committee will monitor progress on reform implementation, and identify areas for further action. The committee will liaise closely the coordinating unit established in the Office of the President for major reforms. Significant progress has already been made in the following areas:

- **Public banks.** The three public banks were recapitalized in 2015 to bring them into line with prudential standards, including the solvency ratio and provisioning requirements highlighted in audits conducted from 2013–15. For the three banks, updated versions of their restructuring plans will be approved by their boards of directors by May 2016 (prior action). These updates take into account the new economic outlook.

- **Legislative and regulatory framework.** The laws concerning the central bank statutes and bankruptcy procedures were approved in April 2016, with the law on banks and financial institutions (hereinafter referred to as the banking law) to be approved by Parliament in May 2016 (parliamentary approval of all three laws are prior actions), in line with good international practices.

- **Banking supervision.** Building on the progress over the past two years, the process of strengthening banking supervision continues. In 2015, penalties were systematically applied to banks that failed to maintain prudential ratios; general and thematic on-site inspections were conducted, especially those related to credit risk management; and the intermediate steps necessary to implement automated reporting and establish a rating system for lending institutions (SYNTEC) has been implemented.

30. We are stepping up our efforts to reform the financial sector in order to reduce its vulnerabilities. Reforms will focus on four priorities:

- **Strategic and operational restructuring of the three public banks.** After the recapitalization, public banks have begun a process of operational restructuring; in the last quarter of 2015 the

banks' board of directors appointed new management. We will ensure the banks implement the restructuring plans approved by their boards of directors. The goals of the restructuring plan will feed into performance-based contracts (which monitor indicators such as the cost-to-income ratio and the restructuring of nonperforming loans, all on a consolidated basis including the banks' various subsidiaries) to accompany the restructuring (2016 end-June structural benchmark). In the medium term, the government will allow technical and strategic partners to purchase equity in the three banks by selling significant parts of its own stake, in order to strengthen banking expertise within the institutions and improve their governance. With respect to other minority stakes in banks held by the government, a divestment strategy is in progress.

- **Resolving nonperforming loans (NPLs)** is based on the following priorities: (i) implementing the bankruptcy law with the issuance of decrees setting out the corresponding implementing provisions by September 30, 2016, including a training program for officers of the court in the competent jurisdictions; (ii) setting up units within each public bank that specialize in NPL management by June 2016 to ensure that they are handled adequately; (iii) placing the governance structures of public banks on an equal footing with those of private banks by amending by December 2016 legal texts forbidding public banks from writing off nonperforming loans; (iv) adopting by December 2016 a new amendment to the law on credit recovery companies, allowing them to renegotiate NPLs directly with customers; and (v) simplifying the conditions whereby credit institutions can remove from their balance sheet unrecoverable loans that are fully provisioned (December 2016, as part of the budget law).

- **Strengthening risk-based supervision.** We will ensure that the 2015–20 action plan of the central bank's Directorate General of Banking Supervision (DGSB) is implemented, placing emphasis on meeting the plan's timeline. The plan has three main components:

  - **Overhauling the regulatory framework** to implement supervision based on the Basel Committee's three pillars (minimum capital requirements, supervisory review process, and market discipline). The framework will imply the adoption of CBT circulars on operational risk June 2016 and market risk the first quarter of 2017, with the support of technical assistance, and a regulatory guidance in September 2016 setting out qualitative standards that must be adhered to by the banks' internal ratings systems pursuant to circular 2006–19, thereby imposing the implementation of rating systems within the banks. By June 2016, the CBT will have comprehensive information on banks' intra-group transactions, including minority and nonfinancial holdings. Supervision will be carried out on a consolidated basis from the second half of 2018, unless the above-mentioned "reporting" information requires another prioritization and revision of the calendar. Lastly, the CBT will issue a circular in June 2016, whereby the lowering of the authorized maximum exposure vis-à-vis related parties will be phased in over two years, to 50 percent of a bank's Tier 1 capital at year-end 2017, and 25 percent at year-end 2018.

  - **Developing the DGSB's operational capacities and information systems.** The SYNTEC system will link the supervisory intensity to banks' risk profiles, and a risk-based supervision manual will be applied systematically starting in December 2016 (structural benchmark). To

optimize banks' data collection and treatment, reporting will be entirely automated from September 2016 onward. The DGSB's capacities will be strengthened by recruiting a dozen supervisors (in addition to the 10 already planned) for this specific purpose (with a closing date for applications no later than June 30, 2016).

- **Increasing on-site inspections over the next three years** and conducting at least seven general and/or thematic inspections a year as additional resources become available. In particular, by March 2017, the CBT will have conducted inspections in the seven largest private banks to verify that frameworks for credit risk management and provisioning meet best standards. The private banks' inspection program will take account those missions carried out in 2015 in two private banks. These seven inspections will be conducted with support from Fund TA and on the basis of terms of reference agreed upon with the CBT (completion of the seven inspections is a structural benchmark for end-March 2017). Moreover, the DGSB will continue to conduct inspections focusing on other prudential concerns (in particular, combating money laundering and monitoring the restructuring of the public banks)

- **Implementing the bank resolution framework and the deposit guarantee fund contained in the new banking law.** Implementation decrees for bank resolution and the deposit-guarantee fund will be adopted by September 30, 2016. The new rules will apply to all banks covered by the new resolution mechanism.

31. To promote financial inclusion and improve access to credit for SMEs and individuals, we will take the following three initiatives:

- **Developing a legal framework for private credit bureaus.** The regulatory framework for the operations of credit bureaus and the central bank's monitoring of their activities will be established in a separate organic law. Establishing private credit bureaus will complement the central credit register maintained at the CBT, allowing banks to better assess risk and grant loans, and reduce lending rates. Customers will be able to more easily switch between banks as part of a competitive marketplace. The new law on credit bureaus is expected to be adopted by Parliament in June 2016.

- **Reviewing the rules regarding the effective cost of borrowing and raising the cap on excessive lending rates.** This reform will be carried out in two phases. First, by December 2016 we will increase the allowable spread between the maximum lending rate allowed and effective rates on loans to at least the same level as it was in 2009 (i.e., 33 percent) (structural benchmark). By June 2017, we will finish overhauling the legal framework governing excessive interest rates by setting the threshold according to the borrower's profile (large enterprises, SMEs, professionals, individuals, etc.) rather than type of loans.

- **Streamlining government's support for the economy by establishing a Bank of Regions (BdR),** which will allow the government to support economic initiatives that the private sector does not finance. A number of public entities (the Banque Tunisienne de Solidarité [Tunisian

Solidarity Bank], the Banque de Financement des Petites et Moyennes Entreprises [SME Financing Bank], the Caisse des Dépôts et Consignation [Savings and Loan Bank], and the Société Tunisienne de Garantie [Tunisian Guarantee Company]) are currently in charge of providing finance for developmental purposes. Some of these entities will be brought together within the BdR, for which the business model is currently being developed. The BdR should be set up by March 2017 with technical support from the KfW German development agency. The BdR's financing solutions (loans, guarantees, etc.) will be offered in partnership with commercial banks.

Structural reforms

32. A favorable business climate is necessary to unleash the potential of the private sector in driving growth and creating jobs. Our first priority is to improve the regulatory framework to allow greater competition, promote market access, protect investors' rights, and encourage transparency. This will require issuing and implementing decrees to operationalize the three laws listed below (structural benchmark for the end-September 2016):

- **The competition law.** The implementation of this law, approved in September 2015, will encourage competition and reduce government intervention by (i) strengthening the advocacy powers of the Competition Board, (ii) defining the duties and responsibilities of the Competition Board and the ministry with regard to competition-related issues, (iii) reducing the deadlines (from six to three months) in which the Ministry of Trade and Commerce reviews proposed concentrations of ownership or mergers submitted by relevant companies, and (iv) strengthening enforcement by increasing company fines from 5 to 10 percent of their turnover if they are in violation of competition laws.

- **Public-private partnerships (PPPs).** Approved in November 2015, the law will be operative once the implementation decrees have been finalized. The government is making PPPs operational through feasibility and budget risk assessments, particularly for two pilot projects in the water and infrastructure sectors. Once the law becomes effective, it will be supported by a monitoring framework for budget risks associated with PPP projects.

- **The investment code.** Approval of the investment code will establish a more transparent regulatory framework. The code will better protect investors, significantly improve investment governance, and promote greater market access, particularly through a program to reduce the number of permits and authorizations required over the next five years. It will also ensure consistency between the country's development objectives and the investment incentives, with tax incentives to be consolidated into the tax code. The government has drafted three implementation decrees that will be issued at the latest by September 2016 once the ARP has adopted the investment code.

33. We will continue to streamline administrative procedures and regulations. We have already streamlined about 376 customs and tax formalities and 154 administrative procedures, considered as priorities for private sector activity in the areas of transport, commerce, industry,

justice, agriculture, social affairs, and land (and state-owned property) affairs. An impact study of the streamlining has started, and once complete in June 2016, we plan to initiate a third streamlining phase of 372 administrative procedures in the areas of housing infrastructure, territorial planning, healthcare, environment, tourism and interior. This stage will be carried out over the next two years.

34. We are committed to reducing labor market frictions. The National Dialogue on Employment, held in March 2016 in Tunis, resulted in a consultative dialogue and an analysis of job market developments. It helped establish a consensus amongst stakeholders on measures for the short and medium term. Following the conference, and with technical assistance from the International Labor Organization, we intend to develop by the first quarter of 2017 a national employment strategy that will: (i) improve the employability of job seekers, (ii) develop local SMEs, and (iii) reform vocational training so that, among other things, vocational training centers are more independent and have better governance. Lastly, we intend to speed up our efforts to implement work programs and support micro-projects that favor the youth and underprivileged areas

Table 1. Tunisia: Quantitative Performance Criteria and Indicative Targets 1/2/

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	Cumulative flows since beginning of 2015 (unless otherwise specified)	Cumulative Flows Since Beginning 2016 (unless otherwise specified)				Cumulative flows since beginning of 2017 (unless otherwise specified)	
	December 2015	March 2016	June 2016	September 2016	December 2016	March 2017	June 2017
	Projection	Projection	Proposed QPC/target	Indicative target	Proposed QPC/target	Indicative target	Indicative target
Quantitative Performance Criteria							
1. Floor on the primary balance of the central government (cash basis excl. grants; million of Tunisian dinars)	-3,246	-274	-1,209	-1,699	-2,326	-814	-676
2. Ceiling on net domestic assets of the Banque Centrale de Tunisie (Stock; million of Tunisian dinars)	1,924	3,220	4,887	3,498	2,191	2,363	2,826
3. Floor on net international reserves of the Banque Centrale de Tunisie (Stock; million of US dollars)	4,488	3,907	3,599	4,261	4,762	4,773	4,523
4. Ceiling on Current Primary Expenditure (million of Tunisian dinars)	18,088	5,189	9,539	14,497	19,724	5,244	9,637
Continuous Performance Criteria							
5. Ceiling on the accumulation of new external debt payment arrears by the central government	0	0	0	0	0	0	0
Quantitative Indicative Targets							
Floor on Social Spending 3/ (million of Tunisian dinars)	1,335	262	626	926	1,534	285	683
Ceiling on the accumulation of new domestic arrears	0	0	0	0	0	0	0
Program assumptions on which adjusters are calculated in case of deviations							
External financing of the central government on a cumulative basis (in US$ million) 4/	1,507	75	309	1,308	2,352	475	1,300
of which: Multilateral (excluding IMF), bilateral and budget grants (in US$ million)	1,370	0	159	626	1,635	400	800
Public external debt service (interest and amortization) on a cumulative basis (in US$ million)	961	230	511	811	1,113	270	1,175
Bank recapitalization and civil service reform costs (in million TD)	647	0	0	0	0	0	0
Privatization receipts in FX (in US$ million)	0	0	0	0	0	0	0
Resident deposits at the BCT (in US$ million) 5/	1,269	1,269	1,269	1,269	1,269	1,269	1,269
Foreign exchange swaps between the CBT and commercial banks (in million TD) 5/	603	603	603	603	603	603	603
Program exchange rate TD/ U.S. dollars	2.01285	2.01285	2.01285	2.01285	2.01285	2.01285	2.01285

1/ Quantitative performance criteria and structural benchmarks are described in the Technical Memorandum of Understanding.
2/ For purposes of calculating program adjusters, foreign currency amounts will be converted at program exchange rates.
3/ Public capital expenditures on social sectors and programs.
4/ Disbursment, includes project loans and capital market access but excludes IMF.
5/ At program exchange rate.

Table 2. Tunisia: Proposed Prior Actions and Structural Benchmarks

Prior actions	Objective	
Approval, by banks' boards, of the updated business plans for all three public banks.	*Financial sector stability*	
Adoption, by the Assembly, of the People's Representatives (ARP), of the CBT law, the banking law, and the bankruptcy law in line with good international practices.	*Ensure financial sector stability, modernize monetary regimes, and support inclusive growth and job creation*	
Adoption, by the Council of Ministers, of the comprehensive tax reform strategy, in line with the principles of fairness and efficiency agreed with IMF staff.	*Fiscal sustainability and fairness*	
Proposed structural benchmarks	**Objective**	**Date**
I. Financial sector reform		
Approval, by the board of Directors of public banks (STB, BH, and BNA), of performance contracts in line with their new restructuring plans.	*Financial sector stability*	Jun-16
Increase of the cap on lending rates to, at least, the 2009 level.	*Financial sector stability*	Dec-16
Systematic use, by the supervisors, of the new manual on risk-based supervision.	*Financial sector stability*	Dec-16
Inspection of the seven largest private banks in line with the best standards and with IMF Technical Assistance as agreed with the CBT.	*Financial sector stability*	Mar-17
II. Budget Policy and Reforms of Public Institutions		
Approval, by the Council of Ministers, of a comprehensive strategy on civil service reform.	*Fiscal sustainability and fairness*	Sep-16
Signature of performance contracts for the five largest public enterprises.	*Better monitoring of fiscal risks*	Sep-16
Completion of the functional review of four ministries (Health, Education, Finance, and Infrastructure).	*Fiscal sustainability and quality public services*	Dec-16
Publication, in the official journal, of the organic budget law.	*Fiscal sustainability and fairness*	Dec-16
Establishment of a Large Taxpayers Unit to include formal responsibility for the major tax and enforcement functions (return processing, taxpayer advisory services, and audit).	*Fiscal sustainability and fairness*	Dec-16
Adoption of a medium-term debt strategy.	*Debt sustainability and deepening of financial markets*	Dec-16
III. Sectoral reforms/private sector development		
Adoption of the implementation decrees for the new law on competition, law on PPPs, and new investment code.	*Inclusive growth and job creation*	Sep-16
Creation of an independent, high anti-corruption authority.	*Good governance and fairness*	Dec-16
Establishment of a databank on vulnerable households.	*Social protection and fairness*	Mar-17

Attachment II. Technical Memorandum of Understanding

1. This Memorandum establishes the agreement between the Tunisian authorities and IMF staff concerning the definition of the quantitative performance criteria and indicative targets under the program supported by the Extended Fund Facility. It also sets out the content and frequency of data reporting to IMF staff for program monitoring purposes.

2. The quantitative criteria and targets are defined in Table 1 of the Memorandum of Economic and Financial Policies (MEFP) attached to the Letter of Intent dated May 2, 2016. For program purposes, all assets, liabilities, and flows denominated in foreign currencies will be valued at the "program exchange rate," as defined below, with the exception of items affecting the government's budgetary accounts, which will be measured at current exchange rates. For program purposes, the exchange rate corresponds to the accounting exchange rate of the CBT prevailing on December 31, 2015, as shown in the table below. For the SDR, the program exchange rate is 1 SDR = 2.797590 Tunisian dinars.

Program Exchange Rates, Tunisian Dinars per FX Currency at End-December 2015
(Accounting exchange rate of the CBT)

Currency	Exchange rate
AED	0.54802
BHD	5.3373
CAD	1.45005
CHF	2.0322
DKK	0.2947335
DZD	0.01878
EUR	2.1993
GBP	2.9837
JPY	0.0167135
KWD	6.63225
LYD	1.44535
MAD	0.203175
NOK	0.228923
QAR	0.552815
SAR	0.53634
SEK	0.23918
USD	2.01285

3. Monetary gold assets will be valued, against the corresponding value in Dinar (at the program exchange rate) at the price of 2,138.15 dinar per ounce of gold in the international market on 12/31/2015 (London morning fixing). The stock of gold is 4.13 tons (4,129,806 grams) on December 31, 2015.

4. For data reporting purposes, the Ministry of Economy and Finance (MoF), the Ministry of Planning and Economic Cooperation (MDCI), the National Institute of Statistics (INS), and the Central Bank of Tunisia (CBT) will follow the rules and the format considered appropriate for data reporting as covered by this technical memorandum of understanding, unless otherwise agreed with IMF staff.

DEFINITION OF PERFORMANCE CRITERIA AND INDICATIVE TARGETS

A. Performance Criteria and Indicative Targets

5. The quantitative performance criteria and indicative targets specified in Table 1 of the MEFP are:

Performance criteria

- A performance criterion (**floor**) on the net international reserves of the Central Bank of Tunisia.
- A performance criterion on the net domestic assets **(ceiling)** of the Central Bank of Tunisia.
- A performance criterion (**floor**) on the primary balance of the central government, excluding grants.
- A performance criterion (**ceiling**) on total primary current expenditure of the central government.
- A continuous performance criterion on the accumulation of new external debt payment arrears (**zero ceiling**).

Indicative targets

- An indicative target (**ceiling**) on accumulation of new domestic arrears.
- An indicative target (**floor**) on capital expenditures in priority social sectors and social programs.

6. Measurement of criteria. The performance criteria on net international reserves and net domestic assets are measured on a stock and semi-annual basis. The performance criteria on the central government deficit on the total primary current expenditure of the central government are measured on a semi-annual basis and cumulatively from the end of the previous year. Adjustment factors will also be applied to some of these criteria. The performance criterion on the accumulation of new external arrears is measured on a continuous basis. Indicative criteria will be monitored on a quarterly basis.

B. Institutional Definition

7. The **central government** comprises all ministries and agencies subject to central budgetary administration in accordance with the organic law on the government budget. Regional governments and municipalities subject to central budgetary administration are part of the central government.

8. The authorities will inform Fund staff of any new entity and any new program or special budgetary or extra-budgetary fund created during the period of the program to carry out operations of a budgetary nature. Such funds or new programs will be included in the definition of the central government.

C. Floor on the Net International Reserves of the Central Bank of Tunisia

9. The **net international reserves (NIR)** of the Central Bank of Tunisia (CBT) are defined as the difference between the CBT's reserve assets and its liabilities in foreign currency to nonresidents.[6]

10. The **CBT's reserve assets** are the foreign assets immediately available and under the CBT control, as defined in the fifth edition of the IMF *Balance of Payments Manual*. They include gold, SDR assets, reserve position at the IMF, convertible foreign currencies, liquid balances held outside Tunisia, and negotiable foreign securities and bills purchased and discounted.

11. The **CBT's liabilities in foreign currency** to nonresidents include any commitment to sell foreign currencies associated with financial derivative transactions (such as swaps, futures, options), any portion of the CBT's assets (gold, for example) used as collateral, IMF and Arab Monetary Fund (AMF) credits outstanding, and deposits at the CBT of international organizations, foreign governments, and foreign bank and nonbank institutions. The government's foreign currency deposits at the CBT are not included in the liabilities, nor is any SDR allocation received after March 31, 2016.

12. All debt instruments issued in foreign currency by the CBT on behalf of the government after May 15, 2013 will be treated as **CBT liabilities**, unless the offering documents (prospectus) state

[6] Deposits of residents in foreign currency (excluding government deposits) at the CBT are a form of external liability of the CBT; for operational and accounting purposes, and because of legal considerations related to the regulation of foreign exchange, the CBT includes residents' foreign currency deposits in the monetary base. To preserve the accounting consistency of the CBT's accounts and be in line with the standard definition of NIR within the framework of IMF programs, it is agreed: (i) to retain the accounting definition of external liabilities used in the CBT balance at December 31, 2015; (ii) to adopt the principle of adjusting NIR (in the opposite direction of the net domestic assets of the CBT) on the basis of the variation in the residents' deposits in foreign currency from end-December of the previous year. It also agreed that the residents' deposits in foreign currency at the CBT include the following components of reserve money: intervention/monetary market in foreign currency, foreign currency of aggregate intermediaries, non-negotiable placement of foreign currencies, and all other items operations in foreign currency (including deposits and derivatives products) created or included in reserve money and resulting in a liability of the Central Bank to residents. At end-December 2015, the value of the stock of deposits in foreign currencies of residents at the CBT, including swaps, was US$1268.8 million at the program exchange rate.

clearly that (i) the CBT is acting as an agent to execute all sovereign debt instruments issued in foreign currency raised through the international markets for general budgetary purposes of the Republic of Tunisia (ii) debt is a liability of the central government; and (iii) a protocol between the CBT and the Ministry of Finance provides clearly that the CBT is authorized to pay all expenses and costs pertaining to the implementation of this issue as well as the interest and principal of the issue sum through direct deduction from the Treasury's current account established in the CBT's books.

13. The value of CBT reserve assets and liabilities in foreign currency will be calculated using program exchange rates (see Table above). On December 31, 2015, the value of the stock of net international reserves was US$4,487.5 million, with the stock of reserve assets equal to $7,496.6 million and the stock of CBT liabilities in foreign currency equal to US$3,009.2 million (at program rates).

D. Ceiling on Net Domestic Assets

14. The **CBT's net domestic assets** are defined as the difference between the monetary base and the net foreign assets of the CBT.

15. The **monetary base** includes: (i) fiduciary money (money in circulation excluding cash balances of banks and the Treasury); (ii) deposits of banks at the central bank (including foreign currency and deposit facility); and (iii) deposits of all other sectors at the central bank (i.e., other financial enterprises, households, and companies).

16. The **CBT's net foreign assets** are defined as the difference between the CBT's gross foreign assets, including foreign assets that are not part of the reserve assets, and all foreign liabilities of the CBT. Net foreign assets are valued at the program exchange rate defined in the above table.

E. Floor on the Primary Balance of the Central Government (Excluding Grants)

17. Under the program, the **primary fiscal balance of the central government (excluding grants, on a cash basis)** is measured on a financing basis and will be the negative sum of: (i) total net external financing; (ii) privatization receipts; (iii) net domestic bank financing; (iv) net domestic nonbank financing; *plus* (v) interest on domestic and external debt paid by the central government and *less* external budgetary grants received by the central government.

18. **Total net external financing** is defined as net external loans of the government, that is: new loan disbursements, *less* repayments of the principal. Project and budgetary loans of the central government are included, as well as any form of debt used to finance central government operations.

19. **Privatization receipts** are the government receipts from the sale of any government asset. This includes revenues from the sale of government shares in public and private enterprises, sales of nonfinancial assets, sales of licenses, and the sale of confiscated assets, excluding the confiscation of bank accounts. For the adjustor in NIR (see below), only receipts in foreign currency are included.

20. Net domestic bank financing of the central government is the sum of: the change in net bank loans to the central government (in Tunisian dinars and foreign currency) and the change in central government deposits at the CBT (this includes all central government accounts at the CBT, in particular (i) Treasury current account excluding the sub accounts N-bis, those related to Public Administrative Entities (EPA) and to local governments; (ii) Tunisian government account (miscellaneous dinar accounts); (iii) loan accounts; (iv) grant accounts; (v) FONAPRA-FOPRODI accounts; (vi) special accounts of the Tunisian government in foreign currency; (vii) accounts in foreign currency pending dinarization (subaccount: "mise a disposition"); (ix) and any other account that may be opened by the central government at the CBT or banks. Following the unification of government accounts at the CBT into a Single Treasury Account, government accounts are consolidated in two categories ("Compte Central du Government "and "Comptes Spéciaux du Government") on the CBT's balance sheet (liabilities side).

21. Net government borrowing from the banking system is defined as the change in the stock of government securities (Treasury bills and bonds) held by banks and any other central government borrowing from banks, less repayments.

22. Net domestic nonbank financing includes: the change in the stock of government securities (Treasury bills and bonds) held by nonbanks (including social security funds) and any other central government borrowing from nonbanks, less repayments. In particular, any use of cash from non-banking institutions (including La Poste) to finance the Treasury would be counted as domestic non-bank financing. Total Treasury bills and other public debt instruments to be taken into consideration are calculated at the nominal/face value shown on the institutions' balance sheet and does not include accrued interest.

F. Ceiling on Central Government Primary Current Expenditure (excluding Interest Payments on Public Debt)

23. Under the program, central government primary current expenditure is defined as the sum of central government expenditure on: (i) personnel wages and salaries; (ii) goods and services; (iii) transfers and subsidies; (iv) other unallocated current expenditure[7].

G. Ceiling on the Accumulation of External Arrears

24. Arrears on external debt payment are defined as late payments (principal and interest) on external debt or guarantees as defined in *External Debt Statistics: Guide for compilers*[8] by the central

[7] The methodologies used to measure current expenditure categories for the central government are those used to design the table of central government financial operations presented in the macroeconomic framework.

[8] The definition of debt set forth in *External Debt Statistics: Guide for Compilers* reads as the outstanding amount of those actual current, and not contingent, liabilities, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which require payment(s) of principal and/or interest by the debtor at some point(s) in the future and that are owed to nonresidents by residents of an economy. Debts owed to nonresidents can take a number of forms, the primary ones being as follows: (i) loans, that is, advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the

(continued)

government or the CBT after 90 days from the due date or the expiration of the applicable grace period.

H. Indicative Ceiling on the Accumulation of Domestic Arrears

25. For program purposes, arrears on **domestic debt payment** are defined as amounts owed to domestic financial and commercial creditors that are 90 days or more overdue with respect to a specific maturity date (or as defined in the contractual grace period, if any). If no maturity date is specified, arrears are defined as amounts owed to domestic creditors that remain unpaid beyond 90 days or more after the date on which the contract was signed or upon receipt of the invoice.

I. Indicative Floor on Social Expenditures

26. Social **expenditures** are defined as capital expenditures (development expenditures) on education, health, social transfers to needy families, the AMEL employment training program (and university scholarships), UTSS indemnities, family allocation as well as development expenditures of the Ministries of Women and Family Affairs, Youth and Sports and Social Affairs, and all new targeted cash transfers in support of vulnerable groups; all current expenditures ("dépenses de gestion") of the above-mentioned sectors and programs, as well as food and energy subsidies, are excluded.

J. Adjustment Factors for the Program Performance Criteria

27. The **NIR** targets are adjusted upward (downward) if the cumulative sum of net external financing of the central government , the sum of budgetary grants, privatization receipts received in foreign currency, the increase (decrease) in the residents' foreign currency deposits at the CBT (including FX swaps) are greater (lower) than the levels observed in the table below. The NIR targets will be also adjusted upward (downward) if the total amount of cash payments on external debt service of the government is lower (greater) than the levels included in the table below.

28. **The net domestic assets (NDA)** targets will be adjusted upward (downward) based on the downward (upward) adjustment of the NIR floor if the cumulative sum of net external financing of the central government, the sum of budgetary grants, privatization receipts received in foreign currency, the increase (decrease) in residents' foreign currency deposits at the CBT are lower (greater) than the levels indicated in the table below. The NDA targets are also adjusted upward (downward) based on the downward (upward) adjustment of the NIR floor if the total amount of

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funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, that is, contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and (iii) leases, that is, arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property.

cash payments on external debt service are greater (lower) than the levels included in the table below. The NDA targets are also adjusted upward (downward) based on downward (upward) change in the stock of foreign currency swaps between Central bank and the commercial banks compared to the level on December 31, 2015 (US$299.4 million, 602.65 million Tunisian dinars). The NDA ceiling will be converted into Tunisian dinars at the program exchange rate.

Program Assumptions on Adjustment Factors for the Quantitative Performance Criteria
(In million of US dollars)

	2016					2017				
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year
Official External Financing	75.0	551.0	999.0	1,361.0	2,985.9	475.0	1,143.2	75.0	893.2	2,586.4
Project loans	65.0	65.0	65.0	65.0	260.0	75.0	75.0	75.0	75.0	300.0
Multilateral donors	-	476.0	419.0	1,281.0	2,175.9	400.0	568.2	-	318.2	1,286.4
AFDB	-	-	200.0	300.0	500.0	-	-	-	-	-
AMF (Arab Monetary Fund)	-	-	-	-	-	-	-	-	-	-
IMF (budget support starting 2017)	-	317.0	-	317.0	633.9	-	318.2	-	318.2	636.4
World Bank Group	-	50.0	-	500.0	550.0	400.0	-	-	-	400.0
European Union	-	109.0	219.0	164.0	492.0	-	250.0	-	-	250.0
Bilateral donors	-	-	-	-	-	-	-	-	-	-
Financial Market Access and other	10.0	10.0	515.0	15.0	550.0	-	500.0	-	500.0	1,000.0
Sukuk and other market financing	-	-	-	-	-	-	500.0	-	500.0	1,000.0
Market issuance with US Treasury guarantee	-	-	500.0	-	500.0	-	-	-	-	-
Loan Transfers to SOEs	10.0	10.0	15.0	15.0	50.0	-	-	-	-	-
Budget Grants	-	-	47.7	45.4	93.1	-	150.0	-	0.9	150.9
Privatization Receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Government External Debt Service	206.5	280.9	282.5	282.6	1052.5	265.9	807.1	445.7	332.2	1851.0
Amortization	103.1	188.2	153.8	224.8	669.9	142.2	725.1	327.4	282.9	1477.5
Interest	103.4	92.7	128.7	57.8	382.6	123.7	82.1	118.4	49.3	373.5
Bank recapitalization and one-off costs linked to the civil service reform	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
FX swaps between the CBT and the commecial banks	299.4	299.4	299.4	299.4	299.4	299.4	299.4	299.4	299.4	299.4
FX swaps between the CBT and the commecial banks (in million of Tunisian dinars)	602.7	602.7	602.7	602.7	602.7	602.7	602.7	602.7	602.7	602.7
Resident deposits at the BCT, including FX swaps	1268.8	1268.8	1268.8	1268.8	1268.8	1268.8	1268.8	1268.8	1268.8	1268.8

Sources: Tunisian authorities and IMF staff estimates.

29. The ceilings on the **NDA of the CBT** will also be adjusted downward or upward based on the amount of CBT reserves released/mobilized because of a possible decrease/increase in the reserve requirement.

30. The floor on the **primary balance of the central government**, excluding grants, will be adjusted upward/downward based on the amount used to recapitalize the public banks and all amount used to finance the severance pay of the voluntary departures which may be part of the civil service reform.

K. Monitoring and Reporting Requirements

31. Performance under the program will be monitored using data supplied to the IMF by the Tunisian authorities as outlined in the table below, consistent with the program definitions above. The authorities will promptly transmit to the IMF staff these data and any data revisions previously transmitted to the IMF Resident Representative's office in Tunisia.

Information to Be Reported in the Context of the Program			
Type of Data and Description	***Periodicity*** ***Weekly (w) Monthly (m) Quarterly (q)***	***Delay in days***	***Responsible department***
GDP: Supply and demand at current, constant, and the previous year's prices, including sectoral indices.	*q*	*45*	*INS*
Inflation: Including the underlying inflation of non-administered and administered prices.	*m*	*14*	*INS*
Fiscal Sector			
Tax and nontax revenue of the central government decomposed on the basis of main tax and nontax revenues items	*m*	*30*	MoF
Total expenditures: current and capital, transfers and subsidies.	*m*	*30*	MoF
Capital expenditure: by type of financing: domestic and external (differentiating loans and grants), and by main sectors and projects (agriculture, social, infrastructure).	*m*	*45*	MoF
Current expenditure: by type of expenditure: wages, goods and services, transfers.	*m*	*45*	MoF
Social expenditure	*q*	*45*	MoF
Domestic and foreign debt			MoF
Stock of domestic and foreign debt: of the central government and debt guaranteed by the government, with breakdown by instrument and type of currency (in dinars and foreign currency with the equivalent in domestic currency).	*q*	*30*	MoF
Stock of domestic arrears as per TMU, as well the stock of accounts payable that correspond to expenditures committed/ payment ordered more than 90 days before (and by type of expenditures),	*q*	*45*	MoF

Disbursement of foreign loans: Breakdown into project loans and budgetary loans by principal donor and identifying the most important projects to be financed in the original currency and its equivalent in Tunisian dinars converted at the current exchange rate at the time of each transaction. **Domestic borrowing from banks and nonbanks:** including bonds, Treasury bills, and other issued securities.	*m*	*30*	MoF
Debt guaranteed by the government: by instrument and type of currency (in dinars and in foreign currencies and its equivalent in national currency) **External and domestic debt service:** amortization and interest.	*m*	*60*	MoF
External payment arrears: external debt contracted and guaranteed by the government.	*q*	*30*	MoF/ CBT
Debt rescheduling: possible rescheduling of debts contracted and guaranteed by the government, agreed with creditors.	*q*	*45*	MoF
Consolidated accounts of the central government at the CBT: The stock of deposits will be broken down as follows: (i) Treasury current account; detailed by sub accounts of the central government, N BIS, outstanding payments, Public administrative entities (EPA), and local governments (ii) special account of the Tunisian government in foreign currency and its equivalent in dinars; (iii) miscellaneous dinar accounts; (iv) loan accounts; (v) grant accounts; (vi) FONAPRA-FOPRODI accounts; and (vii) Foreign exchange accounts pending adjustment in dinars (available).	*m*	*30*	*CBT* MoF/TGT for sub-account
External Sector			
Imports of Petroleum Products: average import price and volume of main petroleum products.	*m*	*30*	*CBT*
Deposits: Stock of foreign currency deposits, according to the residence of the holder.	*m*	*14*	*CBT*
External debt: Debt service (amortization and interest) of institutional agents by type of currency (in foreign currency and its equivalent in dinars). Stock of external debt of institutional agents by type of currency (in foreign currency and its equivalent in dinars). Overall net external position of Tunisia (in conformity with our obligations under SDDS).	*q* *q* *A*	*30* *90* *180*	*CBT*
Balance of payments: Prepared by the CBT	*q*	*30*	*CBT*

Monetary and Financial Sector			
CBT accounts at the current exchange rate: detailed table including the monetary system.	*m*	*30*	*CBT*
CBT accounts at the program exchange rate: Including net international reserves.	*m*	*30*	*CBT*
Foreign exchange market operations, Interbank market, retail market and wire transfers for CBT purchases on the retail market: CBT Interventions (sales and purchases) on the foreign exchange market in million of dinars (and equivalent in US million) including the CBT share in percentage of the market transactions, stock of CBT currency swap (provide details on direction of transactions (TND/FX or FX/TND), amounts of principal, spot exchange rate in swaps agreement, interest rate applied on FX counterpart), detailed information on other BCT's forward foreign exchange operations, including outright forward sales of Tunisian dinar . The terms and conditions of any new transactions (including the extension or renewal of existing terms and conditions) will also be provided. CBT foreign exchange reserves, breakdown by currency and by instrument.	*m*	*30*	*CBT*
Banks' financial soundness ratios: Indicators of financial soundness and regulatory capital adequacy ratios of the banking system, including the quality of assets and the profitability of banks. The indication of the different banks is optional.	*m*	*30*	*CBT*
Direct refinancing of commercial banks by the CBT: Breakdown by bank.	*m*	*14*	*CBT*
NPLs: Stock of banking sector NPLs, and breakdown by commercial banks.	*q*	*60*	*CBT*
Balance sheets of commercial banks, including detailed income statements, in accordance with "Uniform Bank Performance Reporting" agreed with Fund staff.	*q*	*60*	*CBT*
Other information to be reported			
Information on Fiscal, Monetary, and Financial Policy: Decrees or circulars newly adopted or revised concerning changes in tax policy, tax administration, foreign exchange market regulations, and banking regulations. A copy of official notices of changes in gas and electricity rates and any other surcharge (automatic or structural), as well as the prices of petroleum products and levies/surcharges on gas and petroleum.	*d*	*3*	*CBT/MoF*
The price structure of the petroleum products and the needed data to monitor the automatic adjustment mechanism (formulas and data).	*d*	*15*	*Min. of Energy*

INTERNATIONAL MONETARY FUND

TUNISIA

May 17, 2016

REQUEST FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY—SUPPLEMENTARY INFORMATION, SUPPLEMENTARY MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

Prepared By | Middle East and Central Asia Department

This supplement reports on the implementation of the prior actions since the Staff Report was issued on May 3, 2016. While two prior actions have not been met, staff supports Tunisia's request for the extended arrangement under the Extended Fund Facility (EFF), given the substantial progress made toward meeting them alongside the authorities' commitment, as outlined in the authorities' supplement to the MEFP, to continue to address shortcomings by implementing two structural benchmarks. The inability to complete all elements of the prior actions on time, nevertheless, highlights risks to the EFF-supported program in a political environment that remains fragile.

1. **The prior action on the tax strategy has been met**. The Council of Ministers adopted in early May a strategy anchored on the principles of equity and efficiency of the tax system, with a timeline for: (i) broadening the VAT base by reducing exemptions; (ii) rationalizing VAT rates (from three to two); (iii) introducing a more progressive personal income tax (including through less deductions and a significantly higher tax threshold); (iv) reducing further the dichotomy between the offshore and onshore corporate tax rates by 2018; and (v) increasing the tax on dividends. A study on earmarked taxation is expected to further rationalize "special treasury funds" and the taxes funding them. The authorities are also working on reforming their tax incentives framework; staff urges the authorities to rationalize tax incentives as they distort economic decisions and have failed in the past to stimulate investment in Tunisia.

2. **Notwithstanding considerable progress, the prior action on the central bank, banking, and bankruptcy laws has not been met.** The new legislation enhances central bank independence, introduces a lender of last resort mechanism, establishes a banking resolution mechanism and a deposit guarantee fund, and modernizes the bankruptcy regime, representing considerable advances over the existing framework. The bankruptcy law is in line with good international practices. However, the prior action is not met in view of the remaining gaps with good international practices on central bank autonomy (e.g., government presence in the CBT board) and in the resolution framework (eg., constraints of the guarantee fund to finance transactions, creditor hierarchy in liquidation, and government presence in the resolution committee).

3. **The prior action on the business plans of public banks has also not been met.** All three banks revised their business plans, which were subsequently adopted by their boards. Staff judged that one business plan (BH) was in line with minimum regulatory requirements, with the planned issuance of subordinated loans helping BH comply with prudential ratios during the entire restructuring period. However, this was not the case for the business plans of two other banks:

- **For the STB,** progress has been made but not enough to meet minimum prudential requirements as new financial assumptions are more modest than in the initial plan but still depend on finalizing a NPL resolution strategy that is already underway. A newly hired external consultant will help the bank finalize its business plan by end-June.
- **For the BNA,** additional work is needed for it to meet minimum requirements. A Council of Ministers meeting in early May clarified the government's policy on the agricultural sector and on government guarantees backing loans provided to SOEs. This decision paves the way for the bank to revise its plan in the next few weeks with a clear justification of the profitability of its exposure to the agricultural sector and of its NPL reduction strategy. Additional revisions are needed to ensure regulatory compliance throughout the restructuring period.

4. **Staff regrets that the legislation does not meet good international practices in all respects, but welcomes the progress made and encourages the authorities to make future amendments to close remaining gaps.** In addition, staff welcomes the authorities' plans to address some of the shortcomings of the banking law regarding the resolution framework through decrees (e.g., for least–cost test of resolution) and by-laws (e.g., a short timeframe to determine resolution measures for systemic cases). Timely implementation of the related structural benchmarks, as outlined in the supplement to the MEFP, will be critical for the success of the program and hence for the completion of the first review. Staff will, furthermore, continue to work with the authorities to improve the CBT law and align it with good international practices during the EFF-supported program.

5. Staff regrets the latest delays in finalizing banks' business plans and urges their swift adoption to ensure the implementation of sound operational restructuring. The finalization of proper business plans along the lines outlined in the supplement to the MEFP will be critical for the success of the program, and hence for the completion of the first review. Implementation will, furthermore, be enhanced by the signing of performance contracts, which should monitor banks' financial performance on a consolidated basis (at least for some key indicators).

Supplementary Memorandum of Economic and Financial Policies

Tunis, May 17, 2016

Madam Christine Lagarde
Managing Director
International Monetary Fund
700 19th Street, NW
Washington, DC 20431
USA

Madam Managing Director:

1. The information below updates the memorandum of Economic and Financial Policies (MEFP) annexed to our letter dated May 2, 2016 to reflect developments of the past few weeks and our latest commitments on banking reforms (Table 1).

2. The new legislation on the central bank, bankruptcy and banking statutes was adopted in early May 2016. These laws will have a large transformational impact on Tunisia's business environment and banking sector, accelerating the modernization of the country's economic structure in a more efficient and equitable way. To ensure the recently approved legislation reduces the remaining gaps with good international practices on banking resolution, we will introduce improvements in the resolution framework by end-August (structural benchmark) through: (i) adoption of a government decree to implement the framework of the Bank Deposit Guarantee Fund that includes a least cost-test for resolution with an exception for systemic cases; and (ii) adoption of a bylaw of the Resolution Committee providing a short timeframe to determine resolution measures for systemic cases.

3. All three public banks revised their business plans, but two of them need further revisions to ensure regulatory compliance throughout the restructuring period. The recently appointed management of the STB and BNA public banks initiated their organizational restructuring, but found that more time was needed to revise the business plans in order to fine tune their business strategy and adjust accordingly the new organization and terms of reference of each business unit. To remedy the weaknesses already noted by the Central Bank of Tunisia's banking supervision department, the public banks are working on a new version that will be approved by their boards by end-July 2016 (structural benchmark) and address the following concerns:

- **The plan for STB** will fully incorporate revised macroeconomic and financial assumptions. It will take into account the forthcoming capital requirements on operational risk as well as the lifting of forbearance on new NPLs (granted following the 2015 terrorist attacks) and will focus on a proper NPL resolution strategy rather than on an aggressive growth strategy.

- **The plan for BNA** will focus on maintaining an adequate liquidity and solvency levels throughout the restructuring plan, starting with booking a sale of non-strategic assets as soon as possible to ensure it has enough buffers to continue to meet its capital requirements during the entire restructuring period (2016-20). The plan will take into account the forthcoming lifting of forbearance on new NPLs and the recent government decision on the treatment of new loans to agriculture on a commercial basis (the impact of old loans will gradually fade as these get repaid or resolved, helping profitability). The confirmation of government guarantees (callable on first demand) for loans to public entities will help the bank meet regulatory requirements throughout the restructuring period. Sound operational restructuring will help the bank to properly assess, price, monitor and manage credit risk on all loans.

Table 1. Tunisia: Additional Structural Benchmarks

Proposed Structural Benchmarks	Objective	Date
Financial sector reform		
Approval, by the board of Directors of STB and BNA, of revised business plan ensuring regulatory compliance throughout the restructuring period and in line with the principles detailed in the MEFP.	*Financial sector stability*	Jul-16
Approval of secondary legislation to address some of the weaknesses in the banking law regarding the bank resolution framework through the (i) adoption of a government decree to implement the framework of the Bank Deposit Guarantee Fund that includes a least cost-test for resolution with an exception for systemic cases; and (ii) adoption of a bylaw of the Resolution Committee providing a short timeframe to determine resolution measures for systemic cases.	*Financial sector stability*	Aug-16

Sincerely yours,

/s/ /s/

Chedly Ayari
Governor of the Central Bank of Tunisia

Slim Chaker
Minister of Finance

Statement by Jaffar Mojarrad, Executive Director for Tunisia,
Mohammed Daïri, Alternate Executive Director,
Abdelali Jbili, Senior Advisor, and Monia Saadaoui, Advisor
May 20, 2016

We wish to express our Tunisian authorities' deep appreciation for the close engagement with the Fund under the SBA-supported program and the high quality discussions with staff on the proposed new program for which they request Fund support through a four-year Extended Arrangement under the EFF. The authorities also thank Executive Directors and management for their continued support and guidance. Staff analysis and policy recommendations are in line with the authorities' own assessment and policy agenda.

Background and Recent Developments and Outlook

The successful completion of Tunisia's political transition, as reflected in the building of credible and inclusive democratic institutions, was widely recognized at the international level, including through the award of the 2015 Nobel Peace Prize to the Tunisian National Dialogue Quartet for its decisive contribution to this process. Nonetheless, continued weak growth in Europe, and spillovers from the deteriorating security situation in neighboring Libya took a heavy toll on the economy.

Despite these exogenous shocks, the Tunisian authorities persevered with economic reforms under the 2013-15 program to preserve macroeconomic stability and reduce vulnerabilities while supporting growth and job creation, reducing regional inequality, and addressing heightened security challenges. They appreciate staff assessment of the program (Annex 1) and agree that a confluence of adverse factors, including frequent changes in governments, delayed elections, social tensions, and terrorist attacks have hindered policy implementation, especially at the legislative approval stage. They welcome staff recognition that the underlying fiscal stance has improved for most of the program, monetary policy was tightened and the monetary framework strengthened, and progress was made toward greater exchange flexibility. Moreover, growth remained positive, inflation was contained, the external current account deficit remained manageable, reserves continued to be adequate, and pressure on the exchange rate eased. While important steps were undertaken in preparation of major structural reforms, and progress was made in a number of areas as highlighted in the report, the implementation pace fell short of expectations, given the constraints linked to the political transition.

Economic developments in 2015 were marked by the severe shock to growth stemming from the terrorist events, particularly for tourism, remittances, and investment, with social unrest also adversely affecting economic activity and confidence. Offsetting some of these adverse factors were an exceptionally good agriculture production and exports as well as the decline in oil prices, which helped keep growth at 0.8 percent and contained

the deterioration in the external current account. Multilateral disbursements and a bond issue at the beginning of the year helped stabilize gross international reserves at US $ 7.6 billion at end 2015, or the equivalent of more than four months of imports. The authorities' efforts at fiscal consolidation helped bring about a better-than-expected fiscal outcome in terms of primary balance and structural deficit. As shown in Table 4b, current expenditure declined in 2015 compared to 2014 while capital spending was slightly higher. Inflation continued to decline, reaching 3.3 percent at the end of March 2016. However, unemployment remained high, albeit lower than in 2011, and regional inequality persisted.

The authorities are now moving to the next stage of their strategy aimed at deepening reforms in critical areas to strengthen the foundations of growth and job creation, reduce remaining vulnerabilities, and meet pressing social demands. To this end, the government has developed an economic vision and a national program of major reforms that will be further detailed in the 2016-2020 five-year plan to be submitted to the Assembly of the People's Representatives (ARP) in June 2016.

The Economic and Financial Program

As laid out in the economic vision and the MEFP, the authorities' program for 2016-20 is built around a policy mix conducive to macroeconomic and financial stability, and far-reaching structural reforms in many critical areas that would improve the dynamics of inclusive growth, enhance efficiency, foster employment creation, and strengthen resilience of the economy. A good start on the authorities' reform agenda has been the acceleration of legislative approval of key reforms in the banking sector, competition, private public partnership, procurement and public investment, and bankruptcy procedures. Other key reforms of the tax system, investment incentives, civil service, and the business environment are under active preparation.

Early implementation of these reforms, as envisaged, and reduced security concerns and easing of social tensions, along with improved global outlook, are expected to boost growth to 2 percent in 2016 and to about 4-4 ½ during 2017-21. The downward trend in headline inflation is expected to continue, helped by prudent monetary policy. The gradual reduction in the overall fiscal deficit (excluding grants) to 2.4 percent of GDP by 2019 would help reduce public debt to less than 50 percent by 2020. The fiscal consolidation and a rebound of tourism and exports, supported by the expected recovery in Europe, will reduce the current account deficit from an estimated 7.7 percent of GDP in 2016 to around 4 ½ percent of GDP in 2021. Gross international reserves are expected to remain at a comfortable level of close to 5 months of imports.

Fiscal Policy

The 2016 budget sets the stage for fiscal adjustment, even though the pace of fiscal consolidation will be affected by spending on security related to the fight against terrorism. The structural fiscal deficit–adjusted for the economic cycle– is estimated to decline to 4 percent of GDP, or 3.6 percent excluding one-off spending on security. This deficit takes into account the reduction of energy subsidies, the execution of the first measures of the tax reform (reduction of exemptions and rationalization of customs duties), as well as the impact of wage increases. The budget also provides for 16 percent increase in capital spending, which would reach 5 percent of GDP. The authorities are committed to taking additional measures to correct any deviation from the fiscal target while protecting investment and social spending. Over the medium-term, they will continue to improve the composition of public spending toward higher investment and lower wage bill as a ratio to GDP, and better-targeted social spending. This, together with a more equitable and efficient tax system will contribute to the fiscal consolidation objective and help create fiscal space for infrastructure investment, human resource development, social spending, and to deal with contingencies.

The authorities agree with staff assessment that Tunisia's public debt is sustainable under all adverse shocks. With technical assistance from the World Bank, they will finalize a medium-term debt strategy by end-December 2016 allowing for better management and a more appropriate mix between domestic and external borrowing.

Monetary and Exchange Rate Policies

Staff and the authorities agree that the current accommodative monetary policy, following the reduction of the policy rate by 50 basis points in October 2015, is appropriate, given the downward trend in inflation, the existing output gap, and the relatively weak credit growth, and despite the latest wage increases. The Central Bank of Tunisia (CBT) is committed to a prudent monetary policy and remains vigilant to address potential inflationary pressures from delayed second round effects of wage increases or the depreciation of the dinar.

Building on earlier efforts to improve monetary policy transmission, the authorities are moving forward with wide-ranging reforms to strengthen the monetary policy framework and lay the ground work for adopting an inflation targeting framework. The recent adoption of a new central bank law (prior action), confirms price stability as the overriding objective of monetary policy, enhances central bank independence, and sets a lender-of-last resort facility, which will be operational by September 2016 (¶15). The authorities are of the view that government presence in the CBT Board will not impinge on the central bank's independence to carry out its mandate in view of the safeguards included in the new central bank charter. Other steps are under way, with technical

assistance from the Banque de France and the Fund, to streamline money market operations, improve liquidity forecasting, and develop a yield curve. In light of the progress made in strengthening the monetary policy framework, the authorities look forward to availing themselves at an early stage of the option of using a monetary policy consultation clause (MPCC) instead of a performance criterion on the central bank net domestic assets under the program, as allowed for countries with evolving monetary policy regimes.

The authorities remain committed to pursuing a more flexible exchange rate policy to preserve international reserves and facilitate external adjustment. Operational changes introduced recently in the foreign exchange market, including a foreign exchange auction system, will promote competitive bidding and contribute to greater exchange rate flexibility. The CBT has already reduced its market intervention and is committed to limiting it further to the level needed to smooth out excessive exchange rate fluctuations (¶17-18). In parallel, the authorities have taken steps to promote capital mobility and streamline exchange regulations, including removing all caps on foreign borrowing by domestic credit institutions and export-only companies, and eliminating the cap on foreigners' purchases of securities issued by the government or resident companies.

Financial Sector Reform

Progress has been made in fostering a sound banking system, and the authorities are significantly strengthening their efforts in this area. With the recapitalization of three public banks, the solvency ratio of the banking sector was raised from 9.4 percent in December 2014 to 12.2 percent in December 2015, with all banks currently meeting the regulatory minimum capital adequacy ratio of 10 percent, except a small private bank. In addition, following audits of the three public banks, restructuring plans were formulated, with updated versions approved by their respective boards in May 2016 (prior action). Amendments to the plans for two out of the three public banks to address remaining weaknesses already noted by the CBT will be approved by their boards by end-July 2016 (new structural benchmark, see the Supplementary LOI signed on May 17, 2016). However, non-performing loans remain high at 16 percent in December 2015 in connection with the weakening economic activity and the dire situation of the tourism sector, which accounts for 21 percent of NPLs, even though provisioning has improved from 58 percent in December 2014 to 65 percent in December 2015.

To further strengthen the banking system, the authorities' strategy seeks to upgrade the legislative and regulatory framework; strengthen banking supervision; resolve NPLs; complete the restructuring of the three public banks; and over the medium-term, seek technical and strategic partners' participation in public banks by divesting government equity share. On the legislative front, in addition to the recently-approved central bank law, the law on banks and financial institutions (banking law) was approved by the ARP

on May 12, 2016 (prior action). It introduces a banking resolution framework and a deposit guarantee scheme, which will be brought more in line with best international practices following improvements to be adopted by end-August 2016 (new structural benchmark, see Supplementary LOI). A third law on bankruptcy procedures approved in April 2016 (prior action) will remove legal barriers for banks to resolve NPLs, with implementing decrees to be issued by September 30, 2016 (structural benchmark). The authorities will endeavor to ensure proper implementation of the business plans of the three public banks through performance contracts (¶30).

Banking supervision will be further strengthened in line with the 2015-20 action plan with Fund/Bank technical assistance. As detailed in the MEFP, the plan involves among others, overhauling the regulatory framework, improving information on intra-group transactions to carry out supervision on a consolidated basis, developing operational capabilities, and completing intermediate steps for the implementation of an automated reporting system and a scoring mechanism of credit institutions (SYNTEC - Scoring System of Tunisian Credit Institutions). On-site inspections of banks will be increased with Fund TA to cover the seven largest private banks by end-March 2017 (structural benchmark).

The authorities will seek to improve access to credit for SMEs through various measures, including: developing a legal framework for credit bureaus; raising the cap on excessive lending rates; and establishing a Bank of Regions, with technical support from the KfW, to bring lending activities for development purposes under the purview of a single institution.

Structural Reforms

Recognizing the urgent need to accelerate the pace of economic reforms, the authorities have embarked on an ambitious and wide-ranging structural reform program encompassing civil service reform, tax policy and tax administration reform, energy subsidy reform along with improved targeting of social protection, a reform of the pension system, public finance management, including a new organic budget law, and reform of the public investment framework. The reform program also involves an anti-corruption framework with the setting up of a high-level constitutional body to fight corruption and promote good governance. The recently-adopted competition and PPP laws, together with substantial efforts to streamline administrative procedures and reduce red tape, will help improve the business climate. To reduce unemployment, the authorities are focused on addressing skill mismatches through improved education and vocational training and on promoting entrepreneurship. The tax reform strategy was approved in the cabinet on May 9, 2016 (prior action), and the new investment code law, which will establish a level playing field for investors and reduce the dichotomy between on-shore and off-shore taxation while reducing regional disparities, is to be submitted

soon for approval by the ARP. A comprehensive strategy to reform SOEs has been designed with the setting up of a unit within the Ministry of Finance to monitor SOEs and oversee their restructuring.

The authorities will continue the reform of energy subsidies, first through the implementation of a balanced formula of automatic adjustment of prices of petroleum products (gasoline, diesel), and second, through a gradual increase of electricity tariffs to cost-recovery levels with lifeline tariffs to protect the needy. To support the most vulnerable groups of the population, a more effective and better targeted social safety net will be introduced in June 2017, based on a unique social register and a new data base of vulnerable households.

Program Modalities

The authorities believe that the proposed arrangement is appropriate and will provide the needed time frame to support their reform agenda and catalyze international support. They believe that their program is comprehensive and strong, with most of the needed legislation completed as prior actions, and others initiated or under active preparation. While program ownership will be strengthened, including through improved communication, some of the difficult reforms, such as the civil service and the subsidy reforms, will require continued consensus building. Moreover, implementation of the challenging reform agenda (some of which is front loaded) will require adequate technical assistance, including from the Fund.

Conclusion

The authorities are firmly committed to their reform program. While they agree on the downside risks outlined in the report, they wish to highlight the upside risks associated with faster return of confidence as security conditions improve and the democratic process matures, generating greater political and social consensus on needed policies and reforms. They look forward to adequate financial support from the international community and continued close cooperation with the Fund.