FOR AGENDA

SM/83/100

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May 25, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Tunisia - Staff Report for the 1983 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1983 Article IV consultation with Tunisia. A draft decision appears on page 17.

This subject will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Rothman, ext. 73393.

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INTERNATIONAL MONETARY FUND

TUNISIA

Staff Report for the 1983 Article IV Consultation

Prepared by the Staff Representatives for the 1983 Article IV Consultation with Tunisia

Reviewed by the Committee on Article IV Consultations

Approved by Oumar B. Makalou and S. Kanesa-Thasan

May 24, 1983

I. Introduction

The 1983 Article IV consultation discussions with Tunisia were held in Tunis during the period March 8-22, 1983. The Tunisian representatives included Messrs. M. Moalla, Minister of Planning and Finance; M. Belkhodja, Governor of the Central Bank; A. Lasram, Minister of the National Economy; L. Ben Osman, Minister of Agriculture; and other senior officials of ministries and agencies concerned with economic and financial matters. The staff representatives were Messrs. C.A. François (head), S. Rothman, R. Franco, E. Sacerdoti, and Ms. C. Elwell (secretary), all of the African Department.

Tunisia continues to avail itself of the transitional arrangements under Article XIV.

II. Economic and Financial Developments in 1982 and Prospects for 1983

1. Developments in 1982

During the decade ending 1981 Tunisia recorded relatively rapid real economic growth and made considerable progress toward industrialization while maintaining domestic financial stability and a strong balance of payments position. These developments reflected a vigorous investment effort made possible by a sharp improvement in the terms of trade, due mainly to the increase in petroleum prices, and by financial policies which ensured a high rate of domestic savings. It reflected also improved economic management, including a gradual shift away from centralized government control. However, as noted in the appraisal in the staff report for the 1982 Article IV consultation (SM/82/98; May 20, 1982), the prospects for 1982 appeared less favorable. In particular, concern was expressed by the staff that a rapid increase in consumption would result from substantial wage increases granted in February 1982 and that export receipts from petroleum would be lower, with the result that there would be both a widening of the resource gap and an acceleration in the inflation rate.

In the event, the economic and financial outturn for 1982 was one of broad deterioration. Due to a drought-induced decline in agricultural output and agro-based industrial production, and slackened hydrocarbon and phosphate production associated with weakened external demand conditions, growth in real gross domestic product (GDP) was only 1 per cent, compared with an annual average rate of over 6 per cent during the previous five-year period (Table 1). Concurrently, stemming in large measure from the sizable increases in wages (the minimum wage was raised by 32 per cent), the wage bill in the economy is officially estimated to have increased by 28 per cent--twice the rate of growth in nominal GDP--and the increase in private consumption is estimated at almost 17 per cent.

As a result of the rapid increases in both private and public consumption, the ratio of national savings to GNP declined from 23 per cent in 1981 to 20 per cent in 1982. On the other hand, the investment ratio declined by only 2 percentage points to 30 per cent of GNP, and the resultant larger financing needs were covered by an accommodative credit policy, and, for the first time since 1978, by a drawing (US$30 million) from a substantial loan (US$125 million) from the international financial market.

In the fiscal area, despite a substantial increase in revenues (24 per cent) associated in large part with new taxes on imports and higher receipts from petroleum production (including a carryover from 1981), 1/ the consolidated fiscal deficit 2/ doubled as a percentage of GDP to 5.2 per cent, as expenditure growth accelerated to 32 per cent, attributable principally to an increase of 30 per cent in the wage bill, as a result of the sharp increase in pay scales, and to a rise of 59 per cent in outlays for goods and other services following declines in the previous two years. Current outlays rose by 38 per cent and capital expenditures by 21 per cent. Moreover, the net income of the major public enterprises declined by 2 per cent, to the equivalent of 2.5 per cent of GDP, while their level of investment remained high (equivalent to 6 per cent of GDP).

The rate of expansion in domestic credit in 1982 was 23 per cent, with credit to the economy (the private and nongovernment public sectors) rising by 24 per cent; fully 40 per cent of the deposit money banks' expansion of credit to the economy was financed by recourse to the Central Bank. The increase in credit to the Government was equivalent to 3 per cent of money plus quasi-money at end-1981. Money plus quasi-money rose by 19 per cent, well above the rate of increase in nominal GDP (14 per cent). Reflecting excessive domestic demand pressures and also some price liberalization and increases in the administered prices of a number of essential commodities consumer price inflation accelerated to almost 13 per cent (compared with 10 per cent in 1981).

The current account deficit in the balance of payments widened significantly (by 34 per cent) in 1982 to SDR 556 million, or 7.8 per cent of GNP, from SDR 414 million, or 5.9 per cent of GNP, in 1981. Export receipts

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1/ Consisting of profits of the Tunisian Petroleum Company, royalty payments, and complementary surtax payments.

2/ This is the first time that the fiscal data for Tunisia are being presented on a consolidated basis, including all operations in the Treasury accounts, extrabudgetary investment financed by external assistance, and the operations of the social security schemes.

Table 1. Tunisia: Selected Economic and Financial Indicators, 1977-83

	1977-81	1980	1981	1982 Prelim.	1983 Forecast
		(Annual per cent changes)			
National income and prices					
GDP at constant prices	6.1	4.3	5.0	1.0	6.0
GDP deflator	9.5	14.7	10.9	13.2	9.4
Consumer prices	7.8	10.0	9.9	12.6	11.0
External sector (in SDRs)					
Exports, f.o.b.	21.4	18.6	29.1	-13.7	1.9
Imports, f.o.b.	16.7	13.9	21.8	-2.5	5.9
Terms of trade (deterioration -)	-3.0	14.3	6.2	-0.7	-10.6
Nominal effective exchange rate (depreciation -)	-3.0	1.0	0.8	-4.4	-1.2 1/
Real effective exchange rate (depreciation -)	-16.8	-1.9	-2.2	-1.8	1.3 1/
Central government operations 2/					
Revenue and grants	19.2	18.8	18.0	23.9	10.9
Total expenditures and net lending	18.6	12.7	17.1	31.6	15.7
Money and credit					
Domestic credit	17.4	17.6	24.3	23.4	19.6
Government	(15.6)	(1.9)	(16.4)	(20.4)	(27.4)
Economy	(17.8)	(20.6)	(25.6)	(23.8)	(18.5)
Money plus quasi-money	17.5	18.5	19.3	18.9	14.8
Interest rates					
(discount rate)	6.00	5.75	7.00	7.00	7.00 1/
(12-18 month time deposit)	4.88	5.25	7.00	7.00	7.00 1/
(general rediscountable advances)	7.45	7.0-7.5	8.0-2.5	8.0-8.5	8.0-8.5 1/
			(Ratios)		
Central government savings 2//GDP	8.8	9.3	10.3	8.4	6.7
Central government deficit 2//GDP	3.8	2.8	2.6	5.2	6.6
Domestic financing/Total financing	13.8	18.7	-3.0	54.6	50.7
Foreign financing/Total financing	86.2	81.3	103.0	45.4	49.3
Gross capital formation/GNP	30.2	28.8	31.9	29.8	29.4
Gross national savings/GNP	22.3	23.5	23.0	19.9	20.2
External current account deficit/GNP	7.6	5.1	5.9	7.8	8.6
External debt/GDP	38.8	35.3	36.1	40.4	39.8
Debt service/Exports of goods and non-factor services plus private transfers	11.0	12.1	13.6	16.8	17.0
Overall balance of payments (millions of SDRs)	146	63	83	25	-30
Gross official reserves (months of imports)	2.0	2.5	2.1	2.5	2.0

Sources: Data provided by the Tunisian authorities; and staff calculations.
1/ March.
2/ Consolidated basis.

declined by 14 per cent (in terms of SDRs) because of both lower hydrocarbon exports (29 per cent), resulting from reduced production and increased substitution of domestic crude petroleum for imported crude in domestic consumption, and a decline in agricultural exports (19 per cent). Imports (in SDR terms) fell by 2.5 per cent, with lower hydrocarbon imports and reduced outlays for foodstuffs, reflecting a fall in world market prices, the major contributing factors. Net exports of hydrocarbons were stable. The deterioration in the trade balance (SDR 178 million) was only partially offset by a larger surplus on account of services and transfers stemming from a sharp increase in workers' remittances and a modest rise in tourism receipts. However, net capital inflows increased sharply, from SDR 491 million in 1981 to SDR 581 million in 1982, leading to a small overall balance of payments surplus (SDR 25 million, compared with SDR 83 million in 1981). The improvement in the capital account resulted from an inflow of short-term capital, in contrast with an outflow in 1981, apparently associated with leads and lags in trade payments. Direct investment from abroad remained close to the high level reached in 1981, and medium- and long-term borrowing by enterprises and Government declined moderately. Tunisia's external public debt (expressed in SDRs), after remaining broadly stable between 1979 and 1981, rose by 13 per cent in 1982 to SDR 2.8 billion (40.4 per cent of GDP), partly due to the effects of the appreciation of the U.S. dollar vis-à-vis the SDR on dollar-denominated debt. The debt service ratio increased from 13.6 per cent in 1981 to 16.8 per cent in 1982.

The exchange rate of the Tunisian dinar 1/ is determined on the basis of a basket of currencies containing the U.S. dollar, the French franc, the deutsche mark, and the Italian lira. The nominal effective exchange rate depreciated by 4.4 per cent during 1982 and by an additional 1.2 per cent during the first three months of 1983, reflecting the sharp appreciation of the U.S. dollar relative to the major European currencies and some discretionary action (Chart 1). The real effective exchange rate, adjusted for relative price movements, depreciated by 2 per cent on an average annual basis during 1982. However, domestic prices are influenced to a substantial degree by price controls and subsidies, and, adjusted for relative labor costs, the effective rate of the dinar appreciated during 1982 by 7 per cent. Vis-à-vis the SDR, the dinar depreciated by 18 per cent between end-1981 and end-March 1983.

Tunisia maintains a relatively complex exchange and trade system, which is described in detail in the 1983 Report on Exchange Arrangements and Exchange Restrictions. The sale of foreign exchange continues to be limited for most invisibles, and payments for nonliberalized imports require prior authorization. Also, trade restrictions arise from the licensing of imports that have not been liberalized. However, over the past few years there has been a de facto relaxation of trade restrictions, due largely to an extension of the system of annual import authorizations, originally confined to industrial companies, to large trading firms and specialized retailers. Also, there has been an easing of payments restrictions and procedures on invisibles, including travel allowances, and, especially in 1982, the allowance for study abroad.

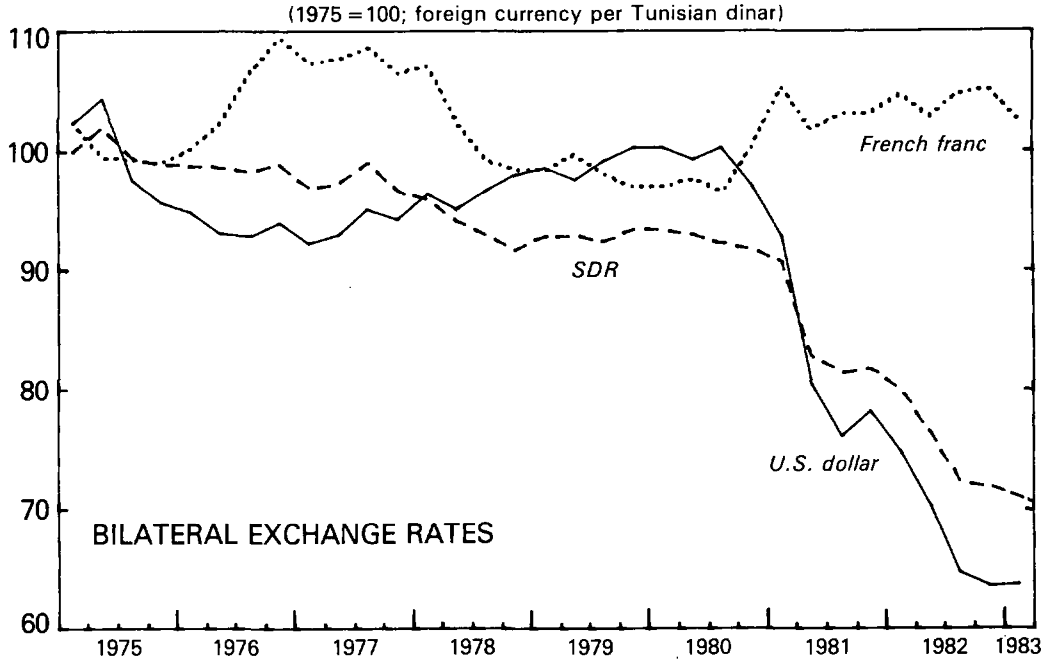
1/ D 1 = SDR 1.413 (March 31, 1983).

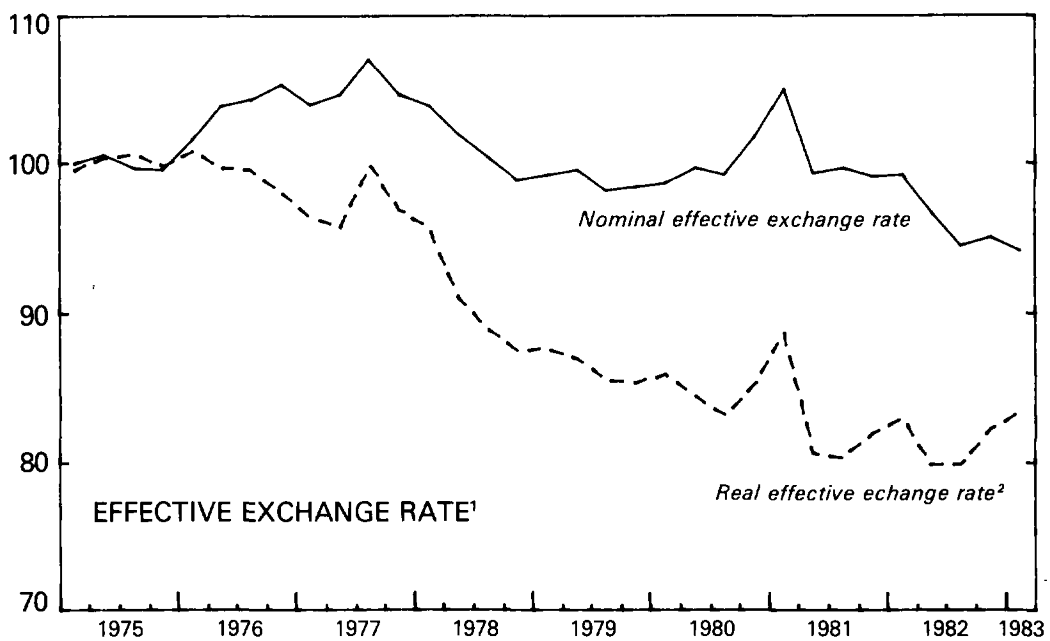
CHART 1

TUNISIA

INDICES OF SELECTED EXCHANGE RATES, 1975-83

(1975 = 100; foreign currency per Tunisian dinar)





Source: IMF Data Fund.

[1] *Weighted by the geographical distribution of trade, tourism receipts, and workers' remittances.*

[2] Effective exchange rate deflated by the consumer price index relative to partner countries.

The bulk of Tunisia's external debt is effected by the Government and other public sector institutions, and the contracting of such debt is closely controlled by both the Ministry of Planning and Finance and the the Central Bank.

2. Prospects for 1983

The economic and financial prospects for 1983 appeared mixed at the time of the discussions, with a more favorable outlook indicated for economic growth but further deterioration foreseen for both the domestic financial situation and the external accounts. Growth in real GDP is now projected at 6 per cent, due mainly to a forecast recovery in the agricultural sector based on adequate rainfall during the critical planting period. The rate of increase in the consumer price index is forecast to decline to about 11 per cent on an average annual basis, and to decelerate to 8 per cent on a December-December basis. However, this moderation would be achieved in part through a tightening of price controls. The growth in nominal GDP is forecast to be 16 per cent.

Regarding public finances, pronounced decelerations in the rates of growth are projected for both revenues and expenditures. However, with receipts still increasing at a much lower rate (11 per cent) than outlays (16 per cent), the consolidated fiscal deficit is forecast to widen further to 6.6 per cent of GDP. The projected deficit is to be financed almost equally from domestic and external sources. The monetary authorities are projecting a lower rate of monetary expansion (15 per cent), with growth of both credit to the economy (18.5 per cent) and total domestic credit (20 per cent) expected to be somewhat more moderate than in 1982.

The current account deficit of the balance of payments is presently projected to widen further to SDR 684 million, or 8.6 per cent of GNP, as a result of stagnation in agricultural exports at their low 1982 level due to delayed effects of the drought, the decline in world prices for petroleum, and general weakness in the international prices for chemicals. Exports are projected to increase by only 2 per cent, compared with growth of 6 per cent forecast for imports. The larger current account deficit will be covered mainly by direct investment and medium- and long-term official borrowing and to a lesser extent by further recourse to the international financial market, and the debt service ratio for 1983 is projected at 17 per cent. This financing is not expected to cause any debt service difficulties in the future. A modest overall balance of payments deficit (SDR 30 million) is projected. Although in part associated with seasonal factors, during the first three months of 1983 gross official international reserves declined by 24 per cent (SDR 132 million) to a level equivalent to 1.7 months of projected 1983 imports (on a c.i.f. basis).

III. Medium-Term Objectives and Strategy

In recognition principally of an anticipated decline in net petroleum exports, due to both a rapid rise in domestic demand for energy and the gradual exhaustion of Tunisia's petroleum reserves, and a forecast deterioration in Tunisia's terms of trade, the Tunisian Government has embarked on a major restructuring effort within the context of the Sixth Development Plan (1982-86). The plan is designed to reduce the economy's reliance on petroleum, 1/ and the strategy is primarily one of raising agricultural production, increasing employment, and diversifying the export base, while adapting to tighter resource constraints by moderating the growth in both consumption and investment. The main structural reorientations include changing the sectoral pattern of investment toward labor-intensive activities, agriculture, export-oriented industries, and tourism, with an increased role accorded the private sector; encouraging a better choice of production techniques and products through appropriate product and factor prices as well as exchange rate policies and a rationalization of the tariff structure; and reforming the state enterprises. With respect to demand management, the plan seeks to maintain relatively rapid real growth in GDP despite a lower investment rate (26 per cent of GDP, compared with 30 per cent under the Fifth Plan), while strengthening efforts to promote both public and private savings. For the budget, this would entail, among other things, containing the growth in the wage bill and expanding the tax base. To moderate the growth in private consumption, in addition to tax measures and more appropriate incomes policies, the plan calls for a number of other actions to encourage private savings, including new savings schemes and more remunerative interest rates.

The Sixth Plan's main quantitative objectives for the 1982-86 period are to maintain an annual real growth rate of 6 per cent, while reducing the external current account deficit as a share of GNP (for the five-year period) by 0.5 percentage point, compared with the outturn under the previous plan (7.6 per cent). Taking into account the projected inflow of direct investment (about 3 per cent of GDP) and the terms and conditions of prospective borrowing, deficits on this scale would be consistent with the maintenance of both the external debt/GDP and debt service ratios at moderate and sustainable levels.

The mission examined in a preliminary manner the feasibility of the plan targets in view of the shortfalls in 1982 and the generally less favorable prospects for 1983-86 than assumed in the plan, mainly for agricultural production and the world market price for petroleum. Although a number of uncertainties remain, it appears that the initial growth and external current account targets for the 1982-86 period will not be attained. For economic growth, the mission forecasts an average annual rate of 5 per cent; even so, for the external current account, as discussed below, the mission projects a higher average annual deficit of about 8 per cent of GNP, which in its judgement calls for the prompt implementation of corrective measures.

1/ For example, in 1982 exports of petroleum accounted for 45 per cent of total exports, while receipts from petroleum production accounted for 20 per cent of consolidated government revenues.

The mission's policy discussions took account of the changed domestic and external circumstances and focused on measures to promote satisfactory economic and financial performance through 1986, including importantly actions to be initiated quickly to stem the deterioration in the domestic financial situation and external accounts forecast for 1983.

IV. Report on the Discussions

1. Production, employment, incomes, and price policies

Given the importance of agriculture for Tunisia's medium-term growth and balance of payments prospects, the discussions on production policy focused on this sector. In the Sixth Plan the share of agricultural investment in total investment is planned to increase to 19 per cent, compared with 12 per cent in the Fifth Plan. The Tunisian authorities said that in addition to increased investment, various instruments were being used to promote agricultural production. Producer prices had been steadily increased since 1980 and would continue to be adjusted. In December 1982 producer prices for cereals were increased by 15-26 per cent, and further increases were possible in 1983. Also, in 1982 the prices for meat and milk had been completely liberalized, and the higher prices for meat had encouraged a significant increase in output. In addition, an agricultural investment code had been approved to provide incentives for agricultural projects similar to those given to industry, and an agency was set up to promote investments in agriculture.

The Tunisian representatives stated that considerable efforts were now being directed in the agricultural sector to expanding extension services, improving marketing facilities, and setting up storage facilities. In 1983 an institution has been established to purchase and store commodities during harvest periods (when prices are low) and to sell them in the offseason (when prices are high). To finance this price stabilization effort, a one per cent tax has been levied on both agricultural imports and the sale of farm commodities.

Increased attention was also being given to the credit needs of the agricultural sector. A national agricultural bank was being established to extend credit to large farmers. The lending rates contemplated would be in the range of 8-10 per cent, compared with 6 per cent charged by the agency responsible for lending to small farmers. The latter were being encouraged by the Government to form marketing cooperatives. Interest rates for agriculture were low compared with those for other sectors, but the authorities believed that this was warranted at this stage of development. However, they also said that the rates for agriculture would rise over the medium term to reach parity with those in other sectors, but that the convergence should be gradual.

Market prospects in the medium term for Tunisian agricultural exports were fairly encouraging, although concern was expressed that rapid increases in domestic demand could absorb an important share of potential exportables. The rapid increase in incomes over the past decade had created a sharp increase in the demand for fruit and vegetables. Regarding specific commodities, prospects for oranges and dates were favorable, and the outlook for fish exports was excellent. Despite heavy pressure from domestic demand, all exports of agricultural products were free of restrictions with the exception of fish exports, which were subject to a licensing system. For tomatoes and other early vegetables, there were also good prospects, as exports to the EC countries before May 15 each year were free of restrictions. Despite the efforts being devoted to increasing agricultural production and the favorable export market prospects, it was recognized by the Tunisian representatives that, in view of the decline in output in 1982 and likely delays in increases for some commodities in 1983 due to the drought, the plan target of 5 per cent annual growth in the sector for the period 1982-86 would be difficult to attain. However, to help compensate for the shortfalls in 1982-83, the authorities indicated that the pace of reform would be quickened.

In order to generate more rapid increases in employment, attempts were being made to encourage labor-intensive industries, mainly through tax incentives. To improve its regional distribution, the Government was providing regionally differentiated bonuses. The mission noted that, to shift away from capital-intensive production techniques, there would have to be a substantial change in the relative cost of capital and labor, which thus far has certainly favored the use of the former.

In view of a probable official downward revision for real GDP growth for the period 1982-86, the Tunisian representatives said that this would also require a lower target for consumption growth so as to not unduly hamper the investment effort. To achieve a moderation in private consumption, the authorities were aiming primarily at containing the expansion in the economy-wide wage bill, but were also intent on restraining other incomes. The Tunisian representatives stressed that the large pay awards granted in 1982 reflected the preoccupation of the Government with labor tranquility, following a prolonged period of social unrest. Under wage negotiations in progress at the time of the mission, it was the Government's intention to limit the increase in the wage bill in 1983 to 16 per cent--the rate of increase projected for nominal GDP--with the minimum wage rising by 12 per cent. The mission stated that a marked deceleration in the growth of wages and salaries was required not only to moderate the growth in consumption but also to bring wage increases more in line with productivity trends. This was essential for achieving the plan's objectives of diversifying and achieving a high rate of growth of exports and of promoting labor-intensive production. Also, as additional measures to curb the growth in consumption, the authorities intend, as discussed below, to issue government bonds with attractive yields and possibly to revise upward the entire structure of deposit rates.

Following the acceleration of domestic inflation during the course of 1982 and in an attempt to moderate the wage demands of labor unions in 1983, in late 1982 the Government imposed a temporary freeze on administered prices and tightened controls on other prices. The Tunisian representatives stated that they were aware that such controls created distortions and led to a nonefficient allocation of resources. However, the current halt in the price liberalization process was only temporary and was considered a necessary trade-off in order to obtain a much lower increase in wage and salary scales than in the past few years. They remained strongly committed to reducing consumer subsidies by raising administered prices.

2. Financial policies

a. Fiscal policies

The discussions on fiscal policies centered on the need to curb the rapidly increasing consolidated deficit. The Tunisian representatives stated that, as far as revenues were concerned for 1983, at this stage, apart from possibly collecting some taxes due from earlier years, not much in additional receipts could be expected. Due to the decline in world market prices for petroleum, revenues from petroleum production had recently been revised downward further, bringing the projected decline from the 1982 level to 10 per cent, equivalent to 2 per cent of total revenues in 1982. Moreover, due largely to the implementation of the first phase of the tax reform, in which, for example, income tax rates for self-employed individuals were reduced in anticipation of increasing the tax base over time, it was projected that taxes on net income and profits would increase by only about 4.5 per cent in 1983, compared with an increase of 19 per cent in 1982. On the expenditure side, the Tunisian representatives pointed out that the increase in outlays for wages and salaries would decelerate markedly in 1983, with most recent projections showing an increase of 15 per cent, compared with the 30 per cent rise in 1982. In addition, capital expenditures would rise by about 12 per cent, compared with an increase of 21 per cent in 1982. Nevertheless, the consolidated deficit would increase from D 241 million (5.2 per cent of GDP) in 1982 to D 358 million (6.6 per cent of GDP) in 1983. Moreover, despite a considerably higher level of domestic financing, with increases from both bank and nonbank sources (including importantly the sale of bonds to the national savings bank and increased deposits of nongovernment public sector institutions with the Treasury), another loan on the international financial market would likely be required during the latter part of the year.

The mission noted that, although it appreciated the built-in rigidities, perhaps some scope still existed to contain expenditure further in 1983. In particular, it suggested postponing some capital expenditures, stretching out the pace of new recruitment, and reducing subsidies and transfers to both public enterprises and consumers. Such subsidies and transfers 1/ are expected to rise by 18 per cent to the equivalent of

1/ Comprising consumer subsidies, transfers to households, and current and capital transfers to public enterprises.

about 26 per cent of total expenditure and 11 per cent of GDP. The Tunisian authorities agreed that subsidy and transfer outlays at their current levels were not sustainable indefinitely. Subsidies for wheat were particularly large (about D 100 million in 1983). However, since wheat products had a large weight in the consumer price index, movements in which affected labor union wage demands, caution had to be exercised in increasing their prices. Nevertheless, the authorities recognized the need for higher prices of subsidized goods and services and intended to increase some administered prices during the second half of 1983.

Concerning the medium term the Tunisian representatives were somewhat more optimistic that offsets to declining export-based petroleum revenues might be forthcoming. They believed that, as the tax reform progressed, with further modifications of income tax rates and the continued phased implementation of a comprehensive value-added tax (which, in principle, was expected to cover most sectors by 1986), and the tax administration was strengthened, the tax base would expand. Also, it was anticipated that declining petroleum revenues from exports would be compensated for by higher petroleum receipts related to domestic consumption, as the subsidy on domestic consumption was gradually eliminated. After examining the revenue outlook through 1986, the mission concluded that a modest increase in the ratio of nonpetroleum revenues to GDP would not compensate for the projected diminished importance of petroleum receipts and that the overall revenue/GDP ratio would decline. The Tunisian authorities, however, were very reluctant to raise tax rates, as they considered that the fiscal burden in Tunisia was already quite high; in 1982 total revenues were equivalent to 35 per cent of GDP. Therefore, the mission suggested that, to stabilize the fiscal deficit in the near future, most of the adjustment would have to be borne by expenditure policies, with an emphasis on continued restraint in wage outlays and capital spending and reductions in subsidies and transfers. The mission pointed out that, in addition to reducing subsidies and transfers to consumers (equivalent to 17 per cent of expenditure in 1983), it would be desirable to curb current and capital transfers to Tunisia's vast system of nonfinancial public enterprises, which are projected to amount to almost 10 per cent of consolidated outlays in 1983. The Tunisian authorities aimed at sharply curtailing outlays on consumer subsidies in the medium term, but said that the population first had to be convinced of the necessity of paying "reasonable" prices for essential goods and services. Concerning outlays on public enterprises, the authorities were hopeful that in the near future the enterprises would improve their financial position and thus be less of a burden on the Government. In this regard, the increased participation of the new development banks would certainly be positive, as they were expected to provide an increased share of public enterprise capital financing. Moreover, in conjunction with the Sixth Plan, an extensive effort was being made to improve the monitoring of the activities of public enterprises to help increase their financial viability. In addition, there has been a start in identifying a limited number of enterprises which should remain under direct government control.

b. Monetary and credit policies

The Tunisian monetary authorities were aware that continued rapid monetary growth was not conducive to financial stability and thus were aiming for a somewhat lower rate of increase in broad money for 1983 (15 per cent), compared with the outturn for 1982 (19 per cent). The projected deceleration in the growth of banking system credit to the economy was based largely on an anticipated decline in lending for stockbuilding and possibly increased self-financing of enterprises. On the other hand, the development banks (which are not included in the monetary survey) would likely be more active in 1983. The development banks' long-term lending and equity participations were forecast to increase by D 183 million, equivalent to 9 per cent of broad money at end-1982. The mission noted that the projected increase in banking system credit to the economy (18.5 per cent) was still in excess of the projected rise in nominal GDP and that, if the development banks lent as currently anticipated and the Government borrowed more than presently projected (the equivalent of 4 per cent of money plus quasi-money at end-1982), there could be another excessive increase in liquidity, which would put additional strains on both domestic prices and the balance of payments. In response, the Tunisian authorities considered the projected increase in banking system credit to the economy as the "noncompressible" minimum in view of the anticipated pickup in economic activity. In addition, they were not too concerned with the possible impact of development bank lending on domestic liquidity expansion, as such lending would increase productive capacity. They did note, however, that it would be important for the Government to meet any unanticipated financing requirements from nonbank sources so as to limit domestic credit expansion.

Concerning interest rates, based on the projected increase in consumer prices for 1983, both the real rate of return to depositors and the real cost to borrowers were negative (e.g., -4 per cent on one-year time deposits and -3 per cent for commercial bank short- and medium-term rediscountable loans), although the negative margins may decline through 1983. To mobilize private savings, additional savings schemes would be established during the course of the year. Also, the authorities were considering issuing "zero coupon" government bonds, which would yield annual rates of up to 10.4 per cent (for a bond with a seven-year maturity). Thus far there had not been a decision on whether the issues would be made on an "obligatory" or "voluntary" purchase basis. The mission stated that the proposed issues appeared to carry more appropriate yields than other savings instruments but that they should preferably be offered on a voluntary basis. Moreover, to prevent merely a switching on the part of the public from one form of savings to another, there should be a harmonization of rates among institutions and instruments, which, in present circumstances, would generally imply an upward revision in deposit rates. The Tunisian authorities concurred with this position and stated that at the time of the new government bond issues, the whole structure of deposit rate would be reviewed, with the possibility of making some upward adjustments.

3. External sector prospects and policies

For 1983, in view of the less-than-favorable prospects for exports, the Tunisian authorities expressed their intention to limit the current account deficit by directly containing imports through a tightening of the import licensing system. In particular, they would attempt to limit the current account deficit to SDR 625 million (7.8 per cent of GNP, comparable to the ratio in 1982), instead of the projected deficit of SDR 684 million (8.6 per cent of GNP), by carefully examining requests for imports, especially of intermediate and nonessential consumer goods. Annual import authorizations for industrial purposes were being limited, in a first stage, to 80 per cent of the 1982 level, while the import program for wholesalers and retailers was being limited to last year's total. Moreover, the authorities were considering a more limited granting of licenses for imports of nonessential consumer goods. The mission stressed that such measures were not satisfactory substitutes for curbing global and thus import demand by restraining wage increases, the fiscal deficit, and credit growth and by the application of a more flexible exchange rate policy, and that such measures would likely be counterproductive. They stated the Tunisian economy was already hampered by a relatively complex system of foreign trade restrictions, and that a further tightening of the system could only have negative effects on production and exports in the medium term. In response, the Tunisian authorities stated that they would remain flexible with respect to authorizations for imports of industrial inputs and capital goods depending upon developments in the balance of payments.

Regarding medium-term prospects, based on the assumption of successful export diversification efforts and a conservative assumption regarding the world price for petroleum (US$29 per barrel), the mission's projections indicated an average annual rate of growth of exports of 10.6 per cent (in terms of SDRs) over the period 1983-86 (Table 2). The principal contributors to this growth are expected to be textile, agricultural, mechanical, and chemical products (mainly phosphate derivatives) in line with increases in productive capacity. Together, these products would account for about 80 per cent of the projected increase in exports. Over the same period, based on the assumption mainly of a curbing of the growth in consumption (to about 5 per cent per annum in real terms) compared with that in recent years (about 6.5 per cent per annum), imports are forecast to increase at a comparable rate (10.4 per cent per annum). Major savings are expected in imports of agricultural products and equipment goods, reflecting higher domestic production. In addition, a slower growth in petroleum imports is expected to result from a more moderate increase in consumption, due to additional domestic price increases and other conservation measures, including the substitution of domestically produced gas for imported petroleum. Net exports of hydrocarbons over the 1983-86 period are projected to remain broadly stable at about SDR 330 million. Net transfers are forecast to increase by 9 per cent per annum over the 1983-86 period as a result mainly of an increase in tourism receipts. Overall, the

Table 2. Tunisia: Balance of Payments and External Debt, 1981-86

(In millions of SDRs)

	1981	1982	1983	1984	1985	1986
	Actual		Projections			
Balance of payments						
Exports, f.o.b.	1,789	1,544	1,573	1,759	2,044	2,313
Imports, f.o.b.	-2,696	-2,629	-2,784	-3,156	-3,500	-3,900
Services and transfers (net)	493	529	527	603	665	747
Current account deficit	-414	-556	-684	-794	-791	-840
(In per cent of GNP)	5.9	7.8	8.6	8.9	7.7	7.2
Grants	17	28	19	19	19	19
Direct and portfolio investment	313	293	282	295	295	295
Medium- and long-term loans (net)	237	195	353	525	522	571
Disbursements						
Official creditors	276	292	309	407	466	492
Private creditors	240	261	404	493	460	520
Amortization	279	358	360	375	404	441
Short-term capital	-76	65	--	--	--	--
Capital account	491	581	654	838	835	884
SDR allocation	6	--	--	--	--	--
Overall balance	83	25	-30	44	44	44
Debt service						
Total service payments	460	526	538	588	669	772
Principal	280	342	346	375	404	441
Interest	180	184	192	213	265	331
Debt service ratio 1/	13.6	16.8	17.0	16.5	16.3	16.7
External debt (disbursed)						
Amount outstanding	2,457	2,775	3,125	3,650	4,172	4,742
In per cent of GDP	36.1	40.4	39.8	41.3	40.7	40.8
Memorandum item						
Exports of goods and services, and private transfers	3,378	3,137	3,162	3,574	4,096	4,632

Sources: Data provided by the Tunisian authorities; and staff projections.

1/ In per cent of exports of goods and services, and private transfers.

mission's projections indicate a current account deficit, which, after rising in 1983-84 to almost 9 per cent of GNP, would decline over the two years 1985-86 to 7.2 per cent of GNP. The mission noted that even though the authorities could probably finance such current account deficits through 1986 without a significant increase in the projected debt service ratio up to 1986, the indicated shift in the composition of financing toward commercial borrowing was somewhat worrisome, as it implied possibly a higher debt service ratio beyond 1986. Moreover, current account deficits on such a scale beyond 1986 would suggest levels of commercial borrowing and a significant increase in the debt service burden both of which would likely not be sustainable over time. Therefore, the mission stressed that the Tunisian authorities aim to contain the current account deficit in 1986 to a level below that presently projected and stressed that this would require an early and rigorous implementation of a stronger adjustment effort than assumed in the balance of payments projections.

The Tunisian authorities shared the mission's concerns and noted, additionally, that any significant excess over the Sixth Plan's target for 1986 (6 per cent of GNP) might actually reduce their borrowing potential in the ensuing plan period. In this context, they would undertake shortly a full-scale review of the plan targets and would adopt appropriate measures to help ensure that the deviation from the plan's current account target for 1986 be kept to a minimum.

The Tunisian authorities stated that over the past two years exchange rate policy had been conducted with the aim of maintaining an adequate margin of competitiveness for the Tunisian economy and that they intended to continue the same policy stance in the period ahead. The mission emphasized the need to use the exchange rate as an efficient instrument to facilitate export promotion, stimulate domestic production, and curb import growth. It pointed out that the rapid increase in wages and labor costs over the past few years has narrowed Tunisia's margin of competitiveness and it was important that the authorities monitor the level of the effective exchange rate on an appropriate and continuous basis. In response, while agreeing with the mission's view, the authorities expressed interest in obtaining Fund technical assistance to establish an indicator of the effective exchange rate on a multilateral basis so as to take account not only of the trade between Tunisia and its partner countries but also the degree of competition provided to Tunisian exports by third countries. It was agreed that in the coming months the Fund staff would establish a multilateral exchange rate model to aid the authorities in carrying out their exchange rate policy. Also, during the discussions the Tunisian authorities stated that they would prefer that the Tunisian dinar continue to be pegged to a basket of currencies, although over the last 12 months the deviations of the dinar from the calculations based on the present currency basket exceeded the permissible margin of 2.25 per cent because strict adherence to the basket would have led to an excessive appreciation vis-à-vis the French franc. Accordingly, the Central Bank intends to revise the composition of the basket very shortly and to adjust it more frequently.

V. Staff Appraisal

In recent years Tunisia has recorded relatively rapid economic growth and made considerable progress toward industrialization while maintaining both domestic financial stability and a strong balance of payments position. Although benefiting from substantial gains in the terms of trade and the growth of oil exports, Tunisia's progress has reflected also economic and financial policies which have ensured a high level of investment and domestic savings as well as generally improved economic management. However, in 1982 Tunisia's economic and financial outturn deteriorated. Exogenous factors such as drought and slackened external demand depressed real economic growth, while highly expansionary fiscal, monetary, and incomes policies generated excessive domestic demand pressures. The cumulative effects of these developments were an acceleration of inflation and a marked widening of the external current account deficit. Notwithstanding the less favorable environment in 1982, the authorities made efforts to promote a restructuring of the economy within the context of the Sixth Development Plan. Thus, agricultural producer prices were raised significantly, there was some limited progress in the liberalization of retail prices, important new development banks began operations, and the authorities' exchange rate policy resulted in some depreciation in the effective rate.

For 1983 there is likely to be a rebound in agricultural production, and growth in real GDP may approximate the plan target (6 per cent). However, current indications are that the domestic financial situation as well as the external accounts are likely to deteriorate sharply. The authorities have responded to the present circumstances by, on one hand, taking some measures to improve the fiscal situation, such as limiting wage increases and capital outlays. On the other hand, they have also tightened import and price controls. The staff believes that appropriate remedial measures should include a less expansionary credit policy, an increase in interest rates, and further efforts to contain the fiscal deficit. The latter could be effected by stretching out new recruitment, postponing some capital expenditures, and reducing subsidies and transfers to both public enterprises and consumers. In addition, due regard should be given to the erosion in Tunisia's margin of competitiveness, which has resulted from the rapid rise in wages and labor costs in the past few years. These steps should be initiated soon to ease pressures on the balance of payments and to prevent an undesirable additional intensification of import restrictions and further backsliding in the liberalization of prices. As discussed above, the authorities have been actively considering various adjustment measures, including in the areas of interest rates and subsidies, and have been closely monitoring the exchange rate to ensure that the dinar is appropriately adjusted in line with relevant price and cost developments.

For the medium term the authorities should be encouraged to implement rapidly the structural reforms envisaged under the Sixth Plan, such as changing the pattern of investment and improving the performance of public enterprises. In this regard, the institutional changes initiated for the agricultural sector as well as the first steps taken to promote a more efficient public enterprise sector are positive developments, which need to be reinforced. However, increased emphasis should be accorded appropriate demand management policies to maintain a viable balance of payments and debt posture. In particular, there is considerable need for firmer incomes, monetary, and fiscal policies. A significant curtailing of real wage gains would seem to be required, not only to contain the growth in consumption but also to help ensure the competitiveness of Tunisian exports. With the declining importance of petroleum revenues, a strong adjustment will be necessary to stabilize the fiscal deficit. Given the reluctance of the authorities to consider increases in tax rates and the relatively slow process of strengthening the tax administration, which is required to obtain benefits from the current tax reform, most of the adjustment will have to be borne by expenditure policies, especially in the areas of wage, subsidy and transfer, and capital outlays. Import and price restrictions are not satisfactory substitutes for balanced financial, incomes, and pricing policies. A resort to further import restrictions would also be inconsistent with the plan's objectives to promote exports, encourage foreign investment, improve the overall efficiency of the economy, and moderate domestic inflation. Rather, the authorities should begin dismantling the extensive system of import restrictions, including a relaxation of import quotas for consumer goods.

Tunisia continues to maintain restrictions on payments and transfers for current international transactions. As in the case of import restrictions, the staff recommends that the authorities aim at the progressive liberalization of these restrictions. Since the restrictions on payments and transfers for current international transactions are maintained by Tunisia in accordance with Article XIV, they are not subject to Fund approval.

It is recommended that the next Article IV consultation with Tunisia be held on the standard 12-month cycle.

The Tunisian authorities will shortly undertake a review of the plan targets through 1986 and intend simultaneously to request Fund technical assistance in preparing a financial and structural adjustment program covering the period 1984-86. The authorities believe that such a program, prepared with the "moral and technical support of the Fund," would help the Government to implement appropriate adjustment policies and to mobilize the external financial assistance required to achieve the envisaged restructuring of the economy and a gradual removal of import restrictions. Such a program is expected to be worked out in October-November, in conjunction with the preparation of the 1984 budget.

VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision in concluding the 1983 Article XIV consultation with Tunisia, in the light of the 1983 Article IV consultation with Tunisia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. No significant changes have been made in Tunisia's system of exchange restrictions since the last consultation. The Fund encourages the authorities to ease restrictions on payments and transfers for current international transactions.

Fund Relations with Tunisia

Date of membership:	April 14, 1958
Quota:	SDR 94.5 million (Proposed quota: SDR 138 million)
Exchange system:	The exchange rate of the dinar is determined in accordance with a basket of currencies. Buying and selling rates for foreign currencies are determined daily by the Central Bank. As of March 31, 1983, the dinar rate of the U.S. dollar was D 1 = US$ 1.524 equivalent to D 1 = SDR 1.413.
Fund holdings:	As of April 30, 1983, the Fund's holdings of Tunisian dinars amounted to SDR 75.3 million, equivalent to 79.7 per cent of quota.
SDR position:	As of April 30, 1983, Tunisia's holdings of SDRs amounted to SDR 14.2 million, equivalent to 41.5 per cent of its net cumulative allocation of SDR 34.2 million.
Gold distribution:	41,066 troy ounces of fine gold
Distribution of profits from gold sales:	US$7.6 million

The last Article IV consultation discussions with Tunisia were held in Tunis during the period March 2-16, 1982. The staff report (SM/82/98) and the recent economic developments paper (SM/82/110) were discussed by the Executive Board on June 30, 1982. The decision adopted was as follows:

1. The Fund takes this decision in concluding the 1982 Article XIV consultation with Tunisia, in the light of the 1982 Article IV consultation with Tunisia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Although no major changes have been made in Tunisia's system of exchange restrictions since the last consultation, some relaxation of restrictions has taken place, including an easing of administrative procedures. The Fund encourages the authorities to ease further restrictions on payments and transfers for current international transactions.

Financial Relations of the World Bank Group with Tunisia

Date of membership IBRD: April 1958

Capital subscription IBRD: SDR 37.3 million

IBRD/IDA lending operations 1/	Committed		Disbursed	
	IBRD	IDA	IBRD	IDA
	(In millions of U.S. dollars)			
Agricultural and rural development	248.8	8.9	74.1	8.9
Education	61.6	19.4	4.6	19.4
Population	12.5	9.5	--	9.5
Power and utilities	280.9	10.5	144.0	10.5
Transportation	233.4	16.9	110.2	16.9
Industry and tourism	271.1	10.0	161.2	10.0
Total	1,108.3	75.2	494.1	75.2
Repayments	118.2	7.2		
Debt outstanding (including undisbursed)	990.1	67.9		
IFC operations (gross commitments)	21.8			

Source: World Bank.

1/ Through the end of April 1983.

TUNISIA - Basic Data

Area, population, and GDP per capita

Area:	164,154 square kilometers
Population: Total (1982)	6.68 million
Growth rate (1982)	2.6 per cent
GDP per capita (1982)	SDR 1,072

	1979	1980	1981	1982 Prelim.	1983 Forecast
	(In millions of dinars)				
Gross domestic product at 1980 prices	3,365	3,510	3,685	3,722	3,945
Agriculture and fishing	448	490	523	477	510
Energy, power, and water	413	432	396	384	405
Mining	41	45	53	42	48
Manufacturing	368	416	444	459	514
Construction and public works	201	207	224	232	233
Services and other	1,266	1,446	1,566	1,626	1,713
Indirect taxes minus subsidies	528	474	479	502	522
GDP at current prices	2,935	3,510	4,088	4,670	5,415
Domestic expenditure	3,081	3,700	4,453	5,135	5,915
Private consumption	1,775	2,171	2,519	2,935	3,377
Public consumption	444	510	619	800	938
Gross capital formation	862	1,019	1,315	1,400	1,600
Resource gap	-146	-190	-365	-465	-500
Increase in consumer prices (per cent)	7.7	10.0	9.9	12.6	11.0
Government finance 1/					
Revenue and grants	952.0	1,131.2	1,334.6	1,654.2	1,834.4
Current expenditure	-728.2	-784.1	-909.9	-1,253.7	-1,472.4
Government savings	213.0	325.1	419.3	390.3	360.5
Direct investment	-265.4	-333.3	-443.5	-507.9	-602.4
Capital transfers, participations, and net lending	-98.0	-112.7	-86.7	-133.4	-117.5
Overall deficit (-)	-139.6	-98.9	-105.5	-240.8	-357.9
Financing					
Foreign (net)	136.8	80.4	108.7	109.4	176.3
Domestic (net)	2.8	18.5	-3.2	131.4	181.6
Of which: banking system	(36.2)	(-0.3)	(24.4)	(41.7)	(75.5)

1/ Consolidated operations of the Central Government.

TUNISIA - Basic Data (concluded)

	1979	1980	1981	1982 Prelim.	1983 Forecast
			(In millions of dinars)		
Money and credit (end of period)					
Foreign assets (net)	165	191	236	252	232
Domestic credit	1,353	1,591	1,978	2,440	2,918
Central Government	(215)	(219)	(255)	(307)	(391)
Economy	(1,138)	(1,372)	(1,723)	(2,133)	(2,527)
Money and quasi-money	1,219	1,445	1,724	2,050	2,353
Money	(786)	(950)	(1,115)	(1,379)	(1,593)
Quasi-money	(433)	(495)	(609)	(671)	(760)
Other items (net)	299	337	490	642	797
			(In millions of SDRs)		
Balance of payments					
Exports, f.o.b.	1,169	1,386	1,789	1,544	1,573
Imports, f.o.b	-1,942	-2,213	-2,696	-2,629	-2,784
Balance	-773	-827	-907	-1,085	-1,211
Net services and transfers	439	487	493	529	527
Current account	-334	-340	-414	-556	-684
Grants	38	65	17	28	19
Direct investment	59	192	313	293	282
Public and private enterprises	234	121	186	169	257
Central Government	52	67	51	26	96
Other 1/	48	-49	-76	65	--
Capital account	431	396	491	581	654
Allocation of SDRs	7	7	6	--	--
Overall balance	-104	63	83	25	-30
Outstanding external debt	2,210	2,321	2,457	2,775	3,125
Debt service ratio	11.0	12.1	13.6	16.8	17.0
Gross official reserves	446	469	467	556	424 (March)
Terms of trade (percentage changes)					
Export prices (in SDRs)	35.6	37.6	-5.0	-4.5	-9.0
Import prices (in SDRs)	20.4	17.0	3.1	-3.2	1.8
Terms of trade	12.8	14.3	6.2	-0.7	-10.6
Exchange rates (period averages)					March
D/SDR	0.5252	0.5271	0.5823	0.6516	0.6940
D/F	0.0955	0.0958	0.0909	0.0899	0.0918
Trade-weighted (nominal; 1975 = 100)	98.9	99.9	100.7	96.3	94.2
Trade-weighted (real; 1975 = 100)	86.2	84.6	82.7	81.2	84.0

1/ Including short-term capital, commercial banks, and errors and omissions.