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February 12, 2021

Statement by Mr. Mozhin, Mr. Palei, and Mr. Potapov on Tunisia
(Preliminary)
Executive Board Meeting
February 17, 2021

1. **We broadly agree with staff's analysis of the complex and urgent challenges facing the Tunisian economy.** The country has been severely affected by the Covid-19 shocks and the global economic recession, aggravating already elevated macroeconomic imbalances. Tunisia experienced a steep recession in 2020, with GDP contraction and the fiscal financing needs far exceeding staff's projections at the time of the RFI approval. According to staff, public debt would become unsustainable unless the authorities implement a significant fiscal adjustment and address the risks stemming from the SOEs sector and the expansion of the wage bill. The outlook is highly uncertain and is exposed to substantial downside risks. At the same time, we support the authorities' emergency package to mitigate the Govid-19 shocks and welcome their efforts to advance the vaccination program for the population.

2. **Social tensions and burden-sharing tradeoffs are among the key challenges that may delay the implementation of the necessary reforms to strengthen macroeconomic performance.** Garnering adequate support requires a delicate approach to finding the right sequencing of reforms, conducting proper consultations with various stakeholders, and ensuring adequate social protection and targeted support for low-income households. We believe that achieving sustainable and inclusive growth also calls for a deeper engagement with the Fund through an upper-credit-tranche (UCT) IMF arrangement. *Could staff comment on the key steps and policy recommendations necessary to reach a social compact? Can the authorities strengthen communication efforts to facilitate the implementation of the reform scenario?*

3. **Given the current uncertain environment, prudent economic policies should be based on conservative assumptions.** We share staff's concerns about the authorities' assumption on the oil price in the 2021 budget, as well as about the lack of information on

how to achieve the fiscal savings and address rising arrears to SOEs and the social security funds. Securing financing for the large fiscal needs can turn out to be challenging, as suggested by the unsuccessful attempt to issue the bond of $750 million and the recourse to direct monetary financing of the budget in 2020. *Could staff elaborate on their assumptions for multi- and bilateral budget support and financial market access in 2021 (Table 8 of the report)?*

4. **The pace of fiscal consolidation requires careful calibration to support economic recovery and restore fiscal sustainability.** We agree with the need to improve the effectiveness of fiscal expenditures by reducing inefficient energy subsidies, trimming the wage bill, and making social assistance more targeted and effective. Similarly, the authorities need to create more fiscal space by accelerating the tax reforms and strengthening tax administration. Such an approach can help the authorities to increase public investments and social spending. At the same time, we would also highlight the need to ensure a strong link between the reduction of energy subsidies and the timely strengthening of the social safety net for poor households.

5. **We appreciate the authorities' concerns about the proposed pace of the wage bill reduction and call on staff and the authorities to continue technical discussions on the possible alternative modalities and approaches to tightening hiring limits and constraining new wage increases.** We thank staff for Annex III and believe that the report could have benefited from a more thorough analysis of the wage bill reforms in Tunisia, including through preparation of a comprehensive Selected Issus paper with a special chapter on this topic. The analysis could have been based on the past recommendations, while taking into account the implications of the Covid-19 crisis. Such an approach, in our opinion, could have helped the Fund gain more traction with the authorities.

6. **Strengthening financial management and governance in the SOE sector should remain the authorities' key priority.** Major SOEs have been experiencing substantial losses over the recent years and remained a significant drag on public resources. As highlighted in the report, major SOEs have large arrears and cross arrears with the government, the social security funds, and other entities. A comprehensive restructuring strategy and a revised regulatory framework are needed to improve the efficiency and financial performance of the SOE sector. *We would appreciate staff's elaborations on the timing for preparation of the new SOE law and its subsequent approval by Parliament.*

7. **Going forward, monetary financing of the budget should be avoided as soon as circumstances allow to preserve the CBT's progress in strengthening the monetary policy framework.** Monetary policy should remain focused on reducing inflation and maintaining adequate international reserves. We are encouraged that the CBT's recent stress-testing exercise showed that major banks' capital ratios are likely to remain above regulatory requirements. We encourage the monetary authorities to transition to the inflation targeting framework and a more flexible exchange rate when the conditions are in place.

8. **The Covid-19 crisis has heightened the need for ambitious structural reforms to foster social and economic transformation of the Tunisian economy.** The authorities are well advised to implement a comprehensive reform of the social security system, as well as policies that facilitate competition, foster innovation, and address high unemployment. On governance, we agree with staff's recommendations to conduct and publish a comprehensive audit of crisis-mitigation spending.