Tunisia

Highlights

- **The economic situation has deteriorated and agreement on an International Monetary Fund (IMF) programme has been delayed again.** Growth slowed in 2022 and into the first half of 2023, as fiscal pressures and external vulnerabilities remained high and sovereign ratings continued to worsen.
- **Tunisia entered a long-term partnership with the World Bank to support growth and create jobs.** The new agreement will capitalise on the country's National Development Plan, offering annual financing of US$ 400-500 million (around €380-470 million) over a period of five years.
- **Steps have been taken to improve food security, enhance financial inclusion and liberalise the foreign-exchange rate.** These include an emergency programme to enhance self-sufficiency in the cereal sector, expanded access to electronic payments, the removal of some foreign-currency restrictions and the announcement of plans to replace some subsidies with targeted cash benefits.

Key priorities for 2024

- **Fiscal consolidation is essential to alleviate the pressure on the country's strained public finances.** This will require continued efforts to enhance revenue collection, but also to reduce the large public-sector wage bill, lower subsidies on various products (including fuel) and move towards more targeted support systems.
- **Accelerating the green transition and improving agricultural output are top priorities.** Scaling up renewables, including by promoting private investment and strengthening the regulatory framework, could improve energy resilience. Moreover, enhancing productivity and stability in the grain value chains and addressing climate risks are necessary to mitigate food shortages.
- **Improving the business environment and reforming state-owned enterprises (SOEs) are necessary to promote growth and job creation.** Reducing the state's footprint in the economy and reforming SOEs, including by advancing the new SOE law, strengthening operational efficiency and eliminating foreign-exchange restrictions are essential to boosting overall competitiveness.

Main macroeconomic indicators (per cent)

	2019	2020	2021	2022	2023 proj.
GDP growth	1.6	-8.8	4.3	2.4	1.9
Inflation (average)	6.7	5.6	5.7	8.3	9.4
Government balance/GDP	-3.4	-9.4	-7.7	-7.6	-7.7
Current account balance/GDP	-7.8	-5.9	-6.0	-8.6	-5.8
Net FDI/GDP [neg. sign = inflows]	-1.9	-1.4	-1.1	-1.4	-1.4
External debt/GDP	90.9	94.9	90.6	91.3	n.a.
Gross reserves/GDP	17.8	21.4	18.6	17.0	n.a.
Credit to private sector/GDP	68.6	72.9	69.8	n.a.	n.a.

Macroeconomic developments and policy response

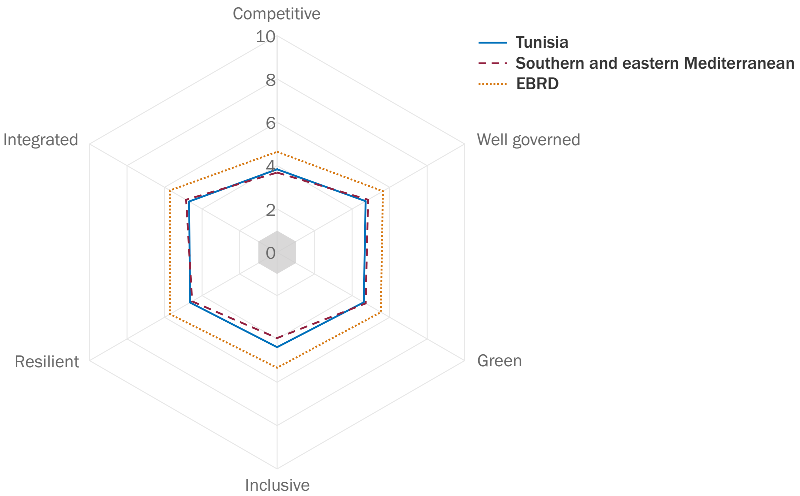
Growth slowed in 2022 and continued to do so into 2023, although the economy showed some resilience to extremely challenging conditions. Gross domestic product (GDP) grew 2.4 per cent in 2022 and just 1.2 per cent year on the year in the first half of 2023. The restrictive business environment, high inflation and social unrest all continued to weigh on economic activity. While the tourism, financial services and industrial sectors expanded, the slowdown in growth was driven by contractions in agriculture (drought impacted agricultural output) and mining (phosphate production dropped). Unemployment declined slightly to 15.6 per cent in the second quarter of 2023, remaining higher among women (21.1 per cent), youth (38.1 per cent) and graduates (23.7 per cent).

Fiscal measures to mitigate the impacts of soaring inflation strained public finances to the limit. Rising commodity prices have severely affected the Tunisian economy, which relies heavily on food and energy imports. Inflation reached 9 per cent year on year in September 2023, slightly below the 30-year high of 10.4 per cent recorded in February. In response to inflationary pressures in 2022 and 2023, the central bank has raised interest rates by a cumulative 175 basis points since May 2022. The government almost doubled subsidies on electricity and basic commodities in 2022, although fuel prices were increased five times in 2022. Minimum wages rose, but the government and unions reached agreement on a longer-term plan to contain the public-sector wage bill (which accounts for over 40 per cent of expenditures). Although tax revenues increased on the back of better tax enforcement, the budget deficit and public debt remained high in 2022, at 7.6 per cent and 80 per cent of GDP, respectively. The fiscal deficit is projected to increase to 7.7 per cent of GDP in 2023 (from an initial budget target of 5.2 per cent), mostly driven by elevated subsidies (due to delayed fiscal reforms and adjustments to the fuel, electricity and gas tariffs) and lower expected tax revenues (on the back of slower economic activity).

External vulnerabilities increased in 2022 and the country was subject to downgrades by ratings agencies, but the situation has stabilised in 2023. The current account deficit increased to 8.6 per cent of GDP in 2022, mostly driven by a widening trade deficit, despite the recovery in tourism and remittances. The current account gap is projected to narrow to 5.8 per cent of GDP in 2023, supported by improvements in tourism, remittances and the trade balance (the latter narrowed by 28 per cent in the first three quarters of 2023). Since March 2022, Moody's Investors Service and the Fitch Ratings agency have downgraded Tunisia's sovereign ratings twice, as the country has experienced pressure in servicing its sizeable external debt. Foreign reserves recovered slightly to US$ 8.4 billion (€8 billion) in October 2023, but cover just 3.8 months of imports.

Domestic and foreign vulnerabilities will continue to weigh on the short-term economic outlook. Growth is forecast at 1.9 per cent in 2023, held back by limited fiscal space, a lack of access to external financing, the restrictive business environment and delays in implementing the structural reforms necessary to empower the private sector. Economic growth should pick up slightly to 2.5 per cent in 2024 if an IMF-supported programme is agreed and reform momentum picks up. Nonetheless, the country's high dependence on tourism, climate risks, reliance on imports and domestic opposition to the necessary reforms will continue to pose major risks to the outlook.

Assessment of transition qualities (1-10)



Structural reform developments

Progress stalled on the IMF-supported programme, blocking other donor support and exacerbating financing constraints. A staff-level agreement (SLA) for a US$ 1.9 billion (around €1.8 billion) IMF Extended Fund Facility was reached in October 2022, but has not yet been signed. The programme would aim to restore external and fiscal stability, lower the public-sector wage bill, review fuel subsidies and tackle inefficiencies in SOEs. The SLA came after the authorities and labour unions reached a milestone agreement on the cornerstones of key reform measures (SOEs and public-sector wage bill). However, amid concerns about the impact on living standards, the government is currently working on a revised reform plan to resubmit to the IMF.

Support from the World Bank and European Union (EU) has been secured. In June 2023 the World Bank announced a new Country Partnership Framework (CPF) 2023-27 to support Tunisia's development plan, by creating quality jobs in the private sector, strengthening human capital, reducing carbon emissions and building resilience to climate change. The programme builds on Tunisia's National Development Plan 2023-25, which aims to boost employment and achieve sustainable and inclusive growth. The government is also planning to strengthen infrastructure for targeted cash transfers (including a digital platform), in line with moving from blanket subsidies to more targeted support schemes. The EU will provide up to €900 million to support the struggling Tunisian economy and an extra €150 million to support the budget, once the IMF programme has been approved. In parallel, the EU will provide support for border management to help the country curb migration.

Progress advanced on the Tunisia-Italy interconnector (ELMED) project. Momentum picked up on implementing the high-voltage direct current interconnector project, with the feasibility study phase completed in 2022 and the procurement phase started in May 2023. The project secured €307 million from the EU in 2022 and US$ 268 million (€254 million) from the World Bank in June 2023 (under the new CPF) to build the necessary infrastructure. Launched in 2019 by the two countries' electricity grid operators, Société Tunisienne de l'Electricité et du Gaz (STEG) and Terna, ELMED aims to link their electricity systems using submarine cables to expand opportunities for the exchange of renewable energy between North Africa and Europe.

Tunisia embarked on a new a programme to improve food security. The Emergency Food Security Support Project in Tunisia (PAUSAT) 2022-26 is designed to enhance food security and self-sufficiency by strengthening resilience to climate and external shocks. The programme is a coordinated effort between development partners, with total financing of US$ 530 million (around €500 million) from the European Bank for Reconstruction and Development, the World Bank, the African Development Bank, the European Investment Bank and the EU. Its key objectives include: (1) increasing cereal production by providing agricultural inputs, (2) providing emergency cereal supplies to avoid shortages and support food security and (3) supporting digitalisation, capacity building and value-chain reforms.

The government is reviewing a new law to gradually liberalise the exchange rate. New regulations are under review to modernise the exchange-rate system and facilitate access to foreign currency. Under the new law, investors and Tunisian firms would be able to open foreign-currency accounts, enabling them to invest, purchase assets and pay any necessary expenses abroad. Moreover, the new law would allow foreign investors to maintain permanent non-resident status, regardless of their duration of stay, enabling them to avoid restrictions applicable to residents. While this is only a first step, the government has reiterated the ultimate objective of gradually reaching full liberalisation of the exchange rate.

The central bank continues to promote financial inclusion by digitising utility payments. With the aim of improving financial inclusion and transparency, the central bank launched a new digital platform in November 2022, allowing citizens to pay their bills online or through mobile applications for no additional fee. The central bank has an overarching objective of promoting financial inclusion by increasing the digitalisation and de-cashing of the economy. The total value of electronic transactions in Tunisia grew by 25 per cent on the year in 2022.