



TUNISIA

July 2018

THIRD REVIEW UNDER THE EXTENDED FUND FACILITY, AND REQUEST FOR WAIVER OF APPLICABILITY AND MODIFICATION OF PERFORMANCE CRITERIA

In the context of the Third Review Under the Extended Fund Facility, and Request for Waivers of Nonobservance of Performance Criteria, and Rephrasing of Access, 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 July 6, 2018, following discussions that ended on May 30, 2018, 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 June 22, 2018.
- 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



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July 9, 2018

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IMF Executive Board Completes Third Review under the Extended Fund Facility (EFF) Arrangement for Tunisia

On July 6, 2018 the Executive Board of the International Monetary Fund (IMF) completed the third review of Tunisia’s economic program supported by an arrangement under the Extended Fund Facility (EFF). The completion of the review allows the authorities to purchase an amount equivalent to SDR 176.7824 million (about US\$249.1 million), bringing total purchases under the arrangement to the equivalent of SDR 808.1485 million (about US\$1,139.0 million).

The four-year EFF arrangement in the amount of SDR 2.045625 billion (about US\$2.9 billion, or 375 percent of Tunisia’s quota at the time of approval of the arrangement) was approved by the Executive Board on May 20, 2016 (see [Press Release No. 16/238](#)). The government’s reform program that is supported by the EFF arrangement aims at strengthening the recovery by reducing macroeconomic vulnerabilities, ensuring adequate social protection, and fostering private sector-led, job-creating growth. Priorities include growth-friendly and socially conscious reforms aimed at stabilizing public debt while raising investment and social spending. Monetary policy focuses on curbing inflation, continued exchange rate flexibility, and strengthening international reserves. Structural reforms supported under the arrangement focus on improving governance, the business climate, fiscal institutions, and the financial sector.

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

“Growth picked up in early 2018 and confidence has improved, but macroeconomic imbalances persist. Unemployment has dropped only marginally, inflation is high, the budget and current account deficits are large, and international reserves are below the recommended level.

“Policy and reform implementation has improved markedly since the Second Review. The Tunisian authorities remain firmly committed to a socially-balanced, gradual approach to macroeconomic adjustment that is supported by the four-year arrangement under the Extended Fund Facility. The success of the authorities’ program depends on sustained efforts

to reduce macroeconomic vulnerabilities, ensure adequate social protection, and foster job creation.

“Achieving the authorities’ fiscal targets requires addressing budget pressures. Policy priorities for 2018 include stronger revenue collection, energy price adjustments to limit the impact of international oil prices on the budget, voluntary separations for civil servants, the absence of new wage increases, unless growth surprises on the upside, and pension reform.

“The recent significant hike in the policy interest rate demonstrates the central bank’s strong commitment to price stability. Further rate hikes may be needed if inflation does not decelerate, especially as key interest rates remain negative in real terms.

“Exchange rate flexibility, supported by more competitive central bank foreign exchange auctions, is critical to help improve the current account position and rebuild international reserves.

“The authorities have increased social transfers and progressed with the database on vulnerable families. Pension reform, as well as efforts to better target social policies, should be accelerated.

“The one-stop shop for investors and the negative list of investment authorizations are positive signals for investors. Structural reform priorities going forward include the appointment of the members of the High Anti-Corruption and Good Governance Authority and reforms of the Anti-Money Laundering/Combating the Financing of Terrorism regime.

“Strong implementation of the authorities’ program is essential to mitigate economic, social, and political risks. Building on the strong partnership with the international donor community, it will be important to sustain strong donor financial support and capacity building to help ensure a successful transition to an economy that fosters inclusive growth with the private sector as its main engine.”



TUNISIA

June 22, 2018

THIRD REVIEW UNDER THE EXTENDED FUND FACILITY, AND REQUEST FOR WAIVER OF APPLICABILITY AND MODIFICATION OF PERFORMANCE CRITERIA

EXECUTIVE SUMMARY

Context. The government has strengthened policy and reform implementation in recent months. All Quantitative Performance Criteria (QPCs) for end-March and three out of nine Structural Benchmarks (SBs) for the Third Review were met. One additional SB was implemented with delay. Growth picked up to 2.5 percent in the first quarter, and confidence has improved, albeit it continues to be affected by divisions in the coalition government, risks of security and migration spillovers from Libya, and higher international oil prices. Inflation has accelerated and weighs on the purchasing power notably of the less well-off, while international reserves remain below prudent levels.

Outlook and policy mix for the Third Review. Growth is on track to reach 2.4 percent in 2018, propelled by agriculture, manufacturing, and tourism-related services. Sustained tightening of the macroeconomic policy mix will help contain inflation and reduce the twin deficits to rebuild reserves and reverse debt accumulation—critical prerequisites for sustained, job-creating investment. The authorities and staff agreed to complement the measures set at the Second Review with: (1) more ambitious energy price hikes to limit the increase in energy subsidies to 0.5 percent of GDP, additional voluntary departure schemes for civil servants, and steps to buttress the financial viability of pensions; (2) further interest rate increases and changes to the Central Bank's collateral framework; (3) augmented social transfers to protect the vulnerable from price increases; and (4) accelerated efforts to boost private sector-led growth. The authorities intend not to grant new wage increases in 2018, unless growth surprises positively.

Risks. Stalled efforts to revitalize consensus on reforms among the parties represented in the unity government, as well as protests across the MENA region against fiscal consolidation could affect the capacity to implement policies and reforms. Residual threats to security and further hikes in international oil prices are other key risks.

Staff supports the authorities' request for the completion of the Third Review under the Extended Fund Facility (EFF). This would make available SDR 176.7824 million (US\$246 million) and catalyze much-needed donor disbursements. Staff also supports the modification of and the waiver of applicability for all end-June QPCs.

Approved By
Adnan Mazarei and
Vitaliy Kramarenko

Discussions took place in Tunis during May 17 to 30, 2018 and continued from headquarters until June 15. The mission team comprised Björn Rother (head), Kerstin Gerling (advance team lead), Alexei Kireyev, Maria Mendez (all MCD), Olivier Basdevant (FAD), Thomas Harjes (MCM), Tim Willems (SPR), Robert Blotevogel (Resident Representative), and Adnen Lassoued (local economist). Monia Saadaoui (OED) participated in discussions. Staff met with the Governor of the Central Bank; the Minister of Finance; the Minister of Development, Investment and International Cooperation; the Minister in charge of Major Reforms; the Minister of Commerce; the Minister of Social Affairs; senior officials; and representatives of the UGTT labor union and the UTICA employers' association, the corporate and banking sectors, the diplomatic and donor community, civil society, academia, media, and political parties.

Samira Kalla, Ravaka Prevost, and Geraldine Cruz provided excellent assistance.

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STRONGER GROWTH, BUT ALSO HIGH IMBALANCES

1. Notwithstanding a fragile context, policy and reform implementation have improved.

The authorities have taken important measures during recent months (Text Table 1), and phosphate production has resumed after strike activity slowed in March. However, political opposition to the reforms supported under the EFF remains entrenched, especially regarding energy subsidies, the civil service, and pensions. Moreover, it will take some time to ascertain the potential impact on economic policies of the divisions within the governing coalition that emerged in the aftermath of the May local elections.

Text Table 1. Economic Policy Measures Implemented During the First Semester

Fiscal Policy	Monetary and Exchange Rate Policy	Structural Reforms
<ul style="list-style-type: none"> • An ambitious revenue package (2.2 percent of GDP), which helped to achieve a fiscal surplus in the first quarter. • Energy price increases: <ul style="list-style-type: none"> - A 6 percent average increase in the price of the three main automobile fuels in June to help achieve additional savings on fuel subsidies of TD 250 million until the end of the year. - A 7 percent hike in electricity tariffs for corporate customers in May. - A 10 percent increase in natural gas tariffs for corporate customers in May. • Wage bill measures: <ul style="list-style-type: none"> - Confirmation of government intention not to grant new wage increases in 2018, unless growth surprises on the upside. - Issuance of a decree limiting new recruits in 2018 to 3,000, suggesting a replacement ratio of only 25 percent. - Implementation of voluntary departures from the civil service, with 5,000 participants in early retirement and 1,770 participants in negotiated departures. A commitment to reopen the volunteer windows in August 2018 and in 2019. 	<ul style="list-style-type: none"> • Two policy rate increases by an unprecedented 75 bps in March and 100 bps in June. • Broadening of the interest rate corridor from +/- 25 basis points to +/- 100 basis points in January. • Observance of monthly FX intervention budgets from March through May. 	<ul style="list-style-type: none"> • Creation of a one-stop shop for investors. • Parliamentary passage of the legislation in support of public bank restructuring. • Adoption of the pension reform by the Council of Ministers, and a commitment to seek parliamentary adoption by end-September with retroactive effect to July. • Completion of the functional reviews of four key ministries.

2. Growth is firming up, but macroeconomic imbalances remain elevated (Figures 1–5, MEFP ¶¶3–9):

- **Growth rebounded** to 2.5 percent of GDP (y-o-y) in the first quarter of 2018 from 1.9 percent in 2017, supported by agriculture, tourism, and electrical and mechanical industries. Foreign direct investment increased by 15 percent (y-o-y), and investment intentions, a leading indicator, are on the rise. Unemployment slightly declined to 15.4 percent.
- **Inflation accelerated further** through May, reaching 7.7 percent (Annex I). Core inflation increased to 7.2 percent, mainly driven by the pass-through of dinar depreciation, wage hikes, and strong credit growth.
- **The current account deficit improved** in the first quarter, supported by the real exchange rate depreciation realized in 2017. Export volumes expanded by 6.2 percent, while import volumes contracted by 1.0 percent (y-o-y). Higher tourism receipts and remittances also helped, buoyed by stronger growth in Europe.
- **Foreign reserve coverage fell** to 72 days of 2017 imports by mid-June, despite the successful efforts of the authorities to stay within the FX intervention budget since March. The dinar has resumed its depreciation after crossing the psychological barrier of TD 3 per Euro on April 27, trading on June 15 almost 4.5 percent lower vis-à-vis the Euro than at the end of 2017.
- **Monetary policy remains accommodating**, despite recent interest rate hikes. The policy interest rate increased by a total of 175 basis points in 2018 to 6.75 percent in June, but key interest rates remain negative or close to negative in real terms and have contributed to record level Central Bank refinancing of commercial banks in May. This in turn has supported continued strong expansion of credit to the economy, which grew at 13 percent (y-o-y) in March.
- **Public and external debt ratios** reached 70 percent of GDP and 80 percent of GDP at end-2017, respectively. The deterioration was mainly driven by the depreciating real exchange rate and the sustained need for debt-financing to close sizeable fiscal and external financing needs.
- **Financial markets showed resilience.** The stock exchange index grew by 22 percent through June 8 to reach a record high, while credit spreads rose slightly reflecting more volatile sentiment toward emerging markets. Aggregate banking sector statistics for end-2017 report adequate capital and liquidity ratios and, for many indicators, higher profitability (Table 9).

3. Program performance improved since the Second Review:

- **All end-March quantitative targets were met** (MEFP ¶10 and MEFP Table 1).
- **Structural reforms progressed** (¶26, MEFP ¶11, and MEFP Table 2). The authorities met three of the nine Structural Benchmarks (SBs) for the Third Review, and implemented one more with delay. They also completed three Prior Actions for the Third Review. The authorities requested to reprogram outstanding SBs and drop two SBs on the Large Taxpayers Unit (LTU) that are no longer critical for the success of the program.

IMPROVING OUTLOOK, MOSTLY DOWNSIDE RISKS

4. A bolder recovery will depend on strong policy implementation (Text Table 2). The 2018 growth forecast of 2.4 percent remains unchanged. A tighter policy mix in combination with sustained exchange rate flexibility would reduce the high twin deficits; inflation would be limited to an average 8.1 percent. With sustained discipline in policies, public and external debt would be contained below 70 and 90 percent of GDP by 2020, respectively. Reserve coverage would improve to above 4 months of imports over the same horizon, consistent with levels suggested by the IMF's Assessment of Reserve Adequacy (ARA) Assessment of Reserve Adequacy standards (Figure 4).

Text Table 2. Selected Economic Indicators, 2015–23									
	2015	2016	2017	2018	2019	2020	2021	2022	2023
	Proj.								
Real GDP growth (in percent)	1.2	1.1	2.0	2.4	2.9	3.4	3.6	4.0	4.2
Consumer price index growth (period average, in percent)	4.9	3.7	5.3	8.1	7.5	5.9	4.9	4.1	4.0
Gross public debt (in percent of GDP)	55.4	62.4	70.3	70.5	70.0	69.4	68.4	67.5	66.5
External debt (in percent of GDP)	62.8	67.6	80.1	86.4	88.9	89.3	88.3	85.8	82.9
Current account balance (in percent of GDP)	-8.9	-8.9	-10.5	-9.6	-8.6	-7.8	-6.9	-6.5	-6.1
Gross official reserves (end of period, in billions of US\$)	7.4	5.9	5.9	6.4	7.0	7.5	7.9	8.7	9.3
Gross official reserves (end of period, in months of next year's imports)	4.8	3.6	3.1	3.5	3.8	4.1	4.2	4.5	4.8

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

5. Exceptionally high risks continue to weigh on the outlook (RAM, Appendix II). Reforms could suffer from socio-political tensions after the recent suspension of the Carthage II process that sought to clarify the governing coalition's economic policy priorities. Major fiscal decisions are particularly at risk, including those on reducing energy subsidies, public wage restraint, and pension reform. Notwithstanding recent improvements, security and migration risks also remain high, including from spillovers of conflicts in Libya and elsewhere in the region. Finally, a further rise in oil prices could jeopardize the fiscal and external adjustment targets (absent an adjustment in domestic prices, each increase in the international oil price by US\$1 worsens the budget by 0.15 percent of GDP and the current account by 0.08 percent of GDP). Tighter global financial conditions would likely only have a limited effect on Tunisia, given its strong reliance on concessional financing from official donors (Debt Sustainability Analysis, Second Review).¹

STRONG, URGENT MEASURES TO PROTECT GROWTH

6. The three-pillar policy framework supported by the EFF remains pertinent. The authorities and staff continue to agree on the need to stabilize the macroeconomy (Section A);

¹ IMF Country Report No. 18/120.

maintain adequate social protection (Section B); and facilitate private sector-led, job-creating growth (Section C). Advancing on these priorities will be critical to keep the country on track toward achieving more economic prosperity and fairness for all Tunisians and reducing macroeconomic vulnerabilities. The authorities remain firmly invested in a gradual and socially-balanced approach to macroeconomic adjustment that minimizes harm to growth and preserves fairness. They cautioned against major risks associated with a more front-loaded strategy, including the impact of a major exchange rate depreciation on inflation, the budget, and debt. Staff emphasized that the gradual approach underlying the EFF-supported program will require sustained discipline in policy and reform implementation, especially in the face of Tunisia's high vulnerabilities.

A. Maintaining Macroeconomic Stability Amid High Imbalances

Fiscal Policy

Background

7. The agreed consolidation path for 2018–20 remains the authorities' fiscal anchor. The authorities' program of reducing the overall deficit to 2.5 percent of GDP by 2020 depends on an effort of about 1 percent of GDP per year. New taxes and stronger tax collection (including on arrears), as well as measures to mitigate the unanticipated increase in international oil prices, are critical to achieve the deficit reduction in 2018. The bulk of the adjustment going forward shifts to expenditure rationalization. Budget outlays on energy subsidies would fall further, pension transfers would decrease, and the growth of the wage bill would slow. Managing contingent risks from state-owned enterprises (SOEs) will also remain a priority. This strategy is expected to achieve a reversal of the current upward trend in public debt, while creating scope for re-orientating expenditure toward social sectors and public investment.

8. New budget pressures for 2018 require immediate attention. While revenues performed well through May, the budget faces pressures from the spending side: (1) without policy change, the recent increases in international oil prices would swell the energy subsidy budget from 2.0 percent of GDP to 3.3 percent of GDP (estimated at an oil price of US\$70 dollars per barrel); (2) the public pension fund faces a higher liquidity deficit (1.2 percent of GDP compared with 1.0 percent of GDP estimated at the time of the Second Review), while the adoption of the reform law for the public pension fund (*Caisse Nationale de Retraite et de Prévoyance Sociale, CNRPS*) and the decree for the private pension fund (*Caisse Nationale de Sécurité Sociale, CNSS*) encounter delays; and (3) wage bill targets for 2018 and the medium term could suffer without compensatory measures for the low interest in voluntary departures (a total of only 1,770 civil servants were identified as of May 2018, relative to the objective of 20,000 set at the time of the Second Review) or if new wage increases were implemented.

Policy Discussions

9. The authorities and staff agreed on urgent measures to remain within budget targets. A supplementary budget law will facilitate budget re-orientation. The measures explained below will help ensure feasibility of the 2018 deficit target of 5.2 percent of GDP (Text Table 3), together with

using the fiscal space created by: (1) a lower wage bill (-0.3 percent of GDP), reflecting the impact of reduced one-off costs for the departure packages due to weaker-than-expected interest among civil servants (-0.7 percent of GDP) that is partially offset by higher-than-expected headcount (0.4 percent of GDP); and (2) the delay in the liquidation of the *Banque Franco Tunisienne* (BFT) that will not happen in 2018 due to protracted legal proceedings associated with the case (-0.4 percent of GDP). The authorities and staff agree that strong revenue performance will likely continue throughout 2018, which, in addition to delays in the execution of lower-priority public investment, could create additional space to absorb higher spending if needed.

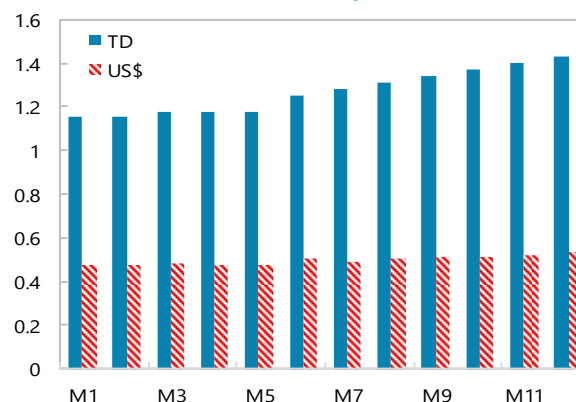
Text Table 3. Changes in Fiscal Program, 2018
(Percent of GDP)

Deficit target	5.2
Spending pressures	2.0
Higher international energy prices	1.3
Higher CNRPS transfers	0.2
Higher wage bill because of lower departures	0.4
Higher social transfers	0.1
Adjustment measures	2.0
Higher domestic energy price adjustments	0.8
Lower one-off costs for departure packages	0.7
Delayed BFT liquidation	0.4
Other	0.1

Sources: Tunisian authorities and IMF staff calculations.

- Measures to contain energy subsidies and protect the poor from the impact of higher prices** (MEFP ¶14). The authorities and staff agreed to accommodate 0.5 percent of GDP of the higher energy subsidy bill in the fiscal program, considering that the scope for adjustment in the fragile socio-political context is limited. This leaves a savings target of 0.8 percent of GDP, which will be realized through: (1) monthly adjustments of domestic prices for the main automobile fuels in response to the recent increases in international oil prices, building on the price hike already realized in June (Prior Action, MEFP Table 2, Text Figure 1); (2) increases in gas and electricity tariffs mainly for corporate customers; and (3) other measures to reduce consumption of subsidized fuels, including better controls on leakages and the introduction of product differentiation. To reduce the impact of higher prices, the authorities announced to increase social transfers by at least TD 100 million for the second half of 2018 (Prior Action, ¶21 and MEFP¶18).

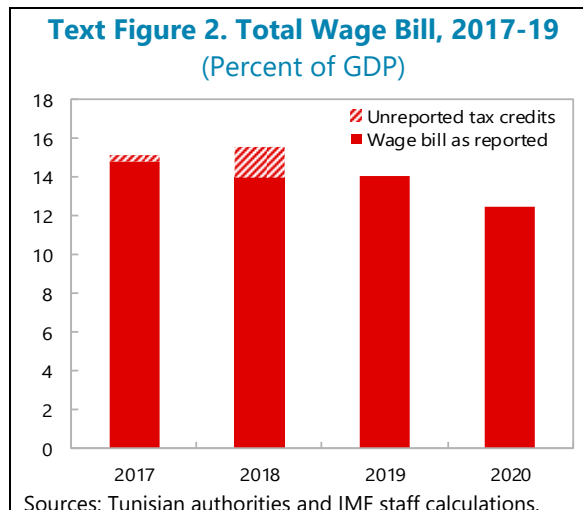
Text Figure 1. Average Domestic Fuel Price Per Liter, 2018



Sources: Tunisian authorities and IMF staff calculations.

- Transfers to the pension funds** (MEFP ¶14). The authorities intend to cover half of the CNRPS liquidity gap for 2018 by SOEs clearing their sizeable arrears to the fund. In addition, to ensure collection of higher contributions for the second half of 2018, the Council of Ministers adopted the delayed pension law (unmet April SB implemented in June) and now seeks Parliament passage by end-September with retroactive effect from July. This will leave 0.4 percent of GDP in needs to be covered by transfers from the budget, compared with 0.2 percent envisaged at the time of the Second Review.

- Wage bill measures** (MEFP ¶14). To remain on track towards the wage bill target of 12.4 percent of GDP in 2020, the authorities intend to: (1) avoid new salary increases in 2018 unless growth surprises on the upside; (2) remain below the hiring limits set for 2018 and 2019; and (3) reopen the departure schemes in the summer of 2018 and in 2019, targeting 8,000 additional volunteers. Higher inflation will also help. The completion of the functional reviews for four big ministries (met June SB) will facilitate the implementation of this approach by helping to identify areas of excess and short demand for labor. The authorities will eliminate tax credits in 2019 to enhance transparency of the public wage bill (Text Figure 2).

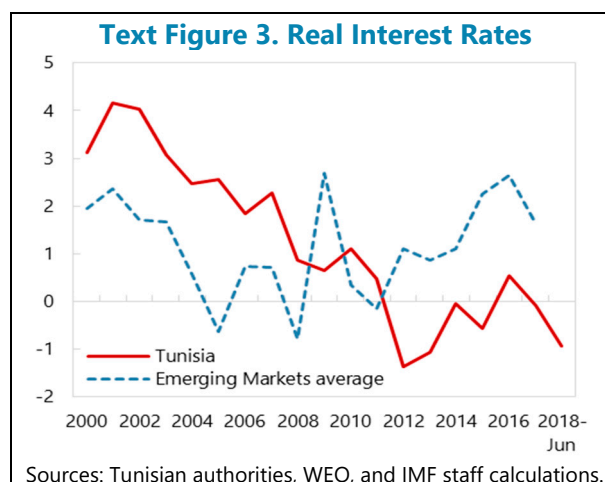


10. Fiscal reforms in support of medium-term deficit consolidation need to continue (MEFP ¶15), supported by technical assistance chiefly from the World Bank, *Agence Française de Développement* (AFD), European Union (EU) and the IMF. On the expenditure side, priority areas include expenditure rationalization, parametric reform of the pension system, treasury cash management, and mitigation of contingent fiscal risks (notably from SOEs). On the revenue side, efforts are geared towards making the tax system simpler and fairer (with a focus on the on- and off-shore system, and liberal professions) and modernizing the tax administration. As to the latter, the authorities are replacing the original focus on creating a Large Taxpayers' Unit (LTU) recommended by the IMF with a broader reform that seeks to integrate all tax administration functions (administration, audit, and recovery) within one umbrella structure, following the model implemented in France. Strong revenue performance in early 2018, including on arrears collection, suggests that this shift will not put at risk budget targets under the EFF.

Monetary Policy

Background

11. The current monetary policy stance still feeds inflation (Figure 5). With inflation now well above the historical average of 3–5 percent and further accelerating to reach an expected 8.9 percent (y-o-y) by end-2018 (Annex I), there is a strong risk that inflation expectations adjust upward and jeopardize the credibility of the Central Bank. Strong credit growth fueled by historically low real interest rates and record-level Central Bank refinancing has contributed to the persistence of price



pressures. Low real interest rates (Text Figure 3) paired with speculation about further dinar depreciation have slowed deposit growth, instead encouraging cash holdings and disintermediation.

12. Monetary policy transmission channels remain ineffective. The CBT has made progress in updating their monetary policy framework (MEFP ¶16), but the unchecked growth of credit after the successive interest rate hikes since April 2017 suggest that monetary tightening has so far only slowly and weakly impacted monetary conditions. Price signals seem to have limited effect due to: (1) delayed pass-through caused by the ceiling on “excessive interest rates” and the practice of adjusting the underlying money market rate only twice a year;² and (2) a generous collateral framework that does not apply haircuts to government paper and fails to discriminate among other collateral (all discounted at 25 percent). Moreover, transmission is hampered by limited exchange rate flexibility and the growing demand for currency that reduces the money multiplier. The authorities explained that high demand for refinancing also reflects structural factors, including a strong reliance of the central government on domestic debt markets.

Policy Discussion

13. Further monetary tightening is essential to contain price pressures (MEFP ¶16). The authorities agreed with staff to continue policy rate hikes until the money market rate reaches positive territory in real terms. This will be essential to curb credit growth and ultimately decelerate inflation. Frequent and firm communication by the Central Bank on its commitment to achieving lower inflation as the CBT’s main mandate, its longer-term inflation objective, and its views on the short-term outlook for policy rates will support this task (Annex III). The authorities and staff shared the view that maintaining a firm anti-inflation stance during the months ahead will be important in the context of sustained exchange rate flexibility and accelerating inflation.

14. Measures should maximize the response of monetary transmission to price signals (MEFP ¶16). The authorities and staff agreed on the important role of the law on excessive interest rates (reprogrammed SB for December 2018 due to an overcrowded agenda in Parliament) in improving transmission, including through more frequent updates of the reference interest rate for the calculation of maximum borrower rates. Moreover, the authorities highlighted that the intended increase in the haircut applied to collateral (to 30 percent from 25 percent), in combination with the tightening of the list of eligible collateral for refinancing, will reduce liquidity demand from banks. Staff emphasized that fully removing interest rate caps; extending haircuts for refinancing also to government paper; modernizing the payments system to discourage the use of currency; and further banking sector reform (¶25) could enhance transmission and protect the CBT’s balance sheet from credit risk. Moreover, staff argued that ongoing efforts by public banks to reduce their large holdings of non-performing loans (NPLs) will also help.

² Currently lending rates in Tunisia cannot exceed the money market rate by more than 20 percent. The authorities plan to increase this limit for firms to 33 percent. The maxima are applied across loan classes and sectors and are only adjusted twice a year.

15. Central Bank safeguards need to be strengthened (MEFP ¶21). While there have been lags in finalizing the implementation of some of the 2016 safeguards recommendations, the CBT is committed to addressing outstanding issues by end-2018.

Exchange Rate Policy

Background

16. Exchange rate flexibility supports external sector adjustment. Real exchange rate depreciation realized over 2017 started to reverse unsustainable trends in the trade balance in early 2018, but more exchange rate flexibility will be needed to achieve a sustainable current account position by encouraging exports and compressing imports.³ This is especially true in light of a growing inflation differential relative to Tunisia's main trading partners. Further depreciation will also facilitate improved reserve coverage (currently standing at about 75 percent of the IMF's ARA metric), which depends on a stronger current account and sustained external borrowing even with the Central Bank's foreign exchange (FX) interventions remaining below agreed budget ceilings (Prior Action, MEFP Table 2). The exchange restriction imposed in October 2017 (a ban on trade credit for certain non-essential imports) has so far only played a minor role in discouraging imports, but created concerns among banks and economic actors.

17. The Central Bank's FX auction mechanism has not yet led to competitive practices.

While being the exclusive tool for interventions since May 2017, the implementation of the mechanism continues to fail standards of competitive auctions: typically, no bids are rejected, and pro-rating applies proportionally across all bids irrespective of their attractiveness.

Policy Discussions

18. Sustained exchange rate flexibility depends on competitive FX interventions. The authorities reiterated their commitment to comply with monthly net FX intervention ceilings with the aim of reaching adequate reserve coverage as soon as possible and reduce the residual overvaluation of the real effective exchange rate that amounted to 10-20 percent at the end of 2017. This will facilitate a gradual transition to a market-based exchange rate system. The CBT also agreed with staff to start implementing more competitive FX auctions in June (reprogrammed SB for August 2018; MEFP ¶¶11 and 17), benefitting from a stronger interbank market as FX inflows from phosphates and tourism should reduce the risk of disorderly market reactions. This change in the auction mechanism could be supported by IMF technical assistance. The authorities cautioned, however, that a more competitive process may require larger FX interventions to smooth exchange rate movements. It would thus be important to make the transition gradually.

19. The exchange restriction will be eliminated. The authorities confirmed their intention to remove the exchange restriction introduced last October 2017 by end-2018 (MEFP ¶17). Capital

³ The elasticity of the current account to the real effective exchange rate equals 0.37. This implies that a 10 percent depreciation will over time improve the current account by 3.7 percent of GDP.

account liberalization would only proceed in line with progress on developing domestic financial institutions and upgrading prudential supervision (MEFP ¶121).

B. Ensuring Adequate Social Protection

Background

20. There has been mixed progress with measures to ensure adequate social protection.

- **Better targeting will benefit from progress with the database of vulnerable households.** The authorities have progressed with cleaning up the database, which suffers from ghost entries and other issues (SB for December 2018). Once completed, it will provide a better basis for more efficient social policies. Supported by the World Bank, the authorities have started to explore options to improve targeting to the most vulnerable through cash transfers, subsidized health services, and a reform of the system of food subsidies.
- **Social spending has increased beyond the program floor established for end-March 2018** (MEFP Table 2). The envelope now includes augmented cash transfers and more health care support for vulnerable families and low-income pensioners, including in response to widespread street protests in January.
- **Delays in reforming the two pension funds have affected their liquidity situation** (MEFP ¶¶14 and 18). The higher-than-envisaged deficit of the CNRPS public pension fund will require a firm approach to arrears clearance from SOEs and higher-than-envisaged budget transfers (¶9). The authorities do not intend to mobilize budget resources for the CNSS private pension fund, which is expected to cover its needs by reinforced collection of contributions and, if needed, asset sales. A direct pass-through of contributions improved the liquidity situation of the medical insurance fund (*Caisse Nationale d'Assurance-Maladie*, CNAM), eliminating the short-term need for further government support.

Policy Discussions

21. The authorities aim at faster progress with reforming social policies (MEFP ¶18 and Table 2). To help protect the poor from the impact of rising prices, the authorities announced to increase social spending by at least TD 100 million (0.1 percent of GDP) for the second half of 2018 (Prior Action) to increase the number of vulnerable families benefitting from cash transfers by 35,000 to 285,000, support school children, and raise subsidies for healthcare, especially for poor pensioners, the chronically ill, and pregnant women. Furthermore, the authorities and staff agreed on elevating the status of the program floor on social spending to a QPC to strengthen this commitment. The Council of Minister adopted a reform law for the CNRPS in June (SB not met, but implemented with delay) as a prerequisite for Parliament consideration. The Prime Minister will sign the decree on the reform of the CNSS once Parliament adopted the CNRPS law. Staff welcomed these steps, but emphasized that the current reforms remain insufficient to close the gap between benefit levels and resources. To ensure financial stability of the pension funds, these first important steps should be followed as soon as possible by more ambitious parametric reform. The authorities

explained that discussions with social partners on the next steps with pension reform would be started by the fall.

C. Creating More Opportunity for the Private Sector

Business Climate and Governance

Background

22. The business environment improved, but governance reform encountered delays. The authorities established a one-stop shop for large investors (met May SB) and adopted a negative list of eight sectors that remain subject to investment authorizations, while freeing all other sectors from prior approval. They also adopted a change in the procedures regarding investment authorizations: the new presumption will be that permission would be granted automatically after the end of a 60-day window in case no response had been received. The authorities are confident that these measures, together with other initiatives such as the recent passage of the StartUp Act, will help attracting new domestic and foreign investment. On governance, the operational start of the High Anti-Corruption Authority encountered delays due to the necessary Parliament approval of its Board members. Work on the energy sector is progressing, including through an action plan for the public electricity company (*Société Tunisienne de L'Electricité et du Gaz*, STEG) to reduce losses and improve collection of outstanding obligations.

Policy Discussions

23. Recent achievements offer a good basis to continue with reforms. Staff welcomed the recent steps to facilitate investment, and recommended follow-up measures such as: (1) enhancing the regulatory framework for public procurement, and improving efficiency and transparency of the public procurement system; (2) strengthening the regulatory framework for public-private partnerships (PPPs); and (3) reforming the legal framework for energy and natural resource management, including renewable energy resources. In those areas, the authorities will benefit from World Bank technical assistance. The authorities emphasized that Parliament already adopted a short list for the board members of the High Anti-Corruption Authority in June, but that their nomination may be delayed through end-2018 (reprogrammed SB for December 2018). Staff emphasized the need to move quickly and ensure that the necessary infrastructure for the authority to investigate high-level or complex corruption cases will be provided (for example, access to databases including asset declarations of public officials and mechanisms for information sharing with other agencies).

Financial Sector

Background

24. Financial soundness indicators have improved, partially reflecting reform progress. Financial soundness indicators for end-2017 do not show a system-wide negative impact from the recent dinar depreciation or higher interest rates; indeed, profitability improved. Reforms to

strengthen the financial system and enhance access to finance have progressed, notably Parliament adoption of a set of laws facilitating NPL restructuring of public banks (met June SB). The vote of the resolution committee on the orderly resolution of the BFT is expected by August (reprogrammed SB for August 2018, MEFP ¶121). The authorities advanced on improving Tunisia's Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) regime, in response to the shortcomings identified by the Financial Action Task Force (FATF) and the EU. They expect that these preventive measures, including commercial registries to improve entity transparency and targeted financial sanctions, will facilitate Tunisia's exit from the FATF-enhanced surveillance list. Work on the financial inclusion strategy also continues, including a financial inclusion indicator database planned for December 2018. The project on the regional bank and on access to finance for small- and medium-sized enterprise (SMEs) was discussed by the Council of Ministers in February 2018.

Policy Discussion

25. Efforts in support of financial sector stability and access to credit need to continue (MEFP ¶121). The authorities are confident that public banks will make swift progress with the reduction of their NPL holdings, supported by the new legislation. The three main public banks currently respect prudential ratios and have started to implement organizational changes that will facilitate loan workouts and better monitoring of credit risk. The authorities also remain committed to implementing measures that will help to modernize banking supervision, improve access to finance especially for SMEs, and strengthen financial sector governance. The authorities and staff agreed on the usefulness of tightened loan-to-value ratios and upgraded, risk-based supervision tools to address risks linked to the recent growth in shorter-term consumption credit.

PROGRAM ISSUES AND MODALITIES

26. Strong conditionality continues to guide program implementation:

- **Quantitative targets** (MEFP ¶10 and MEFP Table 1). Revised QPCs for end-June, end-September, end-December 2018 and new QPCs for end-March 2019 will support: (1) reducing debt through fiscal adjustment while preserving an increase in social spending and, from 2019, public investment; (2) containing inflationary pressures through reducing the growth of base money; and (3) ensuring adequate reserve coverage through lower FX interventions and more exchange rate flexibility. The QPCs on the primary balance and current primary expenditures will drop the adjuster on the previously envisaged BFT liquidation, as complex legal procedures cause unpredictable delays beyond 2018 (see also ¶19). New quarterly QPCs will be set from end-September 2018 on social spending (replacing the current IT) and on net FX interventions (in addition to the monthly IT). The authorities are also seeking a waiver of applicability of all end-June QPCs, as the relevant data, in accordance with the TMU, will only be available after the scheduled date for Executive Board consideration of the Third Review.
- **Structural benchmarks** (MEFP ¶11 and MEFP Table 2). Following the Executive Board's recommendation for parsimony, the authorities request that this Review refrains from setting new SBs, drops the two SBs related to the operationalization of the LTU (MEFP ¶15), and

reprograms the four delayed SBs (on the appointment of the members of the High Anti-Corruption Authority, vote on the BFT, maximum lending rate, and Central Bank's FX auctions).

27. The program remains fully financed, but exceptionally high risks persist. Donors' financing assurances and the envisaged international bond issuances will cover financing needs during 2018–20 (Text Table 4). Strong commitment by the authorities to the agreed reforms and a strong program monitoring framework will remain essential as mitigation strategies for the significant risks weighing on program objectives (115).

Text Table 4. Cumulative External Financing of the Central Government Budget, 2016–20
(In millions of U.S. dollars)

	2016	2017				2018				2019				2020
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q4
						Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total budget grants and loans	1,871	992	2,512	3,072	3,734	537	1,885	2,902	4,265	363	765	1,723	3,280	2,833
Grants	57	0	0	14	75	1	1	71	136	0	0	45	89	90
Loans	1,814	992	2,512	3,059	3,659	536	1,884	2,831	4,129	363	765	1,678	3,191	2,743
Bilateral	0	0	1,000	1,000	1,118	0	124	124	373	0	0	0	100	100
G7	0	0	0	0	118	0	124	124	373	0	0	0	100	100
Other	0	0	1,000	1,000	1,000	0	0	0	0	0	0	0	0	0
Multilateral	835	0	425	881	1,260	432	552	1,396	1,839	259	557	1,366	1,625	1,127
<i>of which:</i> IMF	316	0	315	315	315	245	245	502	759	259	517	776	1,035	520
Market issuance and other	979	992	1,086	1,178	1,281	104	1,208	1,312	1,916	104	208	312	1,466	1,516

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

28. Tunisia maintains the capacity to repay the IMF. Credit outstanding to the IMF will peak at 372 percent of quota in 2020. Obligations to the IMF will reach a maximum of 1.4 percent of GDP or 22 percent of external debt service in 2018 (Table 12). In a more adverse scenario, these ratios could rise considerably but Tunisia is expected to maintain adequate capacity to repay.

STAFF APPRAISAL

29. Growth is improving, but considerable risks continue to weigh on the outlook.

Confidence has strengthened on the back of improved security and the recovery in Europe. First-quarter growth, including for exports, was significantly stronger than in recent years. Agriculture has been the main engine, but there are early and encouraging signs of a more broad-based pick-up. At the same time, macroeconomic imbalances—notably accelerating inflation, low international reserves, and high twin deficits—are fed by weaknesses in external competitiveness, fiscal pressures, accommodating monetary policy, and delays with structural reforms. The potential for additional increases in international oil prices, lower appetite for emerging market credit, and security tensions in the MENA region also weigh on the outlook.

30. Business as usual is not an option in the face of high macroeconomic imbalances. The road to economic growth and jobs goes through maintaining macroeconomic stability, which requires Tunisia to align its spending better with its resources. It is unlikely that 2018 will be the last difficult year for Tunisia's economy; but it will be a decisive year to implement strong policies that

will help reduce vulnerabilities and rebuild buffers to prevent abrupt, and potentially disorderly adjustment. The fiscal consolidation for 2018 is on track after a strong first quarter, but risks to the budget targets have increased. The recent increases in the policy interest rate played an important role in mitigating inflation and better anchoring expectations, but interest rates are still negative in real terms and thus too low to put a break on fast-growing credit. Sustained exchange rate flexibility is needed to protect reserves and achieve a durable improvement in the current account.

31. Achieving fiscal deficit targets will hinge on mitigating budget pressures. The authorities' envisaged fiscal consolidation of 3 percent of GDP between 2018 and 2020 remains indispensable for macroeconomic stabilization. At the same time, this will be harder to achieve with higher oil prices, lower-than-expected numbers of civil servants ready to leave their jobs, and delayed pension reform. Strong revenue performance helped the fiscal accounts in the first quarter; it will now be critical to control spending, notably through monthly fuel price adjustments until the end of the year. It will also be important to maintain the policy of not granting new wage increases in 2018 and move ahead quickly with further measures to ensure the financial viability of pensions. Without these measures, it will be impossible to reduce debt and achieve the desired re-orientation of spending towards more investment and outlays on health and education.

32. Further monetary tightening is needed to decelerate inflation and guide expectations. Inflation has become broad-based during the second quarter and credit growth is expected to continue, albeit at a slower pace. The Central Bank has acted courageously to increase the cost of borrowing in an effort to reduce monetary accommodation of inflationary pressures. Additional interest rate increases during the remainder of the year, complemented with a tightening of the Central Bank's collateral framework, are warranted to bring real interest rates into positive territory and avoid risks to banking sector stability. In the absence of such action, inflation could rise above 9 percent by the end of 2018 and continue to reduce the purchasing power especially of the poor and the middle class.

33. Exchange rate flexibility has a critical role to play in achieving external balance. The real depreciation since April 2017 has helped to expand exports and compress import demand. At the same time, the current account deficit remains elevated, calling for sustained exchange rate flexibility to further re-orient demand towards exports and encourage investment. Staff welcomes the Central Bank's successful efforts over March–May to stay below the agreed ceiling for FX interventions, and urges it to move quickly to competitive FX auctions to promote market-based determination of the exchange rate and protect reserves. The impact of the exchange rate depreciation on debt ratios needs to be mitigated through a sustained tightening of macroeconomic policies.

34. The authorities' reform agenda depends on maintaining adequate social protection. The liquidity needs of the public and private pension funds remain unsustainable and call for swift adoption of legislation necessary for their reform; as well as for additional reform steps as soon as possible. Staff very much supports the broader coverage of vulnerable families benefitting from social transfers. It also calls on the authorities not to reduce subsidies on basic food stuffs. Swiftly

completing the database of vulnerable households will be necessary to improve the targeting of social services to those families who need them the most.

35. Business climate and governance reforms have started to improve conditions on the ground. The one-stop shop for investors, the StartUp Act, and the negative list that limits the number of sectors that still require investment authorization are important positive signals. This momentum should be maintained with suitable follow-up measures, including upgraded frameworks for public procurement and public private partnerships. The delays in the appointment of the members of the High Anti-Corruption Authority are disappointing and should be overcome as soon as possible to strengthen economic governance.

36. Successful efforts to reform the financial sector will bolster confidence. The adoption by Parliament of the laws supporting reduction of public banks' NPLs is a major milestone, opening the way to accelerated credit workout. The intended start of the BFT resolution and the progress realized with strengthening the AML/CFT regime are other important signals of the authorities' willingness to address banking sector issues, including risks affecting correspondent banking relationships.

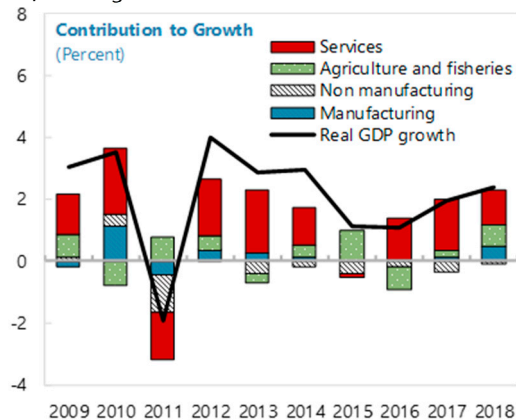
37. Program risks remain exceptionally high. Political stalemate over reforms, especially after the failure of recent efforts to revitalize a broad-based reform consensus, as well as security incidents remain the key risks that continue to threaten performance under the program. Besides, Tunisia is exposed to adverse movements in international oil prices and, to a lesser extent, investor sentiment, which jeopardize fiscal and external deficit targets. Continued close program monitoring through quarterly reviews and additional QPCs will be essential to mitigate these risks.

38. Tunisia will continue to depend on strong engagement by its international partners. Sustained sizeable fiscal financing from external partners—including in the form of grants or highly concessional loans—will remain indispensable to cover Tunisia's financing needs (about US\$3.7 billion in budget support in the three remaining quarters of 2018). Continued TA engagement remains critical to help overcome capacity constraints in upgrading policy frameworks and economic institutions.

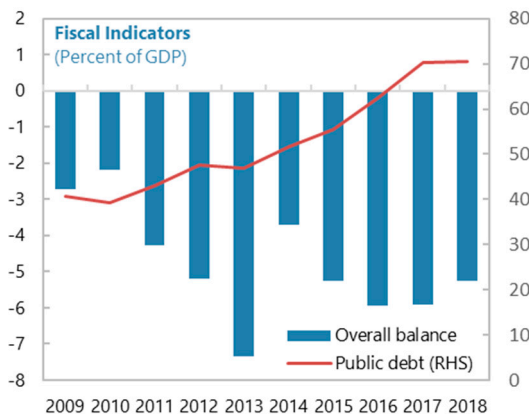
39. Staff supports the authorities' request for the completion of the Third Review under the EFF. It also supports: (1) setting revised quantitative targets for end-June, end-September, and end-December 2018, as well as new targets for end-March 2019; (2) altering the adjusters for QPCs on the primary balance and on current primary expenditures; (3) converting the IT on social spending to a QPC; (4) introducing a new QPC on FX interventions; (5) waiving the applicability of all end-June performance criteria; and (6) making all funds available for budget support.

Figure 1. Tunisia: Recent Economic Developments, 2009–18

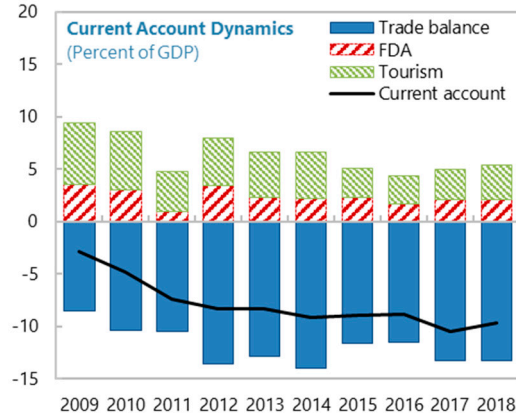
A modest recovery unfolds on the back of agriculture, manufacturing, and tourism.



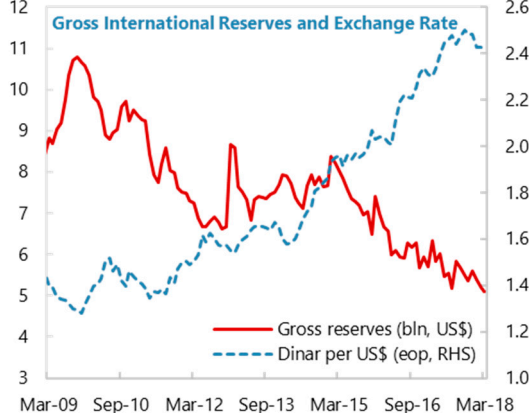
Fiscal consolidation has started in 2018.



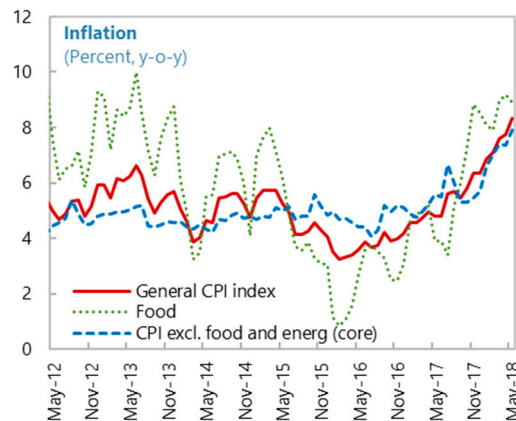
The current account is expected to improve slightly in 2018.



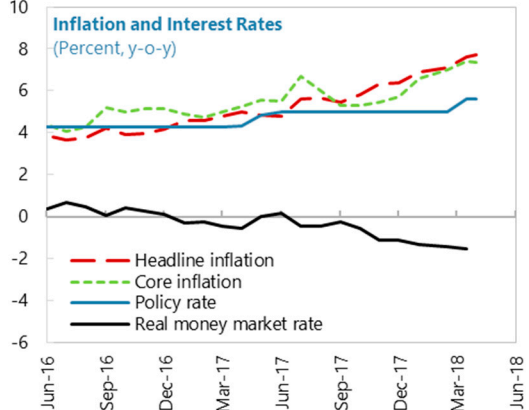
The dinar has depreciated while International reserves have declined further.



Accelerating inflation is broad-based.



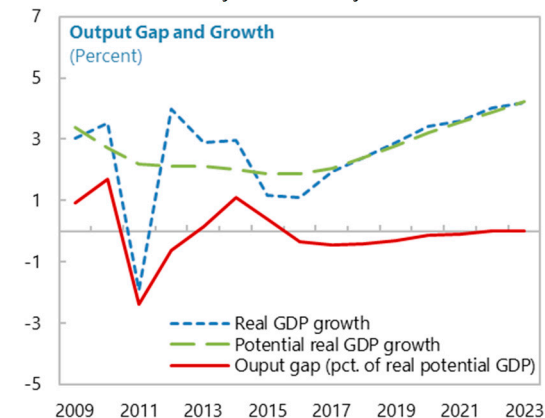
The policy rate was raised four times since early 2017, and the corridor was widened.



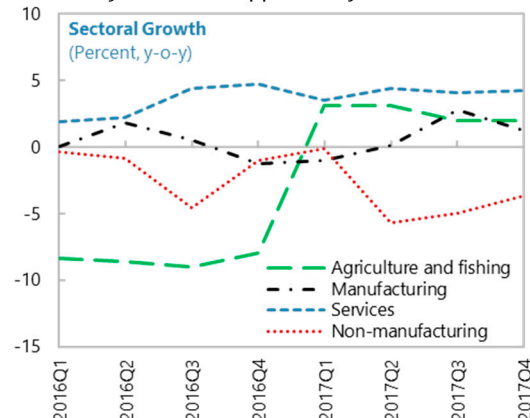
Sources: Tunisian authorities; IMF IFS, and staff calculations.

Figure 2. Tunisia: Real Sector Developments, 2009–23

A more robust recovery is underway.



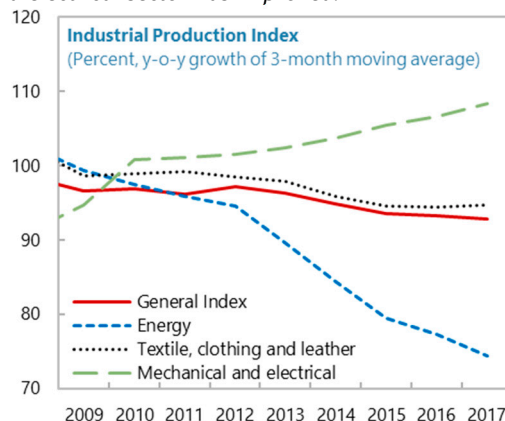
The recovery has been supported by most sectors.



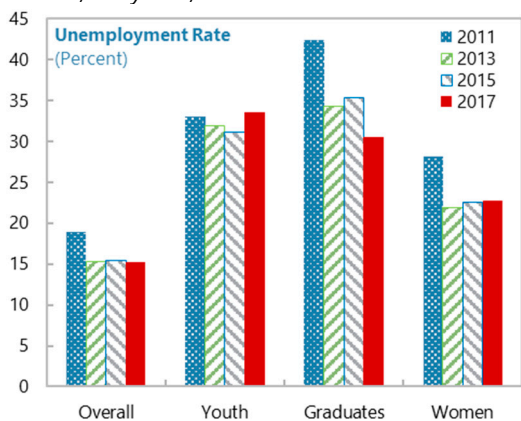
Tourism as measured by tourist arrivals continues its recovery from the shock of the 2015 terrorist attacks.



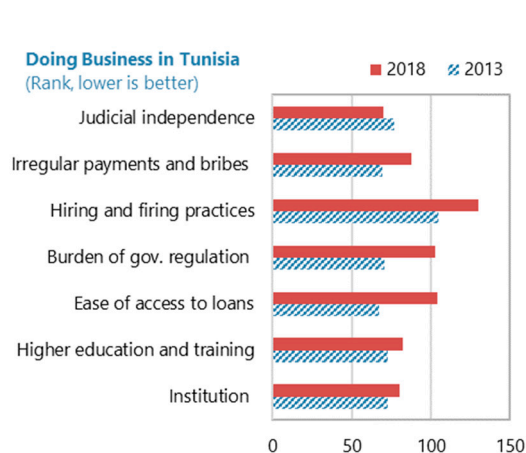
Growth of Industry remains weak, but the mechanical and electrical sector has improved.



Unemployment remains high, especially among graduates, the youth, and women.



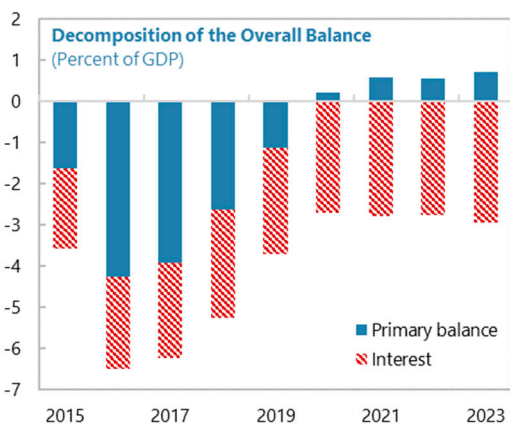
Structural reforms will help improve the business climate.



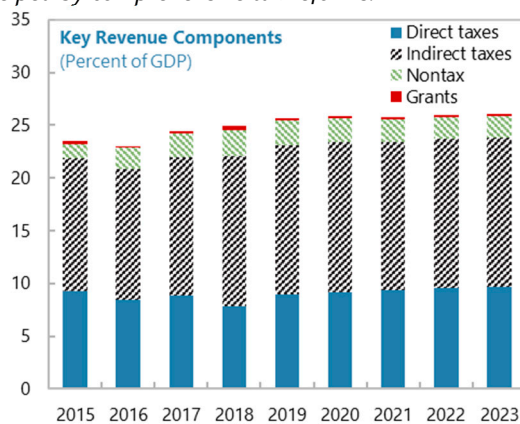
Sources: Tunisian authorities; IMF IFS; World Bank Doing Business Indicators; and staff calculations.

Figure 3. Tunisia: Fiscal Developments and Projections, 2015–23

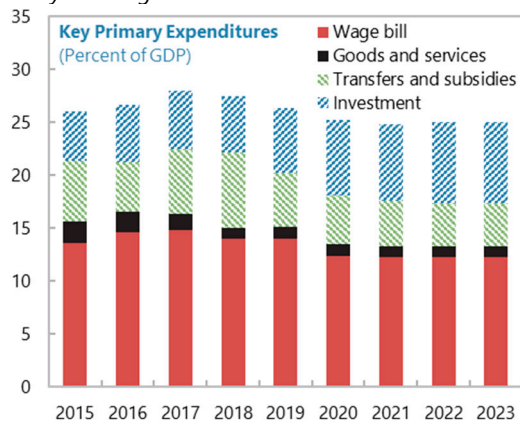
Fiscal adjustment aims at achieving a primary surplus.



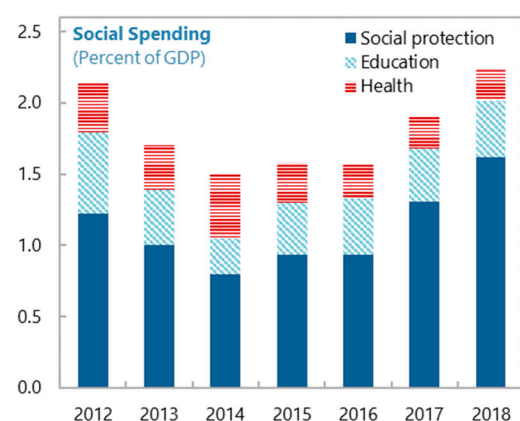
Revenues are projected to increase through 2020, helped by comprehensive tax reforms.



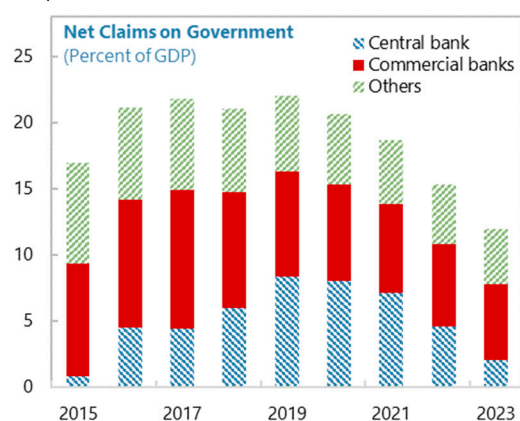
The adjustment would largely come from expenditures, notably the wage bill.



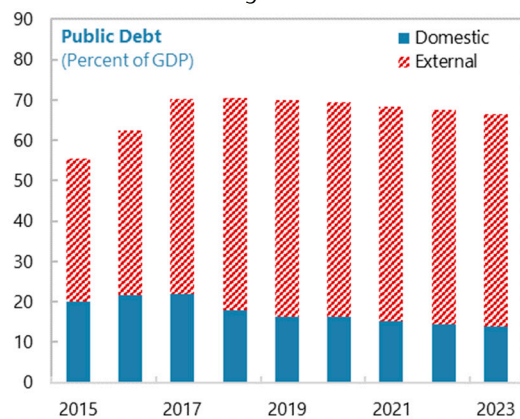
The adjustment intends to preserve social spending.



Public debt levels put pressure on banks' balance sheets, but are set to decline...



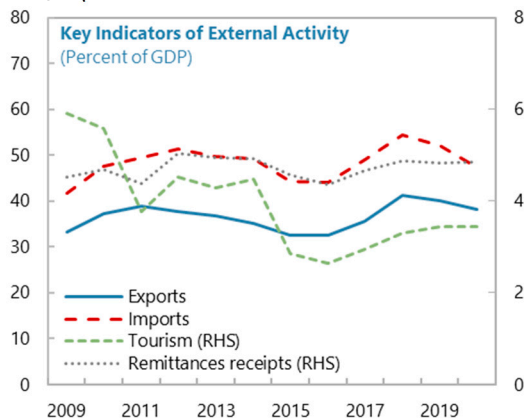
...while external borrowing stabilizes.



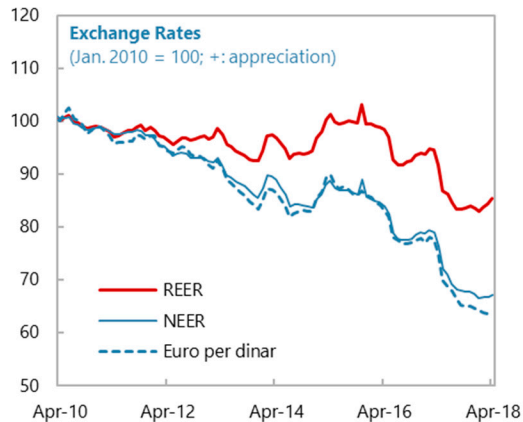
Sources: Tunisian authorities; IMF IFS; and staff calculations.

Figure 4. Tunisia: External Sector Developments, 2009–20

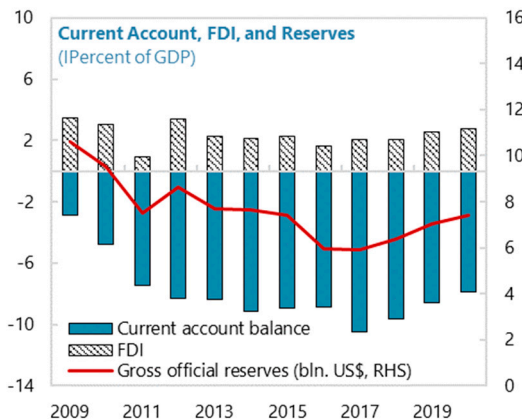
Growth of exports and tourism accelerate in 2018.



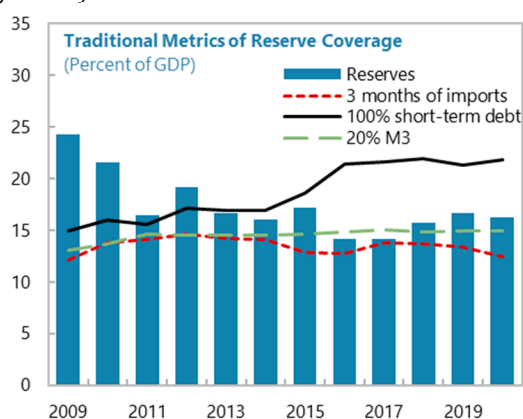
The dinar depreciated noticeably in nominal and real terms since 2016.



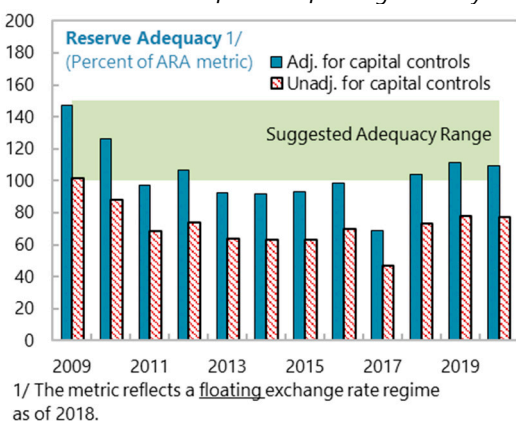
Dinar depreciation helps stabilize the current account and slow reserve losses.



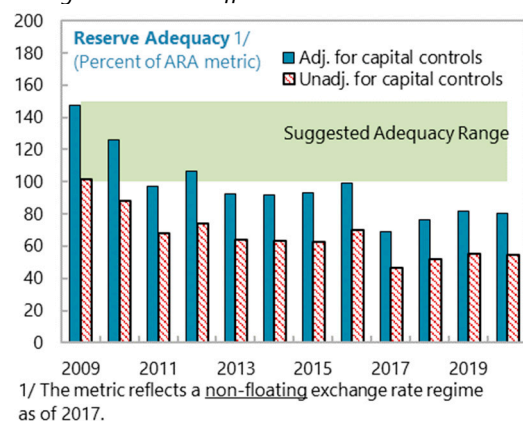
Under the baseline, reserve coverage would improve gradually and...



...return to the IMF's adequacy range by 2019, provided that the dinar remains reclassified as a floating currency.



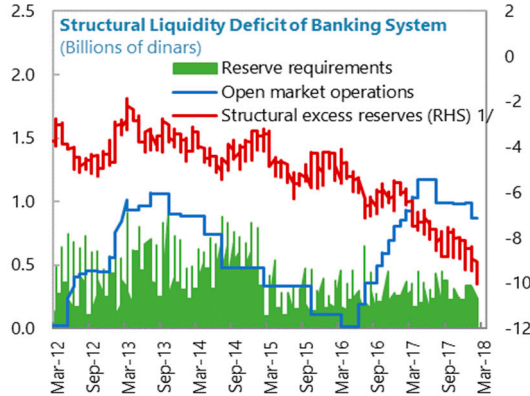
If it continues to be classified as crawl-like, reserve coverage remains insufficient.



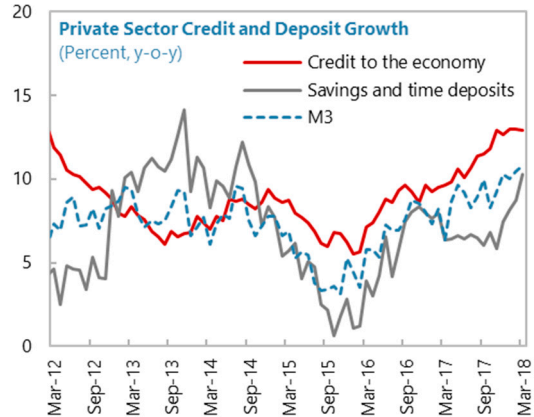
Sources: Tunisian authorities; IMF IFS, and staff calculations.

Figure 5. Tunisia: Monetary and Financial Indicators, 2012–18

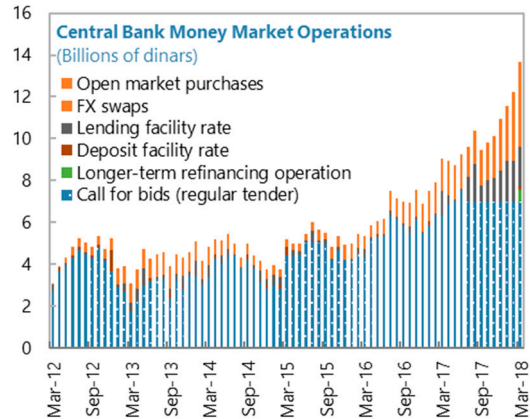
There are structural liquidity deficits in the banking system.



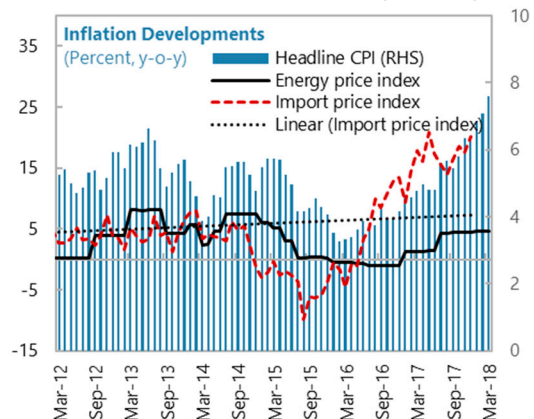
Deposit growth remains below credit growth.



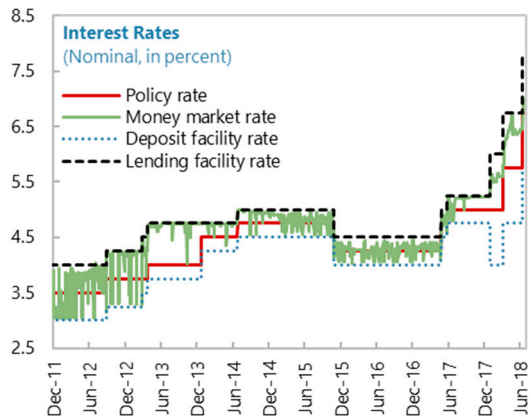
Credit growth was facilitated by record-level CBT bank refinancing.



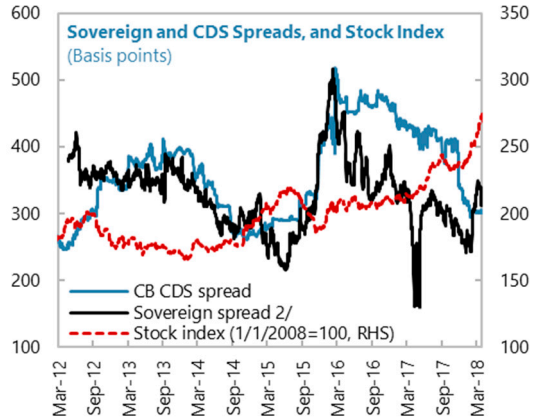
Which, combined with other drivers, has fueled inflation.



In response, the CBT raised the policy rate several times and widened the interest rate corridor.



Spreads are down and the stock market is up.



Sources: Tunisian authorities; Bloomberg; Markit; IMF IFS; and staff calculations.

1/ Deposit facility minus reserve requirements. 2/ Between the Tunisian and US' five-year bonds. The decrease in yields during the first half of 2017 is a result of the April refinancing of the US\$-denominated 5-year Qatari-backed bond and increases in Federal Reserve fund rates.

Table 1. Tunisia: Selected Economic and Financial Indicators, 2015–23

	2015	2016	2017	2018		2019		2020	2021	2022	2023
				Proj.	Prog.	Proj.	Prog.				
Production and income											
	(Annual percentage change)										
Real GDP	1.2	1.1	2.0	2.4	2.4	2.9	2.9	3.4	3.6	4.0	4.2
GDP deflator	3.6	4.7	5.8	7.3	6.4	7.0	5.6	5.2	5.0	4.0	3.8
CPI inflation (average)	4.9	3.7	5.3	8.1	7.0	7.5	6.1	5.9	4.9	4.1	4.0
CPI inflation (eop)	4.1	4.2	6.4	8.9	6.5	6.2	5.9	5.7	4.3	4.0	4.0
Saving investment balance											
	(Percent of GDP)										
Gross national savings	12.5	13.4	12.0	13.4	14.0	14.6	15.7	15.7	17.0	18.1	18.5
<i>of which: central government</i>	0.3	-0.5	-0.4	0.0	-0.2	2.4	2.4	4.7	5.1	5.4	5.5
Gross investment	21.4	22.3	22.5	23.1	23.1	23.1	23.5	23.5	23.9	24.6	24.6
<i>of which: central government</i>	4.7	5.4	5.5	5.3	5.0	6.1	5.8	7.2	7.3	7.6	7.7
Central government operations 1/											
	(Percent of GDP, unless otherwise indicated)										
Total revenue (excl. grants)	23.2	22.9	24.2	24.5	24.6	25.4	25.7	25.6	25.6	25.8	25.9
Total expenditure and net lending	28.8	28.9	30.3	30.1	30.1	29.3	29.3	28.3	28.0	28.2	28.3
<i>of which: wage bill</i>	13.6	14.6	14.8	14.0	14.3	14.0	14.0	12.4	12.2	12.2	12.2
<i>of which: social expenditures 2/</i>	1.6	1.6	1.9	2.2	1.9	2.2	1.9	2.2	2.2	2.2	2.2
Overall balance	-5.3	-5.9	-5.9	-5.2	-5.2	-3.7	-3.4	-2.5	-2.2	-2.2	-2.2
Change in the overall balance ("+" improvement)	-1.5	-0.7	0.0	0.7	0.7	1.5	1.8	1.2	0.3	0.0	0.0
Gross public debt	55.4	62.4	70.3	70.5	73.1	70.0	73.3	69.4	68.4	67.5	66.5
<i>of which: share in foreign currency</i>	35.3	40.6	48.4	52.7	52.6	53.6	54.4	53.1	53.1	53.0	52.5
Money and credit											
	(Annual percentage change, unless otherwise indicated)										
Credit to the economy	6.2	9.7	12.7	7.6	9.0	5.6	8.7	6.6	6.7	6.5	6.1
Broad money	5.3	8.1	10.3	7.5	7.4	6.6	9.1	8.2	9.2	9.0	8.2
Velocity of circulation (GDP/M3)	1.4	1.3	1.3	1.3	1.4	1.4	1.4	1.4	1.4	1.4	1.4
External sector											
Trade balance (pct. of GDP)	-11.7	-11.5	-13.3	-13.3	-13.0	-12.1	-12.2	-11.3	-10.6	-10.0	-9.5
Exports of goods (value)	-15.9	-3.6	4.9	20.6	-1.0	-1.4	3.4	-0.1	1.1	3.5	3.4
Imports of goods (value)	-18.4	-3.8	6.3	16.2	-1.3	-3.0	1.9	-0.5	0.6	2.7	2.7
Exports of goods (volume)	-2.8	0.2	4.6	6.2	8.9	4.6	4.6	3.4	4.1	3.6	3.7
Import of goods (volume)	-2.5	2.3	2.8	-1.0	-1.1	1.7	1.6	2.4	3.3	3.3	4.3
Terms of trade (pct. change, "-": deterioration)	3.3	2.3	-3.1	-2.2	-8.3	-1.3	-1.7	-0.4	-0.2	0.6	1.3
Current account balance (pct. of GDP)	-8.9	-8.9	-10.5	-9.6	-9.2	-8.6	-7.8	-7.8	-6.9	-6.5	-6.1
Foreign direct investment (net, pct. of GDP)	2.2	1.7	2.0	2.0	2.0	2.5	2.5	2.8	3.0	3.3	3.4
Reserve coverage (months of next year's imports of goods)	4.8	3.6	3.1	3.5	3.4	3.8	3.7	4.1	4.2	4.5	4.8
Gross official reserves (eop, billions of US\$)	7.4	5.9	5.9	6.4	6.3	7.0	7.0	7.5	7.9	8.7	9.3
Net international reserves (eop, billions of US\$)	4.5	3.3	3.1	3.2	3.2	3.2	3.2	3.3	3.7	4.7	5.6
External debt (pct. of GDP)	62.8	67.6	80.1	86.4	83.7	88.9	85.5	89.3	88.3	85.8	82.9
External debt service (pct. of exports of GNFS)	10.1	12.3	19.1	17.1	16.0	18.9	18.8	16.3	18.0	14.2	14.4
Memorandum items:											
Population (millions)	11.1	11.3	11.4	11.5	11.6	11.7	11.8	11.8	11.9	12.0	12.1
Nominal GDP (millions of TD)	84,656	89,581	96,661	106,159	106,179	116,898	115,386	127,201	138,353	149,595	161,791
Nominal GDP (billions of US\$)	43.2	41.7	40.0	...	...	...	...	...	...	...	...
GDP per capita (US\$)	3,873	3,699	3,504	3,612	3,463	3,625	3,569	3,748	3,915	4,102	4,308
Unemployment rate (pct.)	14.9	15.6	15.3	...	...	...	...	...	...	...	...
Exchange rate (TD/US\$, average)	2.0	2.1	2.4	...	...	...	...	...	...	...	...
Oil price (Brent, US\$ per barrel)	52.4	44.0	54.4	70.0	62.0	60.7	63.9	58.0	56.6	56.2	56.2

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

1/ Excludes social security accounts, public enterprises, and local governments.

2/ Social spending includes social transfers and programs as well as key ministries' capital expenditures. Its coverage was expanded in 2017.

Table 2. Tunisia: Real Sector, 2015–23
(In percent)

	2015	2016	2017	2018	2019	2020	2021	2022	2023
						Proj.			
Real GDP growth									
Chain index method 1/	0.8	1.0	1.9	2.4	2.9	3.4	3.6	4.0	4.2
Constant 2010 prices	1.2	1.1	2.0	2.4	2.9	3.4	3.6	4.0	4.2
Per capita	0.0	-0.1	0.8	1.3	1.8	2.3	2.6	3.0	3.3
Inflation									
CPI (eop)	4.1	4.2	6.4	8.9	6.2	5.7	4.3	4.0	4.0
CPI (average)	4.9	3.7	5.3	8.1	7.5	5.9	4.9	4.1	4.0
GDP deflator	3.6	4.7	5.8	7.3	7.0	5.2	5.0	4.0	3.8
Contributions to growth (supply; constant 2010 prices)									
Total added value	1.0	0.8	1.6	2.1	2.6	3.1	3.3	3.6	3.8
Sectors	0.4	0.3	1.5	2.1	2.1	2.5	2.6	2.9	3.1
Agriculture	1.0	-0.8	0.2	0.7	0.3	0.3	0.3	0.4	0.4
Manufacturing	0.0	0.0	0.1	0.5	0.4	0.5	0.5	0.6	0.6
Non-manufacturing	-0.4	-0.2	-0.3	-0.1	0.2	0.3	0.3	0.3	0.3
<i>of which: oil and gas extraction</i>	-0.2	-0.2	-0.4	-0.1	0.1	0.1	0.1	0.1	0.1
Services	-0.2	1.4	1.7	1.1	1.2	1.4	1.5	1.7	1.8
<i>of which: hotels and restaurants</i>	-0.5	0.1	0.3	0.2	0.1	0.1	0.1	0.2	0.2
<i>of which: transport</i>	-0.2	0.3	0.4	0.3	0.2	0.3	0.3	0.3	0.3
Intermediary consumption (in - terms)	-0.1	-0.1	-0.2	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1
Public administration	0.6	0.4	0.1	0.1	0.5	0.6	0.6	0.7	0.7
Indirect taxes net of subsidies	0.2	0.3	0.4	0.3	0.3	0.3	0.3	0.4	0.4
Contributions to growth (demand; constant 2010 prices)									
Consumption	1.8	2.2	0.0	...	...	...	...	...	...
Private	0.6	0.7	-0.2	...	...	...	...	...	...
Public	1.1	1.4	0.2	...	...	...	...	...	...
Investment	-1.7	0.3	0.8	...	...	...	...	...	...
Private	0.0	0.2	0.6	...	...	...	...	...	...
Public	0.0	0.1	0.2	...	...	...	...	...	...
Change in stocks	-1.7	0.0	0.0	...	...	...	...	...	...
Net exports	1.1	-1.3	1.1	...	...	...	...	...	...
Exports	-0.3	-0.1	2.6	...	...	...	...	...	...
Imports	-1.4	1.2	1.5	...	...	...	...	...	...

Sources: Tunisia authorities, and IMF staff projections.

1/ Output measured using current and previous year prices.

Table 3. Tunisia: Balance of Payments, 2015–19 1/
(In millions of U.S. dollars, unless otherwise indicated)

	2015		2016		2017		2018					2019						
	Annual	Annual	Annual	Annual	Annual	Annual	Q1	Q2	Q3	Q4	Annual	Annual	Q1	Q2	Q3	Q4	Annual	Annual
							Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	-3,849	-3,694	-4,191	-1,247	-1,168	-742	-854	-4,010	-3,689	-815	-1,228	-723	-850	-3,616	-3,273			
Trade balance	-5,029	-4,806	-5,308	-1,187	-1,405	-1,608	-1,344	-5,544	-5,236	-1,032	-1,559	-1,471	-1,033	-5,096	-5,135			
Exports	14,073	13,568	14,231	4,176	4,577	3,905	4,499	17,158	13,784	4,341	4,187	3,860	4,529	16,916	14,250			
Energy	1,013	765	846	235	218	227	356	1,037	1,022	253	191	206	274	924	1,082			
Non-energy	13,061	12,804	13,384	3,941	4,359	3,678	4,143	16,121	12,762	4,087	3,996	3,654	4,255	15,992	13,168			
of which: non-food	11,017	11,368	11,844	3,270	3,788	3,295	3,778	14,131	11,324	4,087	3,996	3,654	4,255	13,870	11,633			
Imports	-19,102	-18,374	-19,538	-5,363	-5,982	-5,513	-5,843	-22,702	-19,020	-5,373	-5,746	-5,331	-5,562	-22,012	-19,385			
Energy	-2,742	-2,024	-2,513	-802	-933	-899	-844	-3,479	-2,455	-767	-828	-823	-725	-3,143	-2,575			
Non-energy	-16,361	-16,351	-17,025	-4,561	-5,049	-4,614	-4,999	-19,224	-16,565	-4,606	-4,918	-4,507	-4,837	-18,868	-16,810			
of which: non-food	-14,452	-14,567	-15,101	-4,025	-4,536	-4,114	-4,422	-17,096	-14,686	-4,606	-4,918	-4,507	-4,837	-16,492	-14,630			
Services and transfers (net)	1,180	1,112	1,117	-60	237	866	491	1,534	1,547	218	331	748	184	1,480	1,862			
Services	303	320	359	-96	84	495	137	619	532	54	102	400	2	558	602			
of which: tourism	1,231	1,105	1,175	187	241	629	316	1,373	1,160	252	331	548	319	1,452	1,261			
Transfers (net)	877	792	758	36	153	372	354	915	1,015	164	229	348	182	922	1,260			
of which: workers' remittances	1,945	1,794	1,835	405	488	591	514	2,005	1,879	436	480	600	491	2,008	1,942			
of which: interest payments on external debt	-556	561	-649	-233	-245	-123	-142	-743	-603	-217	-211	-196	-201	-874	-523			
of which: IMF	0	16	25					34	33					55	50			
Capital and financial account	4,252	3,629	4,167	800	1,590	989	1,063	4,464	4,333	1,006	1,027	1,077	1,137	4,248	3,915			
Capital account balance	225	95	140	5	-4	66	59	125	121	-4	-4	40	40	72	83			
Financial account balance	4,027	3,534	4,028	795	1,594	923	1,004	4,339	4,212	1,011	1,032	1,037	1,097	4,176	3,833			
Direct investment and portfolio (net)	1,122	638	746	169	172	208	264	812	226	209	253	256	344	1,061	1,033			
Medium- and long-term loans (net)	2,362	1,035	2,238	189	975	696	752	2,636	2,409	338	319	326	304	1,288	1,466			
Disbursements	3,572	2,514	4,528	680	1,499	1,161	1,355	4,717	4,475	951	943	934	922	3,750	3,908			
of which: private	763	645	620	144	141	135	169	589	583	142	140	139	137	558	575			
Amortization	-1,210	-1,479	-2,289	-490	-524	-464	-603	-2,082	-2,067	-613	-623	-607	-618	-2,462	-2,442			
Short-term capital	543	1,861	1,043	-11	132	15	-75	62	437	141	140	138	136	555	1,097			
Other investment (net)	...	...	...	447	315	4	63	829	570	323	320	317	313	1,272	237
Errors and omissions 2/	-4	-1	0	0	0	0	0	0	0	0	0	0	0	0	0			
Overall balance	399	-66	-23	-446	422	247	209	454	644	192	-201	354	288	633	642			
Changes in gross reserves ("+"= accumulation)	385	-489	-23	-446	422	247	209	454	644	192	-201	354	288	633	642			
of which: IMF credit (net)	299	282	0	113	-143	132	132	234	485	158	158	158	159	633	622			
Purchases	301	316	315	256	0	258	258	771	1,014	258	259	259	259	1,035	1,017			
Repurchases	0	34	315	137	137	119	119	537	530	100	100	100	100	402	395			
Financing gap	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Memorandum items:																		
Current account balance (pct. of GDP)	-8.9	-8.9	-10.5	-3.0	-2.8	-1.8	-2.0	-9.6	-9.2	-1.9	-2.9	-1.7	-2.0	-8.6	-7.8			
Capital and financial account balance (pct. of GDP, excl. grants)	9.3	8.4	10.0	1.9	4.0	2.1	2.4	10.4	10.4	2.3	2.4	2.5	2.6	9.8	9.1			
Imports (pct. of GDP)	44.3	44.1	48.9	52.4	60.3	51.4	55.0	54.7	47.2	50.1	54.0	50.6	53.5	52.1	46.2			
Goods import real growth (pct.)	-2.5	2.3	2.8	0.3	-2.4	1.3	-2.9	-1.0	-1.1	-2.3	7.0	-1.7	3.8	1.7	1.6			
of which: non-energy (pct.)	-1.9	5.0	2.1	-3.6	-2.7	1.1	-3.7	-2.3	-0.3	0.0	0.0	0.0	0.0	1.6	1.6			
Exports (pct. of GDP)	32.6	32.5	35.6	40.8	46.1	36.4	42.3	41.3	34.2	40.5	39.4	36.7	43.6	40.0	34.0			
Goods export real growth (pct.)	-2.8	0.2	4.6	12.7	10.0	2.6	0.8	6.2	8.9	6.1	-2.4	1.2	13.8	4.6	4.6			
of which: non-energy (pct.)	0.0	1.7	4.2	9.9	11.9	4.2	3.4	7.1	9.4	5.5	-0.5	5.0	9.2	4.8	4.7			
Gross reserves (billions of US\$)	7.4	5.9	5.9	5.5	5.9	6.2	6.4	6.4	6.3	6.6	6.4	6.7	7.0	7.0	7.0			
Reserve coverage (months of next year's imports of goods)	4.8	3.6	3.1	3.0	3.2	3.4	3.5	3.5	3.4	3.6	3.5	3.7	3.8	3.8	3.7			
Reserve coverage (months of next year's imports of GNFS)	4.1	3.2	2.7	2.6	2.8	2.9	3.0	3.0	3.4	3.1	3.0	3.2	3.3	3.3	3.7			
Reserve coverage (pct. of short-term external debt) 3/	112.7	88.8	89.1	78.7	87.3	92.1	97.7	93.5	98.8	94.5	89.8	93.1	95.7	97.1	102.0			
Reserve coverage (pct. of short-term debt, on remaining maturity)	95.7	73.8	62.9	59.1	61.6	64.6	62.5	71.2	80.9	60.9	62.3	0.0	0.0	78.0	87.4			
Net international reserves (eop, billions of US\$)	n.a.	3.7	3.1	2.4	3.0	3.1	3.2	3.2	3.2	3.2	2.8	3.0	3.2	3.2	3.2			
External medium- and long-term debt (billions of US\$)	20.5	21.3	25.3	26.4	27.5	28.2	28.9	28.9	25.7	29.3	29.7	30.1	30.5	30.5	27.4			
External medium- and long-term debt (pct. of GDP)	47.5	51.5	63.3	60.3	66.0	70.1	73.9	69.0	67.0	68.6	70.2	72.0	74.0	71.4	68.4			
External short-term debt (billions of US\$)	6.6	6.7	6.7	7.0	6.8	6.7	6.5	6.8	6.4	7.0	7.1	7.2	7.3	7.2	6.8			
External short-term debt (pct. of GDP)	15.3	16.1	16.8	15.9	16.3	16.6	16.7	17.4	16.7	16.3	16.8	17.3	17.8	17.5	17.1			
External debt service ratio (incl. IMF, pct. of exports of GNFS)	10.1	12.3	19.1	18.7	17.6	14.6	7.4	17.1	18.5	18.8	19.1	18.7	17.8	18.9	18.8			
Nominal GDP (millions of US\$)	43,156	41,704	39,956	...	...	...	...	...	...	...	...	...	...	...	...

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

1/ In accordance with the Fifth Edition of the Balance of Payments and Investment Position Manual (BPM5).

2/ Differs from zero in current and future years because of stocks valuation effects.

3/ Short-term defined as one year or less remaining maturity.

Table 4. Tunisia: External Financing Needs, 2015–19
(In millions of U.S. dollars, unless otherwise indicated)

	2015	2016	2017	2018					2019				
	Annual	Annual	Annual	Q1	Q2	Q3	Q4	Annual	Q1	Q2	Q3	Q4	Annual
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total financing requirements	11,623	12,319	13,165	8,587	8,338	7,959	8,110	12,749	8,402	8,618	8,016	7,993	12,900
Current account deficit	3,849	3,694	4,191	1,247	1,168	742	854	4,010	815	1,228	723	850	3,616
Amortizations	1,209	1,931	2,280	490	524	464	599	2,082	613	623	607	618	2,455
Central government 1/	599	1,079	1,486	314	308	295	373	1,293	465	461	456	450	1,831
Central Bank 2/	85	375	105	23	21	6	4	53	5	0	0	0	4
Corporate 3/	525	477	690	154	195	163	221	737	144	163	151	168	620
Short-term debt 4/	6,565	6,694	6,694	6,851	6,646	6,753	6,657	6,657	6,974	6,767	6,685	6,526	6,829
Total financing sources	11,623	12,319	13,165	8,587	8,338	7,959	8,110	12,749	8,402	8,618	8,016	7,993	12,900
Foreign direct investment and portfolio (net)	1,122	638	746	169	172	208	281	812	209	253	256	344	1,061
Other investment (net)	-286	129	118	447	315	4	63	829	323	320	317	313	1,272
Disbursements	3,558	3,581	4,427	680	1,499	1,161	1,355	4,717	951	943	934	922	3,750
Central government 1/	2,771	2,952	3,488	536	1,358	1,026	1,187	4,129	810	802	795	785	3,191
Central Bank 2/	25	0	317	0	0	0	0	0	0	0	0	0	0
Corporate 3/	762	629	622	144	141	135	168	589	142	140	139	137	558
Short-term debt 4/	6,565	6,694	6,657	6,974	6,767	6,685	6,526	6,829	6,965	7,103	7,232	7,332	7,232
Other flows net (incl. drawdown in commercial banks NFA)	1,063	1,211	1,192	-129	7	148	94	15	145	-201	-369	-630	217
Drawdown in gross reserves	-399	66	23	446	-422	-247	-209	-454	-192	201	-354	-288	-633
Financing gap	0	0	0	0	0	0	0	0	0	0	0	0	0
of which: multi- and bilateral budget support (excl. IMF)	1,516	576	2,138	188	244	656	504	1,597	0	40	595	145	780
of which: financial market access and other	88	979	1,281	104	1,104	104	604	1,916	104	104	104	1,154	1,466
of which: IMF credit (net) 5/	301	282	0	119	-137	138	138	234	158	159	159	159	633
Purchases	301	316	315	256	0	258	258	771	258	259	259	259	1,035
Repurchase	0	34	315	137	137	119	119	537	100	100	100	100	402
Memorandum items:													
Gross international reserves (eop)	7,401	5,941	5,934	5,488	5,910	6,157	6,373	6,388	6,580	6,379	6,733	7,021	7,021
Government rollover rates (pct.)	467	170	264	171	442	348	318	63	171	170	0	0	0
Corporate rollover rates (pct.)	145	132	90	93	72	83	76	80	98	86	92	82	90

Sources: Tunisian authorities; and IMF staff projections.

1/ Central government includes IMF purchases made available for budget support.

2/ Central Bank includes IMF purchases made available for BOP support.

3/ Includes public and private enterprises.

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

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

Table 5. Tunisia: Central Government Fiscal Operations, 2015–19
(In millions of dinars, cumulative flow since the beginning of the year)

	2015	2016	2017	2018					2019				
	Annual	Annual	Annual	Q1	Q2	Q3	Annual	Annual	Q1	Q2	Q3	Annual	Annual
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	19,945	20,619	23,582	6,665	12,460	19,443	26,426	26,466	7,425	14,849	22,398	29,948	29,938
Revenue	19,653	20,489	23,396	6,663	12,457	19,259	26,061	26,101	7,425	14,849	22,274	29,699	29,663
Tax revenue	18,487	18,702	21,187	5,801	11,390	17,424	23,459	23,821	6,753	13,506	20,260	27,013	27,242
Direct taxes	7,816	7,577	8,560	2,146	4,440	6,358	8,277	8,457	2,604	5,208	7,811	10,415	10,599
Trade taxes	825	640	742	245	512	899	1,286	1,304	349	698	1,047	1,395	1,415
VAT	5,057	5,138	6,092	1,634	3,101	5,091	7,081	7,139	1,887	3,773	5,660	7,546	7,520
Excise	1,773	2,174	2,493	646	1,271	2,161	3,051	3,101	851	1,702	2,553	3,404	3,447
Other indirect taxes	3,016	3,174	3,300	1,130	2,067	2,916	3,765	3,820	1,063	2,126	3,189	4,252	4,261
Nontax revenue	1,162	1,776	2,209	862	1,067	1,835	2,602	2,276	670	1,341	2,011	2,682	2,416
<i>of which: Energy sector</i>	150	0	500	3,248	4,022	6,913	1,148	600	2,294	4,589	6,883	1,081	623
Capital income	4	11	0	0	0	0	0	4	1	2	3	4	4
Grants	292	130	187	2	2	184	365	365	0	0	124	249	275
Total expenditure and net lending	24,395	25,930	29,303	7,742	17,257	24,332	31,999	32,001	8,572	17,053	25,534	34,287	33,833
Total expenditure	23,675	25,839	29,342	7,500	16,605	24,332	32,059	32,061	8,576	17,061	25,546	34,303	33,850
Current expenditure	19,732	21,040	23,997	6,104	13,355	19,879	26,403	26,718	6,785	13,479	20,173	27,141	27,120
Wages and salaries	11,542	13,117	14,352	3,864	7,668	11,257	14,846	15,204	4,100	8,200	12,300	16,400	16,134
<i>of which: one-off civil service reform costs</i>	0	0	0	0	0	0	95	803	107	214	321	428	536
<i>of which: Ministry of Defense and Interior</i>	2,752	3,100	3,265	...	...	...	3,531	3,493	...	...	...	3,796	3,705
Goods and services	1,682	1,737	1,498	292	551	851	1,150	1,550	317	633	950	1,266	1,684
Interest payments	1,644	1,986	2,259	919	1,838	2,313	2,787	2,787	753	1,506	2,258	3,011	2,936
Domestic	687	821	1,255	461	921	1,229	1,537	1,537	290	579	869	1,159	1,170
External	957	1,165	1,004	458	917	1,083	1,250	1,250	463	926	1,389	1,853	1,766
Transfers and subsidies	4,864	4,200	5,888	1,029	3,280	5,415	7,550	6,808	1,507	3,014	4,522	6,029	5,935
Subsidies	2,863	2,211	3,492	520	1,894	3,310	4,726	4,109	826	1,652	2,478	3,304	3,484
Food	1,530	1,581	1,494	173	854	1,212	1,570	1,570	483	966	1,448	1,931	1,781
Energy subsidies (gross)	918	197	1,550	220	820	1,763	2,706	2,089	219	439	658	878	1,214
Other	415	433	448	127	220	335	450	450	124	248	372	496	489
Transfers (incl. CNRPS, social protection, and BFT)	2,001	1,989	2,395	510	1,386	2,105	2,824	2,699	681	1,362	2,043	2,725	2,451
Other current expenditure (non-allocated)	0	0	0	0	18	44	70	369	108	126	143	434	431
Capital expenditure	3,943	4,798	5,345	1,396	3,250	4,453	5,656	5,343	1,791	3,581	5,372	7,163	6,729
Net lending	720	91	-39	242	652	0	-60	-60	-4	-8	-12	-16	-16
Overall balance	-4,451	-5,311	-5,720	-1,077	-4,797	-4,889	-5,573	-5,535	-1,147	-2,203	-3,136	-4,339	-3,896
Errors and omissions	1,421	-497	-311	706	0	0	0	0	0	0	0	0	0
Financing (net)	3,029	5,808	6,031	371	4,797	4,889	5,573	5,535	1,147	2,203	3,136	4,339	3,896
Foreign financing	4,284	2,631	5,070	542	3,155	5,051	7,228	6,791	940	1,880	2,820	3,760	4,176
Domestic financing	-1,254	3,176	962	-170	1,642	-161	-1,655	-1,256	207	323	316	580	-280
Debt	590	2,059	1,552	198	999	-176	-2,255	-1,156	146	-15	286	-30	-230
Non-debt	-1,844	1,118	-590	-368	643	15	600	-100	61	338	30	610	-50
Financing gap	0	0	0	0	0	0	0	0	0	0	0	0	0
Memorandum items:													
Overall balance (excl. grants)	-4,743	-5,441	-5,907	-1,079	-4,799	-5,073	-5,938	-5,900	-1,147	-2,203	-3,259	-4,588	-4,171
Overall balance (cash basis)	-3,029	-5,808	-6,031	-371	-4,797	-4,889	-5,573	-5,535	-1,147	-2,203	-3,136	-4,339	-3,896
Overall balance (excl. grants, cash basis)	-3,321	-5,937	-6,218	-374	-4,799	-5,073	-5,938	-5,900	-1,147	-2,203	-3,259	-4,588	-4,171
Structural balance	-2,453	-3,445	-4,209	...	...	...	-3,912	-4,683	...	...	...	-2,262	-3,896
Cyclically-adjusted structural balance	-4,171	-5,387	-6,774	...	...	...	-5,743	-4,522	...	...	...	-4,077	-3,626
Total current primary expenditure	18,088	19,054	21,738	5,185	11,517	17,566	23,616	23,931	6,032	11,974	17,915	24,129	24,184
Social expenditures 1/	1,335	1,411	1,844	735	1,144	1,766	2,382	2,041	656	1,311	1,967	2,623	2,218
Gross public debt	46,920	55,922	67,982	...	...	...	74,854	77,621	...	...	...	81,826	84,595
Domestic	17,028	19,508	21,155	...	...	...	18,861	21,721	...	...	...	19,194	21,787
External	29,892	36,414	46,828	...	...	...	55,993	55,900	...	...	...	62,632	62,808
Stock of government deposits	2,676	1,683	2,535	2,736	2,092	2,078	2,435	2,635	2,373	2,035	2,005	1,875	2,735
Nominal GDP	84,656	89,581	96,661	26,540	26,540	26,540	106,159	106,179	29,225	29,225	29,225	116,898	115,386

Sources: Tunisian authorities; and IMF staff estimates.

1/ Social spending includes social transfers and programs as well as key ministries' capital expenditures. The definition was expanded in 2017.

Table 6. Tunisia: Central Government Fiscal Operations, 2015–23
(In percent of GDP)

	2015	2016	2017	2018		2019		2020	2021	2022	2023
				Proj.	Prog.	Proj.	Prog.				
Total revenue and grants	23.6	23.0	24.4	24.9	24.9	25.6	25.9	25.8	25.8	26.0	26.1
Revenue	23.2	22.9	24.2	24.5	24.6	25.4	25.7	25.6	25.6	25.8	25.9
Tax revenue	21.8	20.9	21.9	22.1	22.4	23.1	23.6	23.4	23.4	23.7	23.8
Direct taxes	9.2	8.5	8.9	7.8	8.0	8.9	9.2	9.2	9.3	9.5	9.7
Trade taxes	1.0	0.7	0.8	1.2	1.2	1.2	1.2	1.1	1.1	1.1	1.1
VAT	6.0	5.7	6.3	6.7	6.7	6.5	6.5	6.5	6.4	6.5	6.5
Excise	2.1	2.4	2.6	2.9	2.9	2.9	3.0	2.9	2.9	2.9	2.9
Other indirect taxes	3.6	3.5	3.4	3.5	3.6	3.6	3.7	3.7	3.7	3.7	3.7
Nontax revenue	1.4	2.0	2.3	2.5	2.1	2.3	2.1	2.2	2.2	2.1	2.1
<i>of which: Energy sector</i>	0.2	0.0	0.5	1.1	0.6	0.9	0.5	0.8	0.8	0.7	0.7
Capital income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	0.3	0.1	0.2	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Total expenditure and net lending	28.8	28.9	30.3	30.1	30.1	29.3	29.3	28.3	28.0	28.2	28.3
Total expenditure	28.0	28.8	30.4	30.2	30.2	29.3	29.3	28.3	28.0	28.2	28.3
Current expenditure	23.3	23.5	24.8	24.9	25.2	23.2	23.5	21.1	20.7	20.5	20.6
Wages and salaries	13.6	14.6	14.8	14.0	14.3	14.0	14.0	12.4	12.2	12.2	12.2
<i>of which: one-off civil service reform costs</i>	0.0	0.0	0.0	0.1	0.8	0.4	0.5	0.0	0.0	0.0	0.0
Goods and services	2.0	1.9	1.5	1.1	1.5	1.1	1.5	1.1	1.1	1.1	1.1
Interest payments	1.9	2.2	2.3	2.6	2.6	2.6	2.5	2.7	2.8	2.8	2.9
Domestic	0.8	0.9	1.3	1.4	1.4	1.0	1.0	0.9	0.9	0.7	0.8
External	1.1	1.3	1.0	1.2	1.2	1.6	1.5	1.8	1.9	2.0	2.1
Transfers and subsidies	5.7	4.7	6.1	7.1	6.4	5.2	5.1	4.5	4.3	4.1	4.0
Subsidies	3.4	2.5	3.6	4.5	3.9	2.8	3.0	2.2	2.0	1.9	1.8
Food	1.8	1.8	1.5	1.5	1.5	1.7	1.5	1.6	1.5	1.4	1.4
Energy subsidies (gross)	1.1	0.2	1.6	2.5	2.0	0.8	1.1	0.2	0.0	0.0	0.0
Other	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Transfers (incl. CNRPS, social protection, and BFT)	2.4	2.2	2.5	2.7	2.5	2.3	2.1	2.3	2.3	2.2	2.2
Other current expenditure (non-allocated)	0.0	0.0	0.0	0.1	0.3	0.4	0.4	0.4	0.3	0.3	0.3
Capital expenditure	4.7	5.4	5.5	5.3	5.0	6.1	5.8	7.2	7.3	7.6	7.7
Net lending	0.9	0.1	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-5.3	-5.9	-5.9	-5.2	-5.2	-3.7	-3.4	-2.5	-2.2	-2.2	-2.2
Errors and omissions	1.7	-0.6	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing (net)	3.6	6.5	6.2	5.2	5.2	3.7	3.4	2.5	2.2	2.2	2.2
Foreign financing	5.1	2.9	5.2	6.8	6.4	3.2	3.6	2.6	2.5	2.5	2.2
Domestic financing	-1.5	3.5	1.0	-1.6	-1.2	0.5	-0.2	-0.1	-0.3	-0.3	0.0
<i>of which: privatization and sale of confiscated assets</i>	0.1	0.6	0.2	0.5	0.0	0.5	0.0	0.5	0.5	0.5	0.5
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Overall balance (excl. grants)	-5.6	-6.1	-6.1	-5.6	-5.6	-3.9	-3.6	-2.7	-2.4	-2.4	-2.4
Overall balance (cash basis)	-3.6	-6.5	-6.2	-5.2	-5.2	-3.7	-3.4	-2.5	-2.2	-2.2	-2.2
Overall balance (excl. grants, cash basis)	-3.9	-6.6	-6.4	-5.6	-5.6	-3.9	-3.6	-2.7	-2.4	-2.4	-2.4
Structural balance	-4.9	-6.0	-6.0	-5.5		-3.8		-2.7	-2.4	-2.4	-2.4
Cyclically-adjusted structural fiscal balance (CASFB)	-4.9	-6.0	-7.0	-5.4	-4.3	-3.5	-3.1	-2.7	-2.4	-2.4	-2.4
Total current primary expenditure	21.4	21.3	22.5	22.2	22.5	20.6	21.0	18.4	17.9	17.8	17.7
Social expenditures 1/	1.6	1.6	1.9	2.2	1.9	2.2	1.9	2.2	2.2	2.2	2.2
Gross public debt	55.4	62.4	70.3	70.5	73.1	70.0	73.3	69.4	68.4	67.5	66.5
Domestic	20.1	21.8	21.9	17.8	20.5	16.4	18.9	16.3	15.2	14.5	14.0
External	35.3	40.6	48.4	52.7	52.6	53.6	54.4	53.1	53.1	53.0	52.5
Nominal GDP (billions of TD)	84.7	89.6	96.7	106.2	106.2	116.9	115.4	127.2	138.4	149.6	161.8

Sources: Tunisian authorities; and IMF staff estimates.

1/ Social spending includes social transfers and programs as well as key ministries' capital expenditures. The definition was expanded in 2017.

Table 7. Tunisia: Monetary Survey, 2015–19
(In millions of dinars, end-of-period stocks)

	2015	2016	2017	2018				2019					
	Annual	Annual	Annual	Q1	Q2	Q3	Annual	Annual	Q1	Q2	Q3	Annual	Annual
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Millions of Tunisian dinars)												
Net foreign assets (NFA)	1,686	-949	-2,384	-4,526	-1,137	-1,178	-1,267	-2,528	-1,293	-2,377	-1,949	-1,751	-3,006
Foreign assets	17,849	16,644	16,420	14,600	17,603	18,212	19,302	18,518	19,470	18,585	19,246	21,571	20,416
Central bank	15,075	13,932	13,932	12,406	14,275	14,916	15,493	15,406	15,993	15,441	16,424	17,233	17,172
Foreign liabilities	-16,162	-17,592	-18,805	-19,126	-18,740	-19,390	-20,569	-21,046	-20,762	-20,962	-21,195	-23,322	-23,422
Central bank	-5,991	-6,404	-5,758	-6,001	-6,095	-6,313	-7,123	-7,328	-7,196	-7,271	-7,358	-9,277	-9,124
Net domestic assets (NDA)	60,213	67,832	76,162	78,568	77,416	78,066	80,577	81,459	82,069	84,986	85,065	86,335	89,123
Domestic credit	80,448	91,365	102,726	105,615	105,185	106,070	110,154	112,398	112,589	116,327	115,401	118,509	122,865
Credit to the government (net)	14,355	18,893	21,079	21,968	21,302	21,995	22,336	22,994	23,104	24,157	24,910	25,774	25,724
Central bank net credit	688	3,993	4,255	4,625	5,269	5,962	6,302	6,842	7,071	8,124	8,877	9,740	9,675
Commercial banks	7,199	8,649	10,096	10,616	9,307	9,307	9,307	9,502	9,307	9,307	9,307	9,307	9,398
Other	6,468	6,251	6,727	6,726	6,726	6,726	6,727	6,651	6,726	6,726	6,726	6,727	6,651
Credit to the economy	66,093	72,472	81,648	83,647	83,883	84,075	87,819	89,404	89,485	92,170	90,492	92,736	97,141
Other items (net)	-20,235	-23,534	-26,565	-27,048	-27,770	-28,004	-29,576	-30,938	-30,521	-31,340	-30,337	-32,174	-33,742
Broad money (M3)	61,899	66,883	73,777	74,041	76,278	76,887	79,310	78,932	80,776	82,609	83,115	84,583	86,117
Money plus quasi-money (M2)	58,828	63,660	70,378	70,722	72,859	73,440	75,754	75,198	77,155	78,906	79,389	80,791	82,066
Money (M1)	24,444	26,409	30,302	30,170	31,081	31,329	32,317	31,195	32,914	33,661	33,867	34,465	34,045
Currency	8,418	16,661	19,119	18,952	19,524	19,680	20,301	12,033	20,676	21,145	21,275	21,650	13,132
Demand deposits	16,026	9,749	11,182	11,218	11,557	11,649	12,016	19,163	12,238	12,516	12,593	12,815	20,913
Quasi-money	34,384	37,251	40,077	40,552	41,777	42,111	43,438	44,002	44,241	45,245	45,522	46,326	48,021
Long-term deposits (M3-M2)	3,071	3,223	3,399	3,320	3,420	3,447	3,556	3,734	3,621	3,704	3,726	3,792	4,051
	(Annual percentage change)												
Net foreign assets	-22.4	-156.3	151.4	234.7	-49.9	-55.3	-46.9	3.9	-71.4	109.0	65.5	-38.2	-18.9
Net domestic assets	6.3	12.7	12.3	15.2	7.9	6.2	5.8	7.3	4.5	9.8	9.0	7.1	9.4
Domestic credit	7.5	13.6	12.4	14.9	8.5	7.4	7.2	9.2	6.6	10.6	8.8	7.6	9.3
Credit to the government (net)	13.8	31.6	11.6	23.4	6.1	9.8	6.0	9.9	5.2	13.4	13.3	15.4	11.9
Credit to the economy	6.2	9.7	12.7	12.9	9.2	6.8	7.6	9.0	7.0	9.9	7.6	5.6	8.7
Broad money (M3)	5.3	8.1	10.3	10.8	9.8	8.5	7.5	7.4	9.1	8.3	8.1	6.6	9.1
	(Growth in percent of broad money)												
Net foreign assets	-0.8	-4.3	-2.1	-4.7	1.6	2.1	1.5	-0.1	4.4	-1.6	-1.0	-0.6	-0.6
Net domestic assets	6.1	12.3	12.5	15.5	8.2	6.4	6.0	7.6	4.7	9.9	9.1	7.3	9.7
Domestic credit	9.6	17.6	17.0	20.6	11.9	10.3	10.1	12.8	9.4	14.6	12.1	10.5	13.3
Credit to the government (net)	3.0	7.3	3.3	6.2	1.7	2.8	1.7	2.8	1.5	3.7	3.8	4.3	3.5
Credit to the economy	6.6	10.3	13.7	14.3	10.1	7.5	8.4	10.0	7.9	10.9	8.3	6.2	9.8
Broad money (M3)	5.3	8.1	10.3	10.8	9.8	8.5	7.5	6.6	9.1	8.3	8.1	6.6	9.1
Memorandum items:													
Nominal GDP	84,656	89,581	96,661				106,159	106,179				116,898	115,386

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

Table 8. Tunisia: Central Bank Survey, 2015–19
(In millions of dinars, end-of-period stocks)

	2015	2016	2017	2018				2019					
	Annual	Annual	Annual	Q1	Q2	Q3	Annual	Annual	Q1	Q2	Q3	Annual	Annual
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Millions of Tunisian dinars)												
Net foreign assets	9,084	7,528	8,174	6,404	8,180	8,603	8,370	8,078	8,797	8,170	9,066	7,955	8,048
Assets	15,075	13,932	13,932	12,406	14,275	14,916	15,493	15,406	15,993	15,441	16,424	17,233	17,172
<i>of which: proceeds of FX swaps</i>	606	507	1,491	2,838	2,838	2,838	2,838	1,491	2,838	2,838	2,838	2,838	1,491
Liabilities	5,991	6,404	5,758	6,001	6,095	6,313	7,123	7,328	7,196	7,271	7,358	9,277	9,124
Net domestic assets	1,924	5,094	7,062	8,244	8,150	7,387	6,855	7,497	6,602	7,328	6,384	6,482	8,043
Domestic credit (net)	4,897	9,483	12,739	14,072	14,330	14,418	14,681	15,999	15,001	16,313	15,977	16,773	18,991
Net credit to government 1/	688	3,993	4,255	4,625	5,114	5,519	5,850	6,842	6,616	7,665	8,414	9,272	9,675
Credit to banks 2/	4,209	5,490	8,484	9,447	9,216	8,899	8,831	9,157	8,386	8,647	7,563	7,501	9,317
Other items net	-2,973	-4,389	-5,677	-5,828	-6,180	-7,031	-7,826	-8,502	-8,399	-8,984	-9,593	-10,291	-10,948
Reserve money 3/	11,009	12,622	15,236	14,649	16,330	15,990	15,225	15,575	15,399	15,498	15,449	14,438	16,091
	(Annual percentage change)												
Net foreign assets	-1.8	-17.1	8.6	-10.5	6.6	5.2	2.4	-1.2	7.5	-5.0	8.3	-5.0	-0.4
Assets	5.5	-7.6	0.0	-9.5	1.4	7.1	11.2	10.6	12.0	3.5	6.0	11.2	11.5
<i>of which: proceeds of FX swaps 4/</i>	...	-16.3	194.1	456.5	488.8	237.5	90.3	0.0	0.0	0.0	0.0	0.0	0.0
Liabilities	18.8	6.9	-10.1	-8.4	-5.0	9.6	23.7	27.3	18.1	15.2	3.3	30.2	24.5
Net domestic assets	14.0	164.7	38.6	24.2	20.5	4.6	-2.9	6.2	-19.0	-0.8	-6.9	-5.4	7.3
Domestic credit (net)	12.4	93.6	34.3	17.4	17.8	13.2	15.2	25.6	4.7	13.1	8.8	14.2	18.7
Net credit to government 1/	-44.6	480.1	6.6	4.8	15.8	29.7	37.5	60.8	29.4	38.9	43.8	58.5	41.4
Credit to Banks 2/	35.1	30.4	54.5	24.7	18.9	4.9	4.1	7.9	-9.0	-2.8	-14.4	-15.1	1.7
Other items net	11.4	47.6	29.3	9.0	14.3	23.8	37.8	49.7	35.9	27.8	22.6	31.5	28.8
Reserve Money 3/	0.6	14.7	20.7	16.4	18.4	10.8	-0.1	2.2	5.1	-5.1	-3.4	-5.2	3.3
Memorandum items:													
Open market purchases (OMPs)	112	804	982	1,207	1,207	1,207	1,207	982	1,207	1,207	1,207	1,207	982
FX swap operations 4/	606	507	1,491	2,838	2,838	2,838	2,838	1,491	2,838	2,838	2,838	2,838	1,491
Total CBT refinancing of banks (IMF definition, excl. OMPs)	4,815	5,997	9,975	12,285	12,054	11,737	11,669	10,648	11,224	11,485	10,401	10,339	10,808
Total CBT refinancing of banks	4,927	6,801	10,957	13,492	13,261	12,944	12,876	11,630	12,431	12,692	11,608	11,546	13,280

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

1/ Includes subscription to the IMF and the AMF.

2/ Includes the main refinancing facility (appel d'offres) and the lending and deposit facilities.

3/ Excludes deposits of other financial institutions, individuals, and non-financial enterprises.

4/ Introduced at end-2014.

Table 9. Tunisia: Financial Soundness Indicators of the Banking Sector, 2010–18
(Percent, unless otherwise indicated)

	2010	2011	2012	2013	2014	2015	2016	2017	2018 Mar (prel.)
Regulatory capital									
Regulatory capital to risk-weighted assets	11.6	11.9	11.8	8.2	9.4	12.0	11.6	11.9	11.8
Tier 1 capital to risk weighted assets	10.2	10.0	9.5	6.6	7.6	9.3	8.8	8.9	8.9
Capital to assets	8.4	8.5	7.8	5.6	6.2	7.8	8.2	8.4	8.4
Asset quality									
Sectoral distribution of loans to total loans									
Industry	30.5	28.6	27.9	27.8	27.2	27.3	26.9	27.6	27.8
Agriculture	2.9	2.9	2.8	2.8	2.8	2.6	2.6	2.6	2.7
Commerce	15.0	16.0	15.4	15.1	15.6	15.8	15.9	16.0	16.2
Construction	5.9	5.6	5.4	5.5	5.7	6.2	6.2	5.8	5.7
Tourism	7.3	7.3	6.9	6.5	6.1	6.2	5.8	5.3	5.2
Households	22.1	23.4	25.4	26.2	26.2	26.6	26.3	25.8	25.8
Other	16.3	16.3	16.2	16.0	16.5	15.4	16.3	16.8	16.6
FX-loans to total loans	5.3	5.1	4.8	4.8	5.5	5.8	5.7	5.1	4.5
Credit to the private sector (pct. of total loans) 1/	70.6	67.4	67.7	73.7	73.8	73.5	73.7	74.5	74.2
Nonperforming Loans (NPLs) to total loans	13.0	13.3	14.9	16.5	15.8	16.6	15.6	13.9	13.9
Specific provisions to NPLs	-	48.6	45.7	56.4	58.0	56.9	59.0	63.3	61.4
NPLs, net of provisions, to tier 1 capital	60.3	66.2	86.3	111.6	90.3	78.8	68.2	61.8	58.1
Specific provisions to total loans	7.6	7.6	8.0	10.3	10.1	10.5	10.2	8.8	9.0
General provisions to total loans	-	0.4	0.5	0.6	0.6	0.6	0.6	0.6	0.6
Profitability									
Return on assets (ROA)	0.9	0.6	0.6	0.3	0.9	0.9	1.0	1.2	-
Return on equity (ROE)	10.2	5.9	7.2	3.0	11.2	10.8	11.4	13.9	-
Interest rate average spread (btw. loans and deposits)	3.5	3.0	3.0	3.3	3.1	3.0	2.9	3.2	3.3
Interest return on credit	6.2	5.7	5.4	5.9	6.4	6.3	6.0	6.5	6.9
Cost of risk (pct. of credit)	1.7	1.2	1.2	1.9	1.1	1.1	0.9	0.9	-
Net interest margin to net banking product (PNB)	58.6	57.2	58.1	58.9	57.2	54.6	50.9	49.7	-
Operating expenses to PNB	46.5	51.1	50.3	47.3	48.5	49.2	48.5	47.6	-
Operating expenses to total assets	1.6	1.7	1.6	1.6	1.7	1.7	1.7	1.8	-
Personnel expenses to non-interest expenses	59.1	62.6	61.5	60.8	59.3	60.1	58.7	59.1	-
Trading and other non-interest income to PNB	21.8	22.5	20.9	21.6	22.4	24.3	29.5	29.2	-
Liquidity									
Liquid assets to total assets 2/	29.8	26.5	28.2	28.4	28.2	5.6	5.6	5.6	6.1
Liquid assets to short-term liabilities	104.1	89.4	89.2	92.6	96.6	83.8	94.4	91.7	103.9
Deposits to loans	94.6	87.4	89.5	89.6	88.8	87.4	86.8	85.4	84.8
Deposits of state-owned enterprises to total deposits	13.8	12.6	13.2	13.0	11.7	9.5	7.8	6.8	6.3
Sensitivity to market risk									
FX net open position to tier 1 capital	1.4	1.9	2.3	3.1	2.2	3.3	4.9	6.4	9.6

Source: Central Bank of Tunisia.

1/ Coverage of private sector credit may differ from that of Table 7.

2/ 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.

- = not yet available.

Table 10. Tunisia: Illustrative Medium-Term Outlook, 2015–23

	2015	2016	2017	2018	2019	2020	2021	2022	2023
	Proj.								
	(Annual percentage change)								
Real GDP	1.2	1.1	2.0	2.4	2.9	3.4	3.6	4.0	4.2
Total consumption	2.0	2.4	0.0	-4.0	0.5	2.0	2.5	2.9	4.6
Private consumption	0.9	1.0	-0.2	-5.4	1.8	5.0	2.6	2.6	4.7
Public consumption	6.1	7.3	0.8	0.6	-3.5	-7.5	2.1	4.0	4.2
Investment	-7.8	1.2	4.0	12.2	5.1	5.7	5.7	7.0	4.2
Gross fixed capital formation	-0.3	1.2	4.1	12.2	5.0	5.8	5.8	7.0	4.2
Trade balance	-0.3	-2.0	1.8	7.2	3.0	1.0	0.7	0.2	-0.6
Exports of goods and non-factor services	-2.8	0.2	4.6	6.2	4.6	3.4	4.1	3.6	3.7
Imports of goods and non-factor services	-2.5	2.3	2.8	-1.0	1.7	2.4	3.3	3.3	4.3
Inflation (annual average)	4.9	3.7	5.3	8.1	7.5	5.9	4.9	4.1	4.0
	(Percent of GDP)								
Gross national savings	12.5	13.4	12.0	13.4	14.6	15.7	17.0	18.1	18.5
Central government 1/	0.3	-0.5	-0.4	0.0	2.4	4.7	5.1	5.4	5.5
Rest of the economy	12.3	13.9	12.5	13.4	12.1	11.0	11.9	12.7	13.1
Gross investment	21.4	22.3	22.5	23.1	23.1	23.5	23.9	24.6	24.6
Central government 1/	4.7	5.4	5.5	5.3	6.1	7.2	7.3	7.6	7.7
Rest of the economy	16.8	16.9	17.0	17.7	17.0	16.3	16.7	17.0	16.9
Total consumption	88.6	87.7	88.4	87.2	86.1	84.9	83.8	82.7	82.2
Private consumption	69.0	66.9	67.8	66.9	67.1	67.9	67.1	65.9	65.5
Public consumption	19.6	20.8	20.6	20.3	19.0	17.0	16.7	16.7	16.7
Savings-investment balance	-8.9	-8.9	-10.5	-9.6	-8.6	-7.8	-6.9	-6.5	-6.1
Central government 1/	-4.4	-5.8	-6.0	-5.3	-3.7	-2.5	-2.2	-2.2	-2.2
Rest of the economy	-4.5	-3.0	-4.5	-4.3	-4.8	-5.3	-4.7	-4.3	-3.9
Memorandum items:									
Nominal GDP (in millions of TD)	84,656	89,581	96,661	106,159	116,898	127,201	138,353	149,595	161,791
Overall fiscal balance (pct. of GDP) 2/	-5.6	-6.1	-6.1	-5.6	-3.9	-2.7	-2.4	-2.4	-2.4
Social expenditures (pct. of GDP) 3/	1.6	1.6	1.6	1.9	...	...	...	...	...
Gross public debt (pct. of GDP)	55.4	62.4	70.3	70.5	70.0	69.4	68.4	67.5	66.5
Current account balance (pct. of GDP)	-8.9	-8.9	-10.5	-9.6	-8.6	-7.8	-6.9	-6.5	-6.1
External debt (pct. of GDP)	62.8	67.6	80.1	86.4	88.9	89.3	88.3	85.8	82.9
Credit to the economy (yoy growth, pct.)	6.2	9.7	12.7	7.6	5.6	6.6	6.7	6.5	6.1

Sources: Tunisian authorities; and IMF staff estimates.

1/ Excludes social security, public enterprises, and local governments.

2/ Including grants and excluding privatization.

3/ Public capital expenditures of key ministries and social transfers and programs.

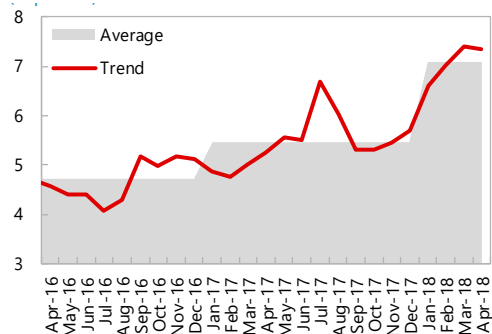
Annex I. Inflation Drivers

After several years of relative stability, core inflation has recently been on an ascending trend. After staying in the 4–5 percent range since 2012, inflation excluding volatile food and energy prices moved to the 5–6 percent range in September 2016 and, after a temporary spike to the 6–7 range 2017, has placed itself in the 7–8 percent range since the early 2018.

This step-wise trend in core inflation points to a broad-based nature of price pressures. Chief among those are:

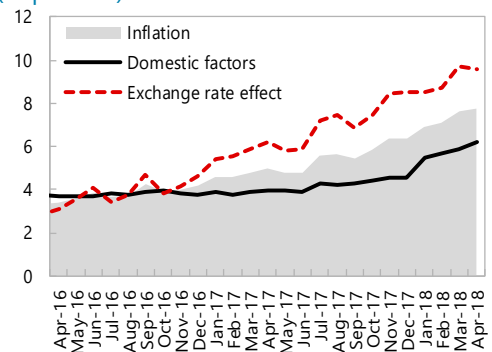
- Dinar depreciation.** Since 2016, the dinar has depreciated relative to the Euro, the currency of Tunisia's main trading partners, by 35 percent, with most of the movement realized since early 2017 (23 percent) in response to a mismatch between FX supply and demand. The gradual ongoing depreciation, translates into an increase in the prices for imported goods, which represent about one third of Tunisia's consumer basket, after several months.
- Wages increases.** Since 2016, the public wage bill has increased by 25 percent (and by 13 percent since 2017, including tax credits). With wage setting influenced by trends in the public sector, private nonagricultural salaries also increased by 15 percent. Wage increases translate into price pressures with a lag of about a quarter. The wage increases in April 2018 (last installment of agreements reached in 2015) are bound to affect prices for the remainder of the year.

Core Inflation, 2016–18 Q1
(In percent)



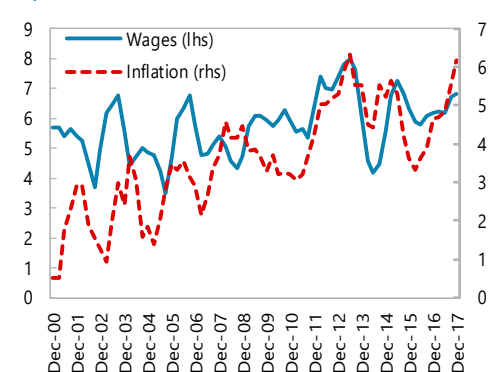
Sources: INS. Core inflation is CPI excluding food and energy prices.

Domestic and Imported Inflation
(In percent)



Sources: INS and IMF staff estimates.

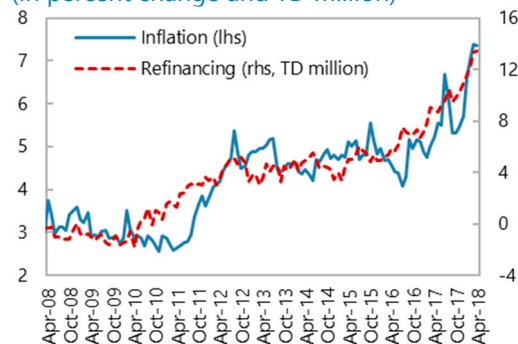
Wages and Inflation
(In percent)



Sources: INS and IMF staff estimates.

- Bank refinancing.** Central Bank credit to banks, mainly in the form of refinancing, has increased by 122 percent since 2016 and by 60 percent since early 2017. This refinancing fed domestic credit, including to households. Inflation tracks the refinancing level closely and contemporaneously.

Inflation and Refinancing
(In percent change and TD million)

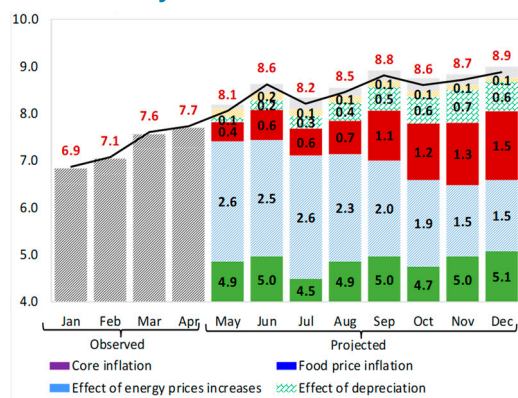


Sources: INS and IMF staff estimates.

These factors will combine with others to accelerate inflation further in the remainder of 2018. Chief among those are electricity and energy price adjustments in the second half of the year, the impact of the tax measures introduced in January 2018 (including a one percent increase in VAT rates), and higher inflation expectation.

Further monetary tightening is needed to contain inflation in the 8–9 percent range by end-2018. Further hikes of the policy interest rate and a strong communication effort would help control price pressures, in the short term notably through their impact on inflation expectations.

Inflation Projection, 2018



Sources: INS and IMF staff estimates.

Annex II. Risk Assessment Matrix¹

Source of Risk and Relative Likelihood	Expected Impact and Recommended Policy Response
Domestic Risks	
<p><i>High</i></p> <p>Slow reform implementation, due to continued political uncertainty, social tensions, and opposition to reforms from vested interests.</p>	<p><i>High</i></p> <p>Growth may fall and macroeconomic stability may be impaired by a halt of structural reforms and stability-focused macroeconomic policies, lower confidence and investment, and diversion of growth-enhancing expenditures to security-related items. Budget financing could be affected by delays in support from IFIs and bilateral donors. Mitigation strategies include (i) effective communication to generate broad buy-in to reforms, (ii) measures to rebuild fiscal and external buffers, including growth-friendly fiscal consolidation and sustained exchange rate flexibility, (iii) acceleration of structural reforms, including to increase the resilience of the financial sector, and (iv) close cooperation with external partners.</p>
<p><i>High</i></p> <p>A deteriorating security situation, due to spillovers from Libya and other conflicts in the region. These could take the form of major refugee flows, increased illicit economic activity including smuggle trade, and violent attacks.</p>	
External Risks	
<p><i>Medium</i></p> <p>Policy uncertainties, due to evolving political processes weighing on global growth and trade flows, as well as uncertainty associated with market fragmentation risks in Europe.</p>	<p><i>Medium</i></p> <p>Growth may fall due to lower confidence and investment; the impact of protectionism on trade and finance flows; higher international oil prices weighing on the budget, the current account, and other economic sector; and increased security spending. Large refugee inflows from Libya could weigh on the budget and on already strained housing and labor markets. Finally, there could be significant social, economic, and political dislocation in case refugee flows from or via Tunisia to Europe accelerated (Tunisia's coast is at a shorter distance from Italy than that of Libya). Mitigation strategies are the same as above.</p>
<p><i>High</i></p> <p>Intensification of the risks of fragmentation and security dislocation in the Middle East region that could lead to socio-economic disruptions, including a sharp rise in migrant flows.</p>	
Source: IMF staff.	

¹ 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. "Short term (ST)" and "medium term (MT)" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Source of Risk and Relative Likelihood	Expected Impact and Recommended Policy Response
<p style="text-align: center;"><i>High</i></p> <p>Tighter global financial conditions: Against the backdrop of continued monetary policy normalization and increasingly stretched valuations across asset classes. Higher debt service and refinancing risks could stress leveraged firms, households, and vulnerable sovereigns, including through capital account pressures.</p>	<p style="text-align: center;"><i>Low</i></p> <p>Sovereign refinancing risks and debt service would increase, but Tunisia's strong reliance on debt to official creditors would limit the impact. Pressures on international reserves could also intensify, even if the capital account remains relatively closed. Mitigation strategies are the same as in the case of policy and geopolitical risks, with an additional focus on debt management and measures to ensure financial sector stability. Moreover, the Financial Action Task Force's (FATF) and the European Union's recent addition of Tunisia to lists of jurisdictions with significant AML/CFT deficiencies increases the risk of a loss of correspondent banking services (CBS). This would hurt cross-border payments, trade finance, and remittances. To mitigate this risk, the authorities are working with the FATF and MENA-FATF to strengthen the effectiveness of their AML/CFT regime.</p>
<p style="text-align: center;"><i>Medium</i></p> <p>Further pressure on traditional bank business models: Legacy problems and potential competition from non-banks curtail banks' profitability globally, possibly leading to a loss of confidence and hence increasing the risk of distress at one or more major banks with possible knock-on effects on the broader financial sector and for sovereign yields in vulnerable economies.</p>	<p style="text-align: center;"><i>High</i></p> <p>Tunisia's growth would be adversely affected through trade, remittances, and investment channels, especially from Europe. Risk mitigation strategies are similar to above, with a strong focus on competitiveness reforms.</p>
<p style="text-align: center;"><i>High</i></p> <p>Structurally weak growth in key advanced economies: Low productivity growth (U.S., Euro area and Japan), high debt, and failure to fully address crisis legacies by undertaking structural reforms amidst persistently low inflation (Euro area and Japan) undermine medium-term growth.</p>	

Source: IMF staff.

Annex III. Monetary Policy—Strengthening the Nominal Anchor

Tunisia abandoned the exchange rate as anchor to direct monetary policy and agents' expectations.

As in many other emerging markets, the exchange rate had long been the anchor of Tunisia's monetary policy framework. Effectively, the Central Bank of Tunisia (CBT) operated a crawling peg, namely a relatively steady rate of depreciation against a Euro/US\$ basket. This rate was not announced explicitly but implicitly chosen to deliver price stability as evidenced by a low average rate of inflation of 3.3 percent over 2000–10. More recently, however, several major shocks—including the 2008 financial crisis and its impact on partner country growth; the prolonged political transition; and the impact of the terror attacks in 2015—have caused Tunisia to transition to more exchange rate flexibility in the face of a diminished stock of international reserves and record-level current account deficits. However, the CBT has continued to intervene significantly in currency markets and is yet to improve the competitiveness of its FX sale auctions.

Transition to a new nominal anchor is needed in the face of accelerating inflation. Inflation has accelerated significantly over the past year to reach a level almost twice the historical average, and is bound to increase further in the remainder of 2018 (Annex I). Against this backdrop, it is paramount for the Central Bank to anchor expectations through a strong, credible commitment to price stability. In its absence of this commitment, economic agents will integrate higher inflation expectations in wage and price formulation. Inflation would rise and erode purchasing power especially for the poor without gains for growth or employment.

Many elements of a credible anchor to achieve disinflation are already established. De jure, the CBT's main objective is "to ensure price stability and to contribute to financial stability so as to support the economic policy of the State in terms of growth and employment" (Circular No. 2017-02 on the Framework for Conducting Monetary Policy). On the operational level, decisions on the policy interest rate—the mid-point of an interest rate corridor defined by standing deposit and lending facilities and the main tool of monetary policy—have been informed by the CBT's inflation forecast. Moreover, in its communiqué accompanying the March and June policy rate increases, the Central Bank started to provide more forward guidance to markets on the inflation outlook, its short-term policy intentions, and its medium-term target to return to levels of inflation consistent with Tunisia's historical average.

The Central Bank could quickly adopt further useful measures to strengthen its focus on disinflation.

- First, it could reconfirm more explicitly that **price stability dominates other objectives** in its decision function, including a concern for employment. This would help the CBT resist the political pressure for an overly expansionary monetary policy stance that, with an upward adjustment of inflation expectations, would likely produce little gains in employment but significant inflation. Staff believes that a strong focus on price stability is especially important in the transition phase to a new policy framework to help build credibility. The approach can become more flexible and take possible short-term tradeoffs between growth and inflation into account once it is more firmly established.
- Second, and in line with the tightening objective, the **policy interest rate should move as quickly as possible into positive territory** in real terms. The longer this takes, the stronger the policy response will have to be to bring inflation back into its target range.
- Third, the CBT could continue to upgrade its analytical toolbox by quickly implementing a **survey of inflation expectations** among firms and household and systematically **extracting information from the yield curve** as critical inputs underpinning policy decisions.
- Finally, efforts to **improve access to finance especially for SMEs** could continue in parallel, through fiscal channels or external partner support for dedicated credit windows.

Annex IV. An Agenda for Technical Assistance, FY18-19

Fund Department	Receiving Agency
Fiscal Affairs Department (FAD)	
• Medium-term tax policy	MoF
• Expenditure rationalization	MoF
• Tax administration core functions (LTU)	MoF
• PFM budget execution and control	MoF
• Public Investment Management Assessment (PIMA)	MoF
• Cash management and treasury functions (METAC)	MoF
• Fiscal Risks (METAC)	MoF
• Pensions	MoF/PM Office/CNRPS
Legal Department (LEG)	
• Strengthening the AML/CFT Frameworks	Commission Tunisienne des Analyses Financières—CTAF and FIU
• Financial and fiscal sector law diagnostic: resolution of NPLs	Ministry of Justice
Monetary and Capital Markets Department (MCM)	
• Central bank strategic planning and budgeting	CBT
• Baking supervision: Strengthening Supervision (Banks' Credit Rating Systems (NPLs))	CBT
Statistics Department (STA)	
• Residential Property Price Index (RPPI)	INS
• Monetary and Financial Statistics: Reporting in SRF	CBT
METAC	
• National Accounts (NA): Elaboration of full set of financial accounts	INS
• National Accounts (NA): consistency between NA and external sector statistics (ESS)	INS
• Banking Supervision: Strengthening Supervision (Implementation of an ICAAP Framework, Basel II and III standards)	CBT
• Banking Supervision: Consolidated supervision	CBT

Appendix I. Letter of Intent

Tunis, June 22, 2018

Madame Christine Lagarde
Managing Director
International Monetary Fund
700 19th Street, NW
Washington, D.C. 20431
USA

Madame Managing Director,

1. The economic recovery is confirming at the beginning of 2018. Growth accelerated to 2.5 percent in the first quarter thanks to an excellent agricultural season and a renewed performance of exports of goods and services. The increase in tourist inflows and foreign direct investment (FDI) is a positive signal of a return of confidence from economic operators. They are also tangible benefits of our efforts to improve the security climate and the business environment. We are, however, aware that these successes, while encouraging, could be weakened if macroeconomic vulnerabilities were to persist. We can thus assure the Tunisians that we are determined to fight inflation, which is weighing on people's purchasing power and growth. At the same time, we will continue to rebalance public finances and reduce the external deficit. We remain vigilant about the evolution of international oil prices and resolved to mitigate their impact on the budget by adequately adjusting domestic energy prices.

2. The consolidation of the democratic system continues in Tunisia. The first free and independent municipal elections were held on May 6, 2018, further anchoring the democratic culture among our citizens and laying the groundwork for local power based on decentralization, as required by the new Constitution. Tunisia remains a vibrant young democracy, a unique experience of successful political transition in the region that has much to contribute to its allies and partners. Today, the sustainability of this experience also means a significant improvement in economic conditions. Our choice to undertake far-reaching reforms is guided by this goal, but we must be careful that this process does not exacerbate social tensions to the point of jeopardizing the confidence of our people in their democracy. We therefore count on the constant and patient support of our partners, particularly through the International Monetary Fund (IMF), for the necessary financial and technical support during this pivotal period in our common history.

3. Performance under the four-year program supported by the IMF's Extended Fund Facility (EFF) has improved significantly. As expected, all quantitative targets at end-March 2018 were met. We observed all four quantitative performance criteria (QPC): (1) the floor on the primary balance of the central government (cash, excluding grants); (2) the ceiling on total primary current expenditure; (3) the cap on net domestic assets of the (NDA); and (4) the floor on net international reserves (NFA) of the Central Bank of Tunisia (CBT). We also observed the continuous zero ceiling on the

accumulation of external arrears and the quantitative indicative target (IT) on social spending. The new quantitative indicative target on net foreign exchange (FX) interventions of the CBT was observed in March, April, and May. We completed three Prior Actions (PAs) for the Third Review, and, at mid-June, three of the nine Structural Benchmarks (SBs) due for the Third Review, and one more SBs with a delay. Substantial progress has been made on many other SBs.

4. In view of the macroeconomic policies implemented to achieve the main objectives of the program and the continuation of the agreed structural reforms, we request the conclusion of the Third Review under the program supported by the EFF and the disbursement of SDR 176.7824 million. To strengthen further the monitoring of our reforms and highlight our commitment to preserve equity and social justice throughout our adjustment process, we propose to include two new QPCs from September 2018 onwards. The first will be related to CBT's net FX interventions, which will be added as a QPC in addition to the monthly IT. The second will be to convert the IT on social spending to a QPC. While end-June PCs appear on track to be met, data are not yet available to assess the performance. We therefore request a waiver of applicability for all end-June quantitative criteria. We have also implemented and are committed to implement the measures listed in the schedule of PAs and SBs, as described in the Memorandum of Economic and Financial Policies (MEFP, Tables 1 and 2) and the attached Technical Memorandum of Understanding (TMU).

5. This Letter of Intent is based on the previous Letter of Intent and the MEFP dated March 14, 2018. The attached MEFP outlines the main elements of the reform agenda and the policies of the Government and of the CBT, which we intend to put in place during the period 2018–20. We remain committed to applying our program rigorously, while being aware of the challenges of the national, regional, and international context.

6. We are convinced that the policies described in the attached MEFP are appropriate for achieving the objectives of our economic program. In addition, we remain vigilant and ready to take any additional measures that may be necessary to achieve these objectives. In line with the IMF's consultation policies, we will discuss with IMF staff the adoption of these measures prior to any revision of the macroeconomic policies contained in this MEFP. All information and data necessary for the monitoring of the program, as well as for the technical assistance (TA) missions requested under our EFF-supported program, will be provided to IMF staff within the agreed deadlines.

7. We authorize IMF staff to publish this Letter of Intent and the attachments (MEFP and Tables 1 and 2) as well as the related IMF staff report.

Very truly yours,

/s/

Marouane El-Abassi
Gouverneur de la Banque Centrale de Tunisie

/s/

Mohamed Rida Chalhoun
Ministre des Finances

Attachments (2):

1. Memorandum on Economic and Financial Policies
2. Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

This memorandum describes the main features of our reform program, which aims at maintaining macroeconomic stability while promoting stronger and inclusive growth.

- 1. Bringing the economic transition to a successful end will consolidate the political transition and remains a priority.** The determined choice we made for the overhaul of our economy calls for an acceleration of concrete reforms to strengthen the economic recovery through investment, exports, and more private initiative. Maintaining public finances and external balances in good health will also be essential. Beyond the economic merits, these policy priorities are necessary to make the democratic transition successful. Being committed to these economic objectives might seem difficult but is nevertheless indispensable and we must explain this choice to the public.
- 2. The Government is committed to implementing its reform plan.** Since the last quarter of 2017, the Government has accelerated the pace of reform, both through the adoption of legal and regulatory texts, and the effective implementation of concrete reform proposals.

I. VULNERABILITIES ON THE RISE DESPITE THE RECOVERY

- 3. The recovery is gaining strength in 2018.** Growth in the first quarter was 2.5 percent, the quickest pace since 2014. This result is mainly explained by the robust performance of olive oil production, but a renewed dynamism in exporting sectors benefiting from the improvement of European demand also played a significant role. In addition, tourism, transport, and financial services continue to show encouraging results. These results could have been better had it not been for the poor performance of the mining sectors due to social problems. The Tunisian economy is now on an upward trajectory, where growth is increasingly driven by investment and exports, promoting inclusive growth in the medium term.
- 4. Gradual reorientation of fiscal policy.** The first quarter has launched fiscal consolidation in line with our commitments made in the 2018 Budget Law. Tax revenues grew 12 percent from their level in the first quarter of 2017, while current expenditure fell by 10 percent, with the wage bill declining by 9 percent at end-March. In parallel, capital spending increased by 22 percent, confirming our goal to reorient government spending towards investment. Outstanding public debt reached the level of 68.45 percent of GDP at end-March against 61.89 percent of GDP in the same period last year. The reduction of public debt is necessary in order to create the fiscal space required to sustain the recovery and create more jobs for young people.
- 5. Inflation has become a major concern.** Inflation increased to 7.7 percent in May 2018, the highest level since 1991. Several one-off factors were at work: in addition to the effect of past salary increases, the surge in inflation is also due to increases in various stamp duties and taxes in the 2018 Budget Law. That said, a monetary policy stance that is not restrictive enough, accompanied by the depreciation of the exchange rate and robust growth in credit to the economy have also pushed up inflation. Indeed, the increase in the policy rate and the widening of the corridor between deposit

and lending rates at the Central Bank of Tunisia (CBT) did not manage to bring the money market rate (TMM) in real terms into positive territory and thus reduce commercial banks' refinancing volumes at the CBT. The latter reached new records to exceed TD 14 billion in mid-May 2018. Bringing inflation gradually back to historical averages (3 to 5 percent) will remain the main objective of the CBT, given that inflation at today's levels is detrimental to social cohesion, accentuates poverty, and discourages new investments.

6. The current account improved somewhat but FX reserves remain under pressure. The current account improved in the first four months of 2018, with the deficit reaching 3.7 percent of GDP (compared to 4.4 percent of GDP for the same period in 2017). This result owed to the good performance of exports of agriculture and agri-food industries, as well as to the recovery in exports of manufacturing industries. At the same time, tourism receipts and remittances have grown considerably. On the other hand, the import bill grew, partly driven by a large deficit in energy linked to the increase in international oil prices. The slight improvement in the current account was not enough to halt the ongoing deterioration of our level of foreign assets. Reserve coverage fell from 93 days of imports at end-2017 to 76 days of imports at end-May, partly due to high debt service and the current account deficit. We are aware that high oil prices for the remaining period of the year, combined with low domestic energy production, would put significant pressure on the external sector of our country.

7. The banking sector remains resilient to tensions. The banking sector remains stable and credit to the economy has been growing rapidly. On the other hand, deposit growth in 2017 was not enough to relieve pressure on banks' liquidity because of the significant contractionary effects from high government financing needs and strong demand for FX, which led to an excessive reliance of banks on Central Bank refinancing. This situation became more pronounced during the first months of 2018. However, the aggregate capital ratio of the banking sector remained around 12 percent at end-March 2018, supported by sound bank profitability arising from strong demand for consumer and housing loans. Non-performing loans remain high, at around 14 percent of total loans at the end of March 2018, provisioned at 58 percent (excluding reserved interest). The adoption of two laws giving public banks more flexibility in terms of credit activities and debt write-off in May 2018 will start the process of non-performing loans (NPL) resolution at public banks. We hope that reinvigorating this activity will improve access to finance for the entire economy, especially for small and medium-sized enterprises (SMEs).

8. Improvements in the business environment. The Government has paid particular attention to the implementation of major economic reforms to further improve the business environment. 2018 saw the establishment of the governance structures created by the new Investment Law, namely the Tunisian Investment Authority and the Strategic Investment Council. FDI has grown at its fastest pace since 2010. Moreover, the adoption of the "Startup Act" is part of our strategy "Startup Tunisia" aimed at transforming Tunisia into an attractive regional hub for new companies. Also, with the view to boost public-private partnerships (PPPs) in strategic investment projects, a high-level conference on PPPs and their possible applicability to concrete investment proposals is scheduled for June. In addition, our participation in the G20 initiative "Compact with

Africa” will be a good platform to highlight to potential investors our progress in improving the business climate.

9. Urgent implementation of reforms is a top priority. Recognizing the acute pressures and fragility of our macroeconomic conditions, the Government has embarked on a resolute effort to restore the soundness of economic fundamentals. To maintain macroeconomic stability, control fiscal and external balances and contain debt, it will be essential to foster more sustainable and inclusive growth. We will redouble our efforts in this vein, because the later the reforms are put in place, the higher will be the adjustment costs and the greater will be the delay in reaping the dividends of reform.

II. ACCELERATING REFORMS IS ESSENTIAL TO SUSTAIN THE RECOVERY

10. Our performance under the program improved at the beginning of this year, which allowed us to meet all the quantitative criteria of the program at end-March 2018:

Quantitative Performance Criteria (QPC)

- We observed the floor on the **primary balance** of the central government, thanks to a good performance of government revenue (tax and non-tax revenues) as well as strict discipline in expenditure execution.
- We observed the ceiling on **total primary current expenditure** at end-March following measures taken to contain the wage bill (limiting new recruitment and stopping promotions) and control energy subsidies (price increases of car fuel products and electricity).
- We observed the ceiling on **net domestic assets** (NDA) at end-March. Despite persistent pressure on the liquidity of commercial banks, we managed to contain somewhat the volume of refinancing of commercial banks at the CBT. Increases in the policy rate and the widening of the interest rate corridor have deterred banks from relying on CBT funding.
- We observed the floor on **net international reserves** (NIR) at end-March. This result is mainly due to two factors: (i) the slight improvement in the current account deficit in the first quarter (linked to the good performance of agricultural exports); (ii) our effort to restore confidence in the FX market, which has stimulated the supply of FX while containing our interventions in the form of sales.

Continuous Performance Criteria

- We observed the zero ceiling on the accumulation of new **external debt payment arrear** by the central government.

Quantitative Indicative Targets

- We observed the zero ceiling on the accumulation of new **domestic arrears**.
- We observed the ceiling on **net foreign exchange interventions** by the CBT for the months of March, April, and May.
- We observed the floor on **social spending** in line with our commitment to strengthen the protection of the most vulnerable.

11. We revised the list of Structural Benchmarks (SBs) with a view to rationalize their number and prioritize their effective implementation.

Met Structural Benchmarks

- **Structural reforms/private-sector development.** The new Investment Law has now entered into force, with the Tunisia Investment Authority (*met SB*) becoming fully operational and the publication of the government decree on the negative list of investment activities that remain subject to authorization on May 11, 2018.
- **Financial sector reform.** Parliament (i.e. the Assembly of the People's Representatives, ARP) adopted a law on May 22, 2018 simplifying loan write-off rules ensuring that final judicial judgments are no longer necessary. It also voted at the same meeting a law allowing public banks to write-off non-performing loans in the same way as private banks (*met SB*).
- **Fiscal policy and reforms of public institutions.**
 - After a long consultation with social partners on the parametric components of the pension reform, the Council of Ministers adopted a draft bill on June 20, 2018 (*SB not met, but implemented with delay*), and asked Parliament to pass it before end-September 2018.
 - After the completion of the functional review of the Ministry of Equipment, the final reports on the functional reviews of four key ministries were delivered. The results of the reviews will be the basis for the current reflection on how to implement the government's strategy for modernizing the public service.

Reprogrammed Structural Benchmarks

- **Governance/private-sector development.** The decree appointing the members of the High Anti-Corruption and Good Governance Authority could not be signed in due time in view of the need for further consultations between party blocs in parliament (*reprogrammed SB* for December 2018).
- **Financial sector reform.** The law on the effective lending rate ceiling (TEG) is currently under discussion in parliament. Contrary to what was initially envisaged, the interest rate cap for loans to individuals will remain at its current level of +20 percent above the average lending rate,

while the threshold for SME loans will be raised to +33 percent. We decided to leave the interest rate cap for individuals unchanged to support the bargaining power of households vis-à-vis banks (*reprogrammed SB* for December 2018).

- **Exchange rate policy.** The CBT's auction mechanism to sell FX to the market has improved as the auction now systematically rejects the least competitive offer on a bank by bank basis. We will need the time between now and end-August to render the auctions fully competitive (*reprogrammed SB* for August 2018). This new operational approach aims to keep our interventions in the FX market within the limits agreed in the program for April and May 2018 (*Prior Action*).

Not met Structural Benchmarks

- **Financial sector reform.** The banking resolution committee has become operational and is scheduled to hold its first meeting on June 28, 2018. The committee's first meeting will focus on examining and reviewing the situation of the *Banque Franco Tunisienne* (BFT), which the CBT had referred to the committee. The process leading to the orderly resolution of the BFT has thus started (*reprogrammed SB* for August 2018).
- **Fiscal policy and reforms of public institutions.** After a first increase in January, the quarterly fuel price adjustments continued in April; although the price increases remained below the level prescribed by the automatic fuel price formula (*missed SB*). In order to cope with recent pressures from higher international oil prices and contain the fiscal deficit, future adjustments will be significant and based on the measures described in paragraph 14 of this memorandum (*Prior Action*).

Dropped Structural Benchmarks

- **Fiscal policy and reforms of public institutions.** We created a General Committee on Taxation, Public Accounts, and Collections (CGFCPR) in December 2017 to overcome the challenges associated with the fragmentation of tax functions. This committee will follow the model launched by France in 2007. We are aware that the merger of the General Directorate of Taxes (DGI) and the General Directorate of Public Accounting and Collections (DGCP) is an onerous operation that includes technical, human, legal, managerial, and procedural challenges. Completing the merger can take several years. We request to drop two important SBs related to the establishment and operationalization of the new Large Taxpayers Unit (LTU) since its implementation will require more time, given the new direction in our efforts to modernize tax administration. The dropping of the SBs will not have a direct impact on tax revenues.

A. Maintaining Macroeconomic Stability

12. **We intend to urgently implement measures to address pressing vulnerabilities and protect the ongoing recovery.** The good performance of the Tunisian economy during the first

quarter confirms our forecast of a growth rate of 2.4 percent for the whole of 2018. This positive signal encourages us to persevere on our path of reform, as major pressures on the budget, external balances and inflation persist. Without a proactive response, we run the risk of negatively affecting macroeconomic stability, which would undermine the nascent recovery, tarnish the social climate, and derail the economic transition. Our response in terms of economic policies will focus on: (i) the pursuit of well-targeted fiscal consolidation in an international context characterized by higher oil prices and greater risk aversion in international markets; (ii) a tightening of monetary policy to avoid unhinging inflation expectations; and (iii) a continuation of increasing the flexibility of the exchange rate.

Fiscal Policy

13. The fiscal consolidation course remains on track. The fiscal deficit reduction path agreed in the Second Review of the Program remains relevant, based on a consolidation of around 1 percent of GDP per year, starting in 2018, to reduce the deficit to less than 2.5 percent of GDP by 2020. This strategy will reverse the unsustainable trend that public debt has taken in recent years. Strict spending discipline, fairer taxation, more dynamic tax collection (including for the collection of arrears), and a reorientation of spending to social sectors and public investment remain priorities. Although desirable in the presence of inflationary pressures, a stronger fiscal adjustment is unrealistic given the imperfection of social safety nets and the sharp rise in international oil prices. To ensure adequate financing of the budget, we are counting on mobilizing external resources, notably by issuing two sovereign bonds in international markets in July and in December of this year. Domestic financing will be consistent with the financing needs established in the 2018 Budget Law.

14. Our greatest priority will be to minimize expenditure deviations from the agreed ceilings. Strong spending pressures in the first half of the year would likely increase the budget deficit by around 1 to 2 percent of GDP in the absence of an appropriate policy response. As a result, we are considering the following measures to minimize any slippages in spending and we will introduce by the end of September a Supplementary Finance Law that takes the following commitments into account:

- **Controlling the wage bill.** The expected results of the two departure programs—(i) the early retirement program and (ii) the negotiated voluntary departures—may unfortunately prove unachievable. Approximately 5,000 civil servants will benefit until July 2018 from early retirement, which will result in savings of TD 120 million a year. However, to date, only 1,771 employees have shown an interest in the negotiated voluntary departure program. To maintain the objective of a wage bill of 12.4 percent of GDP by 2020, we have decided to launch a second wave of the voluntary departures program in July 2018. At the same time, we continue our policy of strictly limiting the number of new hires to less than 3,000 civil servants per year in 2018 and to less than 3,000 in 2019. Regarding wage bargaining, we renew our commitment not to grant no additional wage increases in 2018 and 2019, unless growth surprises on the upside compared to our current forecasts for the period 2019–20, and without

affecting the planned adjustment path of the wage bill to 12.4 percent of GDP in 2020. Besides, in the interest of budget transparency, we will eliminate the use of tax credits starting in 2019.

- **Containing energy subsidies.** The sharp rise in international oil prices since the beginning of the year is a major risk for the budget. Without additional measures, assuming an average price per barrel of US\$70 in 2018, the total energy subsidy bill in 2018 would be around TD 3,600 million (compared to TD 1,500 million included in the 2018 Budget Law). Despite important policy measures, especially regarding price adjustments, which can generate savings of about TD 900 million, we will have to increase the energy subsidy budget to TD 2,700 million (2.5 percent of GDP), while maintaining the overall deficit at 5.2 percent of GDP. To achieve the savings, we will adjust fuel prices upwards on a monthly basis. We made a first increase on June 22 of 70 millimes on average, which will be followed by monthly adjustments from July to the end of 2018 to achieve a saving of TD 250 million. If the cap of TD 2,700 million for energy subsidies in 2018 risks to be exceeded, we will make an extraordinary increase in October to stay within the limits of the programmed envelope. The increase in June and subsequent monthly adjustments, as well as the possibility of an extraordinary adjustment in October, were the subject of public statements in June 2018 (Prior Action). In addition, we will continue to revise upward the electricity and gas rates mostly for corporates after the May hike for corporates, which will save another TD 300 million. The remaining savings will come from other measures aimed at rationalizing consumption, notably by reducing the supply of subsidized fuels in exchange for a new, more efficient and non-subsidized product offering. To protect the most vulnerable from the impact of this price adjustment policy, we will increase targeted social spending (see Section B, Paragraph 18).
- **Reforming the social security funds.** After extensive consultations with social partners, the Government adopted the pension reform on June 20, 2018 (SB not met, but implemented with delay), aiming to reduce the financial imbalances of our two pension funds, for public (Caisse Nationale de Retraite et de Prévoyance Sociale, CNRPS) and private-sector employees (Caisse Nationale de Sécurité Sociale, CNSS) and the medical insurance fund (Caisse Nationale d'Assurance-Maladie, CNAM). Parliament approval and the entry into force of the law is expected before the end of September 2018, with retroactive effect from 1 July 2018. The main components of the reform include: (i) a parametric reform of pensions (including retirement age, contribution rate, and indexation); (ii) a governance reform of the funds; and (iii) the implementation of a new arrears recovery strategy for CNRPS, CNSS, and CNAM. Due to the delay in the implementation of the reform, the Government will transfer about TD 300 million to the CNRPS, with the remaining shortfall being filled by renewed efforts in arrears collection. The projected deficit of CNSS would be fully covered by a stronger collection effort (including from some state-owned companies that have seen their bank accounts frozen due to their failure to transfer contributions to the pension fund). The adoption of the reform law is a first step towards a comprehensive consolidation of the financial position of the social security funds, and will be complemented by larger reforms in the years to come.

15. Greater revenue mobilization remains a priority. Regarding tax administration, we intend to merge the DGI and the DGCP, in line with the model of the French tax administration. To this end, we have initiated a large-scale program of technical assistance and capacity building. We hope to complete the first step of merging the collection and control functions before the end of 2018. At the same time, in the context of the 2019 Budget Law, we have planned to implement the convergence of tax rates between the "offshore" and "onshore" tax regimes to respond to requests from the European Union (EU), with a view to permanently remove Tunisia from the EU's list of non-cooperative tax jurisdictions. In addition, the 2019 Budget Law will also introduce a VAT reform for the liberal professions¹ (raising the rate from 13 to 19 percent) from 2019 to reinforce the impartiality of the reforms (*SB* for December 2018).

Monetary Policy

16. Accelerating inflation requires a tighter monetary policy stance. Inflation reached 7.7 percent in May, an unprecedented level since 1991. Even more worrying, these upward trends in inflation are expected to continue for the remainder of the year due to the depreciation of the dinar and rising international prices, especially for energy. Given that inflation is now outside the 3 percent to 5 percent corridor for 9 months and continues to accelerate, there is a risk that inflation expectations become unanchored. The sharp increase in money and credit aggregates observed so far, as well as the record performance of the Tunis stock market index following the rise in interest rates in March, suggest that the stance of monetary policy remains accommodative. In fact, it adds to inflationary pressures. Given that inflation at such levels weighs on the purchasing power of the Tunisian people, affects the competitiveness of the economy and undermines the recovery as well as the social climate, we are implementing a strategy to combat inflation based on the following main elements:

- **Steering the real money market rate (MMR) to a positive level.** Our short-term operational target will be a positive real money market rate. Following the 75-basis point increase in March, we raised the policy rate by another 100 basis points in June. Thanks to these efforts, we expect that our credibility as the guarantor of price stability would strengthen and the acute pressure on banks' liquidity would decline, which would then slow the supply of credit to the economy. After the two increases this year, the money market rate in real terms remains negative, calling for additional adjustments in the second half of the year to reach neutrality. We stand ready to tighten monetary policy faster than expected if inflation (especially core inflation) remains above our forecast in the coming months. Efforts to tighten monetary conditions will also help us reduce the record level of bank refinancing from the Central Bank. We will contain the refinancing by TD 1 billion by the end of the year.
- **Strengthening the forward-looking communication of monetary policy.** Direct and ongoing communication to the public about our commitment to prioritize our price stability mandate will help guide inflation expectations. The better we manage to anchor expectations, the smaller the

¹ Activities where profits are derived from intellectual activity.

necessary adjustment will be to bring down inflation towards its historical average over the medium term.

- **Enhancing the monitoring of balance sheet effects and managing macro-prudential risks.** We have strengthened the refinancing framework of the Central bank to better control risks to the Central bank's balance sheet. We have increased the haircut of private assets from 25 percent to 30 percent and we will proceed to a daily valuation of negotiable securities used as collateral for refinancing operations based on the new yield curve as of July 4, 2018. We will continue to deepen our understanding of the impact of the envisaged monetary tightening and more exchange rate flexibility. To date, our analysis suggests that monetary tightening would not cause significant risk to the solvency or liquidity of banks, businesses and households. Interest expenses, for the average firm, for example, represent only 2 percent to 3 percent of total expenses. Similarly, the overall profitability of the banking system was 1.2 percent in terms of return-on-assets (ROA) and 13.9 percent in terms of return-on-equity (ROE) last year, and exposure to currency risk remains low (about 8 percent of assets). However, we will develop new analytical capabilities to analyze balance sheet effects, particularly new supervision instruments and new skills for banking supervisors.
- **Continuing to improve transmission channels.** Better monetary transmission will depend on: (i) strengthening the role of the CBT as a guarantor of price stability through proactive monetary policy that puts price stability above all other competing objectives; (ii) reducing commercial banks' use of the CBT's refinancing window in favor of more activity in the interbank market; (iii) relaxing the constraint posed by the interest rate cap applied to business loans and a more frequent updating of the calculation used to determine the level of the effective lending rate ceiling (the TEG).

Exchange Rate Policy

17. More exchange rate flexibility is necessary to facilitate a reduction in external imbalances. The observed improvement in the current account in the first quarter is partly due to greater exchange rate flexibility. This approach will allow us to stimulate exports, especially manufacturing, discourage imports of consumer goods, and ultimately protect the CBT's FX reserves by giving more importance to the fundamentals of supply and demand for FX. According to our empirical estimates, the elasticity of the current account with respect to the real effective exchange rate is non-negligible, confirming the important role of the exchange rate flexibility to ensure the sustainability of Tunisia's external position. In the short term, we are committed to:

- **Limiting net sales of FX.** We have strictly observed the limit on net sales by the CBT in the FX market agreed under the program in the months of April and May (*Prior Action*). This achievement has helped maintain the dinar on a flexible path, where the exchange rate better reflects market forces. In addition, we will introduce more competitive FX auctions in the coming months (*reprogrammed SB* for August 2018). This operational change will ensure that the CBT's interventions serve to smooth excessive volatility without leaning against an alignment of the

dinar with fundamentals that determine its equilibrium rate. We will seek technical assistance from the IMF to guide this transition to a competitive currency auction system.

- **Reviewing exchange restrictions.** We reaffirm our commitment to withdraw the circular 2018-01 (which replaces the original circular 2017-09) limiting access to financing for imports of non-priority goods by the end of the year. We found that the effect of this measure on imports was mixed and that its introduction created uncertainty for economic operators about the prospects for FX regulation in the years to come.

B. Providing Adequate Social Protection

18. Strengthening the scope of social protection remains a central moral commitment in our reform agenda:

- **Broadening the social safety net.** In order to compensate the poorest families and the most vulnerable (the unemployed and retired) against rising energy prices and rising inflation, the Council of Ministers met twice on 1 and 11 June 2018 to examine social intervention policies. We have increased the financial envelope for the financing of social expenditures by about TD 100 million (for the remaining six months of the year) over and above the measures announced in January 2018, while at the same time increasing the effectiveness of the targeting of the poorest.
 - The National Program of Assistance to Necessary Families (PNAFN) will be our main instrument to reach our goal of protecting the most vulnerable. We have already increased the allowances for the average needy family by around TD 30 (TD 75 million) at the beginning of the year. We will strengthen this policy further through the following measures:
 - (i) extending coverage to 35,000 households on the waiting list to increase the number of targeted households from 250,000 to 285,000 (TD 108 million a year); and
 - (ii) covering transport costs for children and students from families in need (TD 1 million a year).
 - To mitigate the back-to-school and university expenses of the population in general and the middle class in particular, this year we have planned two re-entry allowances for families:
 - (i) granting allowances of TD 500 for back-to-school expenses for new graduates per family (TD 26 million per year); and
 - (ii) granting exceptional return allowance of TD 150 for categories B, C, D and A3 (TD 40 million per year).
 - To consolidate the provision of health care through our network of health centers close to the vulnerable populations, we decided to:

- (i) increase the stockpile of medicines for chronic and heavy diseases (TD 25 million per year) for the benefit of primary care facilities; and
- (ii) consolidate the maternal health care program (TD 15 million a year).

The measures to increase social spending have been the subject of a public announcement by the Government (*Prior Action*).

- **Protecting social spending.** Social spending will play a key role in our efforts to mitigate the social impact of fiscal and monetary adjustment in this difficult time. For this reason, we have agreed to elevate the current indicative target on social spending to a formal quantitative performance criterion from September. Two-thirds of our social expenditures take the form of social assistance (mainly cash transfers to vulnerable families and job training programs) and two-fifths are dedicated to education spending (mainly scholarships).
- **Continuing social security reform.** The reform bill approved by the Council of Ministers (*SB not met, but implemented with delay*) and scheduled to be discussed in Parliament is in itself insufficient to ensure the viability of the social security system due to the structural gap between benefits (pensions up to more than 80 percent of salaries) and the financial resources available to the pension funds. The financial situation, already precarious in 2018, is likely to worsen in the coming years, particularly with longer life expectancy. This bill is only a first step towards a more comprehensive reform of the retirement system aimed at resolving its structural deficits. We will continue to work closely within the Social Protection Committee with our social partners—the public labor union (*Union Générale Tunisienne du Travail*, UGTT) and employers' association (*Union Tunisienne de l'Industrie, du Commerce et de l'Artisanat*, UTICA)—and with the technical support of the World Bank and the International Labor Office to improve the quality of the reforms with the objective of achieving financial equilibrium of the pension funds.

C. Creating More Opportunities for the Private Sector

Governance and Business Climate

19. Boosting the business climate. The first half of 2018 saw the establishment of the governance bodies of the new Investment Law. Put differently, the law effectively came into force. Specifically, the Tunisian Investment Authority started operations (*met SB*), which is now the sole interlocutor of new investors, operating as a “one-stop shop” to facilitate formalities and administrative procedures. Second, the Strategic Investment Council brings together private and public representatives to promote global and sectoral strategies. In addition, the government has made concrete progress towards its goal to substantially reduce the number of authorizations necessary for new investment. The publication of a government decree on May 11 specifies eight sectors (“negative list”) where authorizations remain mandatory—for all other sectors, any investment is now free of prior authorization. If an authorization remains necessary, the decree also sets the deadlines for granting authorizations, between 60 and 90 days. If these time limits have lapsed, the authorization is considered granted according to the principle of “silence is consent”.

20. Strengthen good governance and the fight against corruption. The Government reiterates its irreversible commitment to fight against this economic evil that undermines public confidence and weakens political support for the reform program. To this end, our main instrument will be the High Anti-Corruption and Good Governance Authority (HACGGA), which will be created on the basis of the current National Anti-Corruption Authority (*Instance Nationale de Lutte Contre la Corruption*, INLCC). Despite considerable efforts, the decree appointing the members of the Board of the High Authority could not be published because of the complex consultations between the party blocs in Parliament in charge of selecting the members. Parliament is aware of the importance of quickly nominating the board members and we hope that the process will be completed by September (*reprogrammed SB* for December 2018).

Financial Sector

21. Continue financial sector reforms. The overhaul of the financial sector is a major component of our economic vision for the country, leading to economic and social inclusion and more economic opportunities for all Tunisians. In concrete terms, the overhaul of the system involves improving the quality of banks' loan portfolios, strengthening financial stability and bank liquidity, enhancing banking supervision, and improving access to finance.

- **Resolving non-performing loans.** We are moving forward in our effort to strengthen the asset quality of the banking system, especially of public banks:
 - Parliament adopted two fundamental laws to put public banks on an equal footing with private banks when it comes to resolving NPLs. These laws will better enable public banks to achieve the objectives of their restructuring plans (*met SB*): (i) a law allowing public banks to abandon classified loans on the same basis as private banks, (ii) a law simplifying the rules for write-off so that only a first judicial judgment of a first instance is necessary. Regarding the law of write-off, the Directorate General of Tax Legislation at the Ministry of Finance will issue guidance notes on applying the new rules to the industry by end-June 2018.
 - The decree stipulating that the public banks are not subject to the assent of the commission established by Article 474 of the Commercial Code was adopted in January by the Council of Ministers and should be signed by the Head of Government by end-June 2018.
 - The Ministry of Justice, in collaboration with the Ministry of Finance, has already requested technical assistance from the United Kingdom. We are waiting for the development of the training schedule that will be finalized by the end of June 2018. The Ministry of Justice remains committed to identifying the commercial courts that will specialize in banking issues, and the training program will be set up by September 2018.
 - The Ministry of Tourism (in collaboration with the *Agence Foncière Touristique*, the Banking Association and the Federation of Hoteliers) is continuing to explore a mechanism to reprofile hotels whose sustainability is not assured. The objective will be to allow them to

restructure their debts and upgrade the level of their touristic services. We are committed to propose concrete actions by September 2018.

- The draft bill on collection companies has been delayed. We continue to work on the text to refine the details of Article 19 related to the protection of debtors. Parliament will adopt the law by December 2018.
- The Ministry of Finance and the Financial Sector Reforms Committee (COREFI) continue to prepare a comprehensive strategy on NPL treatment and resolution in the banking sector, which will be published in December 2018.
- **Operationalizing the resolution framework for banks and financial institutions in difficulty.** Following the consultation with ministerial departments in charge of the litigation that opposes the Tunisian State and ABCI (former majority shareholder of BFT), the resolution committee, constituted last December, is scheduled to hold its first meeting on June 28, 2018 to examine the situation of the BFT transmitted by the CBT. The committee will prepare a roadmap for the next steps in resolving the BFT, considering the legal, financial and political complexities involved in this process (*reprogrammed SB* for August 2018). The deposit guarantee fund started its activities and began to build its pool of financial resources through contributions from the CBT, the Ministry of Finance and commercial banks in June 2018.
- **Pursuing the modernization of banking supervision.** In the current context of monetary tightening and rising inflation, we are committed to continue improving our supervision capacity to ensure that the financial sector remains sound. To this end, the staff of the Banking Supervision Directorate at the CBT will hire an additional 12 supervisors by the end of September 2018. We will continue to work closely with METAC to develop the tools put in place by Pillar II of the Basel Accord aimed at monitoring market and interest rate risk and assessing the capital adequacy of commercial banks. These initiatives include: (i) continuing to strengthen the CBT's internal capacity to implement ICAAP; (ii) issuing a circular on capital adequacy based on Basel II guidelines for measuring and managing market risks; and (iii) clarifying the CBT's regulatory framework for interest rates (IRR), concentration and strategic risks. We are also continuing our efforts to move to consolidated supervision by the second half of 2019 and continue to monitor the resolution strategy for bad debts in the tourism sector (based on the white paper adopted in February 2018), including with respect to the loans granted an exemption to the contagion principle.
- **Facilitating access to financing.** The Ministry of Finance and the *Comité de Réforme du Secteur Financier* (COREFI) have made considerable progress towards the National Strategy for Financial Inclusion, which should be validated by the Government in September 2018. We continue to work on the development of financial inclusion indicators based on a survey (with the assistance of the European Investment Bank, EIB) to be finalized by the end of 2018. These indicators should be regularly published to monitor financial inclusion in Tunisia. We are also waiting for the adoption of the law on the regulation for credit bureaus (pending the discussion in Parliament), which aims to improve financial access by collecting and sharing financial data.

COREFI continues to work on the De-Cashing Strategy, which will be published by the end of June 2018. This topic has become even more important in the light of the liquidity pressures in the banking system. The objective of reducing currency in circulation and moving towards innovative payment services (such as online and mobile payments) is part of the fight against the parallel financial system and tax evasion. The strategy will contain an action plan for the short term that aims to limit cash payments within the public administration and adapting the regulatory framework for electronic payments. Finally, with the assistance of the *Kreditanstalt für Wiederaufbau (KfW)*, we are exploring a strategy to increase financial access for small and medium-sized businesses through the *Banque de Région* (approved by the Government in February 2018). In the medium term, we also aim to unify and strengthen other state instruments to support SMEs.

- **Improving the safeguards framework of the CBT.** To date, we have made progress in implementing the recommendations of the IMF safeguards assessment mission. In this context, and concerning: (i) risk management, we have drafted a text establishing the Risk Committee; (ii) the lender as a last resort framework, we issued a circular in December 2016 to regulate the framework. In addition, and to consolidate the controls on liquidity lending operations, the Bank prepared and shared a circular in March 2017 on the operational framework underpinning the conduct of monetary policy; (iii) as regards an external assessment of the internal audit function, the CBT's General Control Directorate will first carry out a self-assessment before resorting to an external evaluation.
- **Reinforcing our AML/CFT framework and combatting the parallel economy.** Under the leadership of the Financial Intelligence Unit "the Tunisian Commission for Financial Analysis (CTAF)", the commitments made under the action plan agreed with the Financial Action Task Force (FATF) are progressing. Tunisia has made progress since the adoption of the action plan in November 2017:
 - The government published a new decree on 4 January 2018 on the freezing of terrorist assets.
 - The Government has adopted two draft laws. The first law amends the 2015 AML/CFT law to consider, in particular, the fight against proliferation. The second law will deal with the commercial register, the register of effective beneficiaries, and the register of associations. Their adoption by Parliament is expected by June.
 - On 5 April 2018, the CTAF published six new decisions guiding the designated non-financial businesses and professions (DNFBPs), including accountants, lawyers, notaries, real estate agents, jewelers and casinos, on the detection and reporting of suspicious transactions. The CTAF organized awareness raising days for these professions. The government has issued ministerial orders on the same subject.
 - The Board of the *Ordre des Experts Comptables* has published standards on due diligence measures for accountants.

- In this context, the CTAF organize a workshop for more than 50 controllers of the various professions grouped under the DNFBPs as well as associations with a view to prepare an operational manual for the control function.
- Banks, Financial Market and Insurance Authorities finalized their risk assessments and have started to implement controls and imposed sanctions, based on a risk-based approach.
- The CTAF has strengthened its human resources by hiring 12 new staff members.
- As part of our efforts to refine the regulatory framework governing the banking sector in the area of Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT), the CBT has prepared a draft amendment to Circular No. 2017-08 to ensure full compliance with international standards, particularly taking into account the latest updates of the FATF Recommendations (February 2018).

Use of Public Resources

22. Actions that support fiscal consolidation continue:

- **Better managing state-owned enterprises.** The implementation of the performance contracts with four large state-owned enterprises allows us to monitor their financial situation, thanks to the dashboards of key indicators (particularly financial indicators) for the 30 largest state-owned enterprises, which is now operational at the Directorate General of Participations (DGP). We will also sign a performance contract with TUNISAIR that reflects the company's commitments made in its restructuring plan (*SB* for December 2018).
- **Exploiting the results of functional reviews.** The last outstanding functional review, involving the Ministry of Equipment, has been completed and validated (*met SB*). The information from all functional reviews to date is closely aligned with the priorities established by our Civil Service Reform Strategy, including improving management of human resources, the redeployment of excess staff to address potential staffing needs in other areas (especially in the interior regions), and the simplification of the pay and benefits system.

Table 1. Quantitative Performance Criteria and Indicative Targets 1/
(Cumulative flow since the beginning of the year, unless otherwise indicated)

	2016		2017											
	Dec.		Mar.		Jun.			Sep.				Dec.		
	Act.	Prog.	Ind.	Act.	Prog.	Adj.	Act.	Prog.	Ind.	Act.	Prog.	Adj.	Act.	Prog.
Quantitative Performance Criteria 2/														
1. Floor on the primary balance of the central government (cash basis excl. grants, millions of TD) 3/	-3,951	Not Met	-814	-92	-1,247	-1,247	-3,123	Not Met	-1,141	-2,868	-3,784	-3,784	-3,959	Not Met
2. Ceiling on total current primary expenditure of the central government (millions of TD) 3/	19,054	Met	5,244	5,574	10,379	10,379	10,284	Met	14,932	14,702	21,757	21,757	21,823	Not Met
3. Floor on social spending (millions of TD) 6/	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
4. Ceiling on net domestic assets of the Central Bank of Tunisia (stock, millions of TD) 4/	5,094	Not Met	2,363	5,351	5,500	5,605	6,640	Not Met	4,337	6,761	3,834	1,684	7,062	Not Met
5. Floor on net international reserves of the Central Bank of Tunisia (stock, millions of US\$) 5/	3,335	Not Met	4,773	3,105	2,906	2,884	2,951	Met	3,311	3,117	2,937	3,660	3,120	Not Met
Continuous Performance Criteria														
• Ceiling on the accumulation of new external debt payment arrears by the central government (millions of US\$)	0	Met	0	0	0	n.a.	0	Met	0	0	0	n.a.	0	Met
Quantitative Indicative Targets														
• Ceiling on the accumulation of new domestic arrears (millions of TD)	0	Met	0	0	0	n.a.	0	Met	0	0	0	n.a.	0	Met
• Floor on social spending (millions of TD) 6/	1,411	Not Met	285	589	965	n.a.	1,132	Met	1,226	1,502	1,533	n.a.	1,844	Met
Program assumptions on which adjusters are calculated in case of deviations														
• External financing of the central government (excluding IMF, millions of US\$) 7/	1,555		475	992	2,166		2,196		3,007	2,757	3,226		3,419	
• of which: multilateral and bilateral budget grants (millions of US\$)	57		0	0	0		0		48	14	108		75	
• Public external debt service (interest and amortization, millions of US\$)	1,431		270	263	1,055		1,080		1,481	1,521	1,823		1,902	
• Bank recapitalization and civil service reform costs (millions of TD)	0		0	0	0		0			0			0	
• Privatization receipts in FX (millions of US\$)	0		0	0	0		0			0			0	
• Estimated cost of liquidating the Banque Franco Tunisienne (BFT, millions of TD) 3/	n.a.		n.a.	n.a.	n.a.		n.a.		n.a.	n.a.	n.a.		n.a.	
• Residents' FX deposits at the Central Bank of Tunisia (millions of US\$) 5/ 8/	908		-1,269	960	960		963		960	963	960		1,224	
• FX swaps between the Central Bank of Tunisia and commercial banks (millions of TD) 5/ 8/	445		603	453	453		393		453	594	453		1,147	
• FX swaps between the Central Bank of Tunisia and commercial banks (millions of US\$) 5/	221		299	225	225		195		225	295	225		570	
• Program exchange rate TD/US\$	2.01285		2.01285	2.01285	2.01285		2.01285		2.01285	2.01285	2.01285		2.01285	

Source: IMF staff estimates.

1/ Quantitative performance criteria and adjusters are described in the Technical Memorandum of Understanding. Further, for purposes of calculating program adjusters, foreign currency amounts will be converted at program exchange rates.

2/ From 2018 onwards, the test dates for quarterly QPCs will be end-March, end-June, end-September, and end-December.

3/ From end-June 2018 onwards, the adjuster on bank liquidation no longer applies.

4/ End of period. From 2018 onwards, the adjuster on FX swaps between the Central Bank of Tunisia and commercial banks will no longer apply.

5/ From 2018 onwards, the adjuster on FX swaps between the Central Bank of Tunisia and commercial banks, and that on residents' FX deposits at the Central Bank of Tunisia will no longer apply.

6/ Social spending includes social transfers and programs as well as key ministries' capital expenditures. Its coverage was expanded in 2017. Besides, the quantitative indicative target on social spending will be converted into a quantitative performance criterion from September 2018 onwards.

7/ Disbursement, includes project loans and capital market access, but excludes IMF.

8/ At program exchange rate.

Table 1. Quantitative Performance Criteria and Indicative Targets (concluded) 1/
(Cumulative flow since the beginning of the year, unless otherwise indicated)

	2018												2019																	
	Mar.			Prog.	Apr.		May		Jun.		Jul.		Aug.		Sep.		Oct.		Nov.		Dec.		Jan.		Feb.		Mar.			
	Prog.	Adj.	Act.		Ind.	Act.	Ind.	Act.	Prog.	Ind.	Ind.	Prog.	Ind.	Ind.	Prog.	Ind.	Ind.	Prog.	Ind.	Ind.	Prog.	Ind.	Ind.	Prog.	Ind.	Ind.	Prog.	Ind.	Ind.	
Quantitative Performance Criteria 2/																														
1. Floor on the primary balance of the central government (cash basis excl. grants, millions of TD) 3/	-1,722	-1,722	545	Met	n.a.	n.a.	n.a.	n.a.	-2,961	n.a.	n.a.	-2,760	n.a.	n.a.	-3,151	n.a.	n.a.	-394												
2. Ceiling on total current primary expenditure of the central government (millions of TD) 3/	6,237	6,237	5,185	Met	n.a.	n.a.	n.a.	n.a.	11,517	n.a.	n.a.	17,566	n.a.	n.a.	23,616	n.a.	n.a.	6,032												
3. Floor on social spending (millions of TD) 6/	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1,766	n.a.	n.a.	2,382	n.a.	n.a.	656												
4. Ceiling on net domestic assets of the Central Bank of Tunisia (stock, millions of TD) 4/	9,374	9,279	8,244	Met	n.a.	n.a.	n.a.	n.a.	8,150	n.a.	n.a.	7,387	n.a.	n.a.	6,855	n.a.	n.a.	6,602												
5. Floor on net international reserves of the Central Bank of Tunisia (stock, millions of US\$) 5/	2,352	2,400	2,408	Met	n.a.	n.a.	n.a.	n.a.	2,966	n.a.	n.a.	3,075	n.a.	n.a.	3,153	n.a.	n.a.	3,186												
Continuous Performance Criteria																														
• Ceiling on the accumulation of new external debt payment arrears by the central government (millions of US\$)	0	n.a.	0	Met	n.a.	n.a.	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0												
Quantitative Indicative Targets																														
• Ceiling on the accumulation of new domestic arrears (millions of TD)	0	n.a.	0	Met	n.a.	n.a.	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0												
• Floor on social spending (millions of TD) 6/	721	n.a.	735	Met	n.a.	n.a.	n.a.	n.a.	1,144	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.												
Program assumptions on which adjusters are calculated in case of deviations																														
• External financing of the central government (excluding IMF, millions of US\$) 7/	209		292		n.a.	n.a.	n.a.	n.a.	1,640	n.a.	n.a.	2,400	n.a.	n.a.	3,506	n.a.	n.a.	104												
of which: multilateral and bilateral budget grants (millions of US\$)	0		1		n.a.	n.a.	n.a.	n.a.	1	n.a.	n.a.	71	n.a.	n.a.	136	n.a.	n.a.	0												
• Public external debt service (interest and amortization, millions of US\$)	466		502		n.a.	n.a.	n.a.	n.a.	994	n.a.	n.a.	1,353	n.a.	n.a.	1,789	n.a.	n.a.	635												
• Bank recapitalization and civil service reform costs (millions of TD)	0		0		n.a.	n.a.	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0												
• Privatization receipts in FX (millions of US\$)	0		0		n.a.	n.a.	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0	n.a.	n.a.	0												
• Estimated cost of liquidating the Banque Franco Tunisienne (BFT, millions of TD) 3/	0		0		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.												
• Residents' FX deposits at the Central Bank of Tunisia (millions of US\$) 5/ 8/	n.a.		n.a.		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.												
• FX swaps between the Central Bank of Tunisia and commercial banks (millions of TD) 5/ 8/	n.a.		n.a.		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.												
• FX swaps between the Central Bank of Tunisia and commercial banks (millions of US\$) 5/	n.a.		n.a.		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.												
• Program exchange rate TD/US\$	2.01285		2.01285		n.a.	n.a.	n.a.	n.a.	2.01285	n.a.	n.a.	2.01285	n.a.	n.a.	2.01285	n.a.	n.a.	2.01285												

Source: IMF staff estimates.

1/ Quantitative performance criteria and adjusters are described in the Technical Memorandum of Understanding. Further, for purposes of calculating program adjusters, foreign currency amounts will be converted at program exchange rates.

2/ From 2018 onwards, the test dates for quarterly QPCs will be end-March, end-June, end-September, and end-December.

3/ From end-June 2018 onwards, the adjuster on bank liquidation no longer applies.

4/ End of period. From 2018 onwards, the adjuster on FX swaps between the Central Bank of Tunisia and commercial banks will no longer apply.

5/ From 2018 onwards, the adjuster on FX swaps between the Central Bank of Tunisia and commercial banks, and that on residents' FX deposits at the Central Bank of Tunisia will no longer apply.

6/ Social spending includes social transfers and programs as well as key ministries' capital expenditures. Its coverage was expanded in 2017. Besides, the quantitative indicative target on social spending will be converted into a quantitative performance criterion from September 2018 onwards.

7/ Disbursement, includes project loans and capital market access, but excludes IMF.

8/ At program exchange rate.

Table 2. Prior Actions and Structural Benchmarks

Prior Actions	Objective			
✓ Foreign exchange interventions. Compliance with the monthly intervention budget in April and May.	<i>Exchange rate flexibility</i>			Met
✓ Fuel prices. (1) Adoption of a ministerial order announcing a significant increase in the prices of the three main fuel products in June; and (2) public announcements of (i) the cap on energy subsidies at 2.5 percent of GDP (2,700 million dinars) in 2018; (ii) a monthly price adjustment for the three main fuel products from July; and (iii) an additional one-off price correction in October if the energy subsidy budget were likely to be exceeded.	<i>Fiscal sustainability and fairness</i>			Met
✓ Social protection. Public announcements of an increase in social transfers for vulnerable households.	<i>Social protection and fairness</i>			Met
Structural Benchmarks	Objective	Date	Revised Date	Status
I. Sectoral reforms/private sector development				
✓ Operationalization of the investment code. Establishment of a one-stop investment agency.	<i>Private sector development</i>	May-18		Met
• High anti-corruption and good governance authority (HACGGA). Signature of the decree appointing the members of the HACGGA.	<i>Good governance and fairness</i>	Jun-18	Dec-18	Not met
• Social policy. Establishment of a databank on vulnerable households.	<i>Social protection and fairness</i>	Dec-18		
II. Financial sector reform				
• Banque Franco Tunisienne (BFT). Vote of the resolution committee on the orderly resolution of the BFT.	<i>Financial sector stability</i>	May-18	Aug-18	Not met
• Maximum lending rate. Adoption by Parliament of a law and decree on increasing the maximum lending rate for corporates and SMEs from +20 percent above the average lending rate to +33 percent.	<i>Financial sector stability</i>	May-18	Dec-18	Not met. Draft law in Parliament. Augmentation limited to +20% for individuals.
✓ Portfolio quality. Adoption by Parliament of (i) a law to make it possible for public banks to abandon claims on credits like their private peers (both in the context of the insolvency law and outside of this context); and (ii) a law simplifying write-off rules, eliminating the requirement for a final judgment.	<i>Financial sector stability</i>	Jun-18		Met
III. Fiscal policy and reforms of public institutions				
• Fuel prices. Quarterly application of the automatic fuel price adjustment mechanism.	<i>Fiscal sustainability and fairness</i>	Mar-18 until end of program		Not met at end-March.
✓ Pensions. Adoption, by the Council of Ministers, of the comprehensive pension reform strategy to ensure financial sustainability.	<i>Fiscal sustainability and fairness</i>	Apr-18		Not met, but fully implemented on June 20.
✓ Functional review. Completion of the functional review of four ministries (Health, Education, Finance, and Infrastructure).	<i>Fiscal sustainability and quality public services</i>	Jun-18		Met
• State-owned enterprises (SOEs). Signature of a performance contract for TUNISAIR.	<i>Better monitoring of fiscal risks</i>	Dec-18		
• Organic budget law. Publication, in the official journal, of the Organic Budget Law.	<i>Fiscal sustainability and fairness</i>	Dec-18		Draft law in Parliament.
• Value-added tax (VAT). Increase of the VAT rate for liberal professions from 13 to 19 percent.	<i>Fiscal sustainability and fairness</i>	Dec-18		
• Large Taxpayers Unit (DGE). Operationalization of the transfer, and merger, of control (in-depth verification) and tax arrears management (recovery) functions into the new umbrella structure for tax administration (created by the 2018 budget law).	<i>Fiscal sustainability and fairness</i>	Jul-18		Dropped because the authorities opted for a different and more comprehensive reform path. This change in strategy is not macro critical given continued revenue performance.
• Large Taxpayers Unit (DGE). Transfer of control (in-depth verification) and tax arrears management (recovery) functions for large enterprises to the DGE and their operationalization.	<i>Fiscal sustainability and fairness</i>	Dec-18		
IV. Monetary and exchange rate policies				
• Foreign exchange auctions. Implementation of a full foreign exchange auction mechanism by the Central Bank of Tunisia.	<i>Exchange rate flexibility</i>	Jun-18	Aug-18	Not met

Attachment II. Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) establishes the agreement between the Tunisian authorities and IMF staff concerning the definition of the **quantitative criteria and targets** under the program supported by the Extended Fund Facility (EFF). They are defined in Table 1 of the Memorandum of Economic and Financial Policies (MEFP) attached to the Letter of Intent dated June 22, 2018.

2. This TMU also sets out the **content and frequency of data reporting** to IMF staff for program monitoring purposes. To this aim, 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 TMU, unless otherwise agreed with IMF staff.

DEFINITION OF PERFORMANCE CRITERIA AND INDICATIVE TARGETS

A. Performance Criteria and Indicative Targets

3. The **quantitative criteria and targets** specified in MEFP Table 1 are:

- **Quantitative Performance Criteria (QPC):**

- (1) (quarterly floor) on the **primary balance** of the central government (cash basis, excluding grants);
- (2) (quarterly ceiling) on total **current primary expenditure** of the central government;
- (3) (quarterly floor) on **social spending** (starting from end-September 2018);
- (4) (quarterly ceiling) on **the net domestic assets** (NDA) of the CBT;
- (5) (quarterly floor) on **the net international reserves** (NIR) of the CBT; and
- (6) (quarterly ceiling) on **net foreign exchange interventions** of the CBT (starting from end-September 2018).

- **Continuous Performance Criterion (CPC):**

- (7) (zero ceiling) on the **accumulation of new external debt payment arrears**.

- **Indicative Targets (IT):**

- (8) (quarterly ceiling) on **accumulation of new domestic payment arrears**;
- (9) (monthly ceiling) on **net foreign exchange interventions** of the CBT; and
- (10) (quarterly floor) on **social spending** (through end-June 2018).

4. **Measurement of criteria.** The QPCs on the central government's (1) primary balance (cash basis, excluding grants), (2) total current primary expenditure, and (3) social spending are measured

on a quarterly basis and cumulatively from the end of the previous year. The QPCs on the CBT's (1) NDA and (2) NIR are measured on a quarterly and stock basis. The QPC on the CBT's net foreign exchange interventions is measured on a quarterly and non-cumulative basis. The CPC on the accumulation of new external debt payment arrears is measured on a continuous basis. The IT on the CBT's net foreign exchange interventions is measured on a monthly and flow basis. The other ITs on (1) the accumulation of new domestic payment arrears and (2) social spending are measured on a quarterly and cumulative basis. Adjustment factors will apply to some of these criteria.

5. Valuation. For program purposes, all assets, liabilities, and flows denominated in foreign currencies will be valued at the "program exchange rate" (as defined below), except for items affecting the government's budgetary accounts (which will be measured at current exchange rates). The program exchange rate corresponds to the CBT's accounting exchange rate that prevailed on December 31, 2015, as shown in the table below. For the SDR, the program exchange rate is 1 SDR = 2.797590 Tunisian dinars. Moreover, monetary gold assets will be valued against the corresponding value in Tunisian dinars (at the program exchange rate) at the price of 2,138.15 Tunisian dinars per ounce of gold in the international market on December 31, 2015 (London morning fixing). The stock of gold is 4.13 tons (4,129,806 grams) on December 31, 2015.

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
KRW	0.001707098
CNY	0.3102
SAR	0.53634
SEK	0.23918
US\$	2.01285

B. Institutional Definition

6. 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. The authorities will inform IMF 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 Primary Balance of the Central Government (Cash Basis, Excluding Grants)

7. Under the program, the **primary balance of the central government (cash basis, excluding grants)** is measured on a financing basis and will be the negative sum of the following: (1) total net external financing; (2) privatization receipts; (3) net domestic bank financing; (4) net domestic nonbank financing; *plus* (5) interest on domestic and external debt paid by the central government; and *less* (6) external budgetary grants received by the central government.

8. **Net external financing** is defined as net external loans of the central government, i.e. new loan disbursements *less* repayments of the principal. Also included are project and budgetary loans of the central government, and any form of debt used to finance central government operations.

9. **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.

10. **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 deposits of the central government at the CBT. The latter includes all central government accounts at the CBT, in particular: the (1) Treasury current account excluding the sub accounts N-bis, those related to Public Administrative Entities (EPA) and to local governments; (2) Tunisian government account (miscellaneous dinar accounts); (3) loan accounts; (4) grant accounts; (5) accounts of *Fond National de Promotion de l'Artisanat et des Petits Métiers* and *Fonds de Promotion et de Décentralisation Industrielle* ("FONAPRA-FOPRODI account"); (6) special accounts of the Tunisian government in foreign currency; (7) accounts in foreign currency pending dinarization (subaccount: "mise à disposition"); (8) 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 Gouvernement* and *Comptes Spéciaux du Gouvernement*) on the CBT's balance sheet (liabilities side).

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

12. 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 do not include accrued interest.

D. Ceiling on Total Current Primary Expenditure of the Central Government (Excluding Interest Payments on Public Debt)

13. Under the program, **total current primary expenditure of the central government** is defined as the sum of its expenditure on the following items: (1) personnel wages and salaries; (2) goods and services; (3) transfers and subsidies; and (4) other unallocated current expenditure.¹

E. Floor on Social Spending

14. Under the program, **social spending** is defined as capital expenditures (development expenditures) on education; health; social transfers to low-income families, employment training programs (and university scholarships), *Union Tunisienne de Solidarité Sociale* (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. Excluded are All current expenditures ("dépenses de gestion") of the above-mentioned sectors and programs, as well as food and energy subsidies.

F. Ceiling on Net Domestic Assets of the CBT

15. Under the program, the **CBT's net domestic assets** (NDA) are defined as the difference between the monetary base and the net foreign assets of the CBT.

16. The **monetary base** includes the following: (1) fiduciary money (i.e. money in circulation excluding cash balances of banks and the Treasury); (2) deposits of banks at the CBT (including foreign currency and deposit facility); and (3) deposits of all other sectors at the CBT (i.e. other financial enterprises, households, and companies).

¹ 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.

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

18. The Directorate General of Statistics (i.e. Directorate of Monetary and Financial Statistics) will be responsible for **monthly forecasts of reserve money** and will calculate NDA projections for the next six months. These projections will be submitted to IMF staff, after consultation with the Directorate General of Monetary Policy.

G. Floor on the Net International Reserves of the CBT

19. Under the program, the **CBT's net international reserves (NIR)** are defined as the difference between the its reserve assets and its liabilities in foreign currency to nonresidents.

20. The **CBT's reserve assets** are the foreign assets immediately available and under 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.

21. The **CBT's liabilities in foreign currency** to nonresidents include any commitment to sell foreign currencies associated with financial derivative transactions (e.g., swaps, futures, options); any portion of the CBT's assets (e.g., gold) 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. Those liabilities do neither include the government's foreign currency deposits at the CBT, nor any SDR allocation received after March 31, 2017.

22. 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 clearly that (1) 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; (2) debt is a liability of the central government; and (3) a protocol between the CBT and the MoF 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.

23. The value of **CBT reserve assets and liabilities** in foreign currency will be calculated using program exchange rates (Table above). On December 31, 2017, the value of the stock of NIR reserves was US\$3,120.2 million, with the stock of reserve assets equal to US\$5,480.6 million and the stock of CBT liabilities in foreign currency equal to US\$2,360.4 million (at program exchange rates).

H. Ceiling on Net Foreign Exchange Interventions of the CBT

24. Under the program, the CBT's **net foreign exchange interventions** are defined as the difference between outright foreign exchange sales (including conversions) and outright foreign

exchange purchases (including conversions), via the following channels: Reuters, auctions, and the interbank market. The computation of net sales may also include CBT net sales in other formal or informal markets (or instruments) that the CBT may choose to substitute for outright net sales (e.g., transactions in derivatives). Transactions of the CBT with the central government in the context of budget operations of the central government are not considered net sales (unless they take place through one of the channels mentioned above). In this respect, purchases of the foreign currency proceeds of a potential Eurobond or other official financing cannot be interpreted as CBT purchases of foreign exchange for the computation of the CBT net sales total.

I. Ceiling on the Accumulation of External Arrears

25. Under the program, **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*² by the central government or the CBT from the due date or the expiration of the applicable grace period.

J. Ceiling on the Accumulation of Domestic Arrears

26. Under the program, **arrears on domestic payments** 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.

K. Adjustment Factors for the QPCs

27. The **primary fiscal balance** targets (cash basis, excluding grants) are adjusted upward/downward based on the amount used to (1) recapitalize public banks and (2) finance the severance pay of the voluntary departures which may be part of the civil service reform.

² 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: (1) loans, that is, advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the 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); (2) 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 (3) 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.

28. The **NDA** targets are adjusted upward (downward) if (1) the cumulative sum of external budget financing (including grants and loans, excluding from the IMF) and privatization receipts received by the central government in foreign currency is lower (greater) than the levels indicated in MEFP Table 1. The NDA targets are also adjusted upward (downward) if (2) the total amount of cash payments on external debt service are greater (lower) than the levels included in the MEFP Table 1. The NDA ceiling will be converted into Tunisian dinars at the program exchange rate specified in the table above, and adjusted downward (upward) based on (3) the amount of CBT reserves released (mobilized) because of a possible decrease (increase) in the reserve requirement.

29. The **NIR** targets are adjusted upward (downward) if (1) the cumulative sum of external budget financing (including grants and loans, excluding from the IMF) and privatization receipts received by the central government in foreign currency is greater (lower) than the levels observed in MEFP Table 1. The NIR targets will also be adjusted upward (downward) if (2) the total amount of cash payments on external debt service of the government is lower (greater) than the levels included in the MEFP Table 1.

L. Monitoring and Reporting Requirements

30. 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) Annual (a)	Delay (in Days)	Responsible Department
Real Sector			
• 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:			
○ 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.	m	30	MoF
○ 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).	m	60	MoF
○ External and domestic debt service: amortization and interest.	m	60	MoF

Information to Be Reported in the Context of the Program (continued)			
Type of Data and Description	Periodicity Weekly (w) Monthly (m) Quarterly (q) Annual (a)	Delay (in Days)	Responsible Department
○ 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: with a breakdown of the stock of deposits 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).	q	30	CBT
○ Total disbursements of external debt of institutional agents by type of currency (in foreign currency with its equivalent in dinar).	q	30	CBT
○ Stock of external debt of institutional agents by type of currency (in foreign currency and its equivalent in dinars).	q	90	CBT
○ Overall net external position of Tunisia (in conformity with our obligations under SDDS).	a	180	CBT
● Balance of payments: prepared by the CBT.	q	30	CBT
Monetary and Financial Sector			
● CBT accounts at the current exchange rate: monthly situation of the Central Bank by sector (figures at the end of the period).	m	15	CBT
● Reserve money and net domestic assets (NDA): monthly forecast.	m	15	CBT

Information to Be Reported in the Context of the Program (continued)			
Type of Data and Description	Periodicity Weekly (w) Monthly (m) Quarterly (q) Annual (a)	Delay (in Days)	Responsible Department
<ul style="list-style-type: none"> • Monetary policy operations and liquidity factors: daily and monthly balances. Detailed table including: i) intervention on the money market of the central bank (Dinars); (ii) deposit facility; (iii) ordinary tenders (iv) loan facility; (v) overnight lending; (vi) repo at 1-7 days and 3 months; (vii) FX swap exchange; (viii) open market operations; (ix) minimum reserves; and (x) excess reserves. 	m	15	CBT
<ul style="list-style-type: none"> • Monetary survey at the current exchange rate: monthly balance of the banking sector, counterparts of broad money, leasing banks, and resources of the resident financial system; preliminary (30 days) and definitive (45 days). 	m	30 and 45 days	CBT
<ul style="list-style-type: none"> • Interest rates of financial operations: detailed tables on lending and savings rates and effective global tariffs produced by the Observatory of Financial Inclusion. 	m	30	CBT
<ul style="list-style-type: none"> • Credit data: monthly data on credit distribution by sector (private/public); credit to enterprises (by economic sector); and credit to individuals (by purpose). 	m	30	CBT
<ul style="list-style-type: none"> • Foreign exchange market operations, interbank market, retail market and wire transfers for CBT purchases on the retail market: <ul style="list-style-type: none"> ○ CBT interventions (sales and purchases) on the foreign exchange market in million of dinars (and equivalent in US million) including total market transactions, foreign exchange sales to energy companies and all exchange rates for all such transactions, total FX demand by banks, total FX positions of banks, 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. 	w	1	CBT
<ul style="list-style-type: none"> • IMF account statements: monthly consolidated statements of the IMF No. 1, No. 2, and Securities Account. 	m	30	CBT
<ul style="list-style-type: none"> • 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

Information to Be Reported in the Context of the Program (concluded)			
Type of Data and Description	Periodicity Weekly (w) Monthly (m) Quarterly (q) Annual (a)	Delay (in Days)	Responsible Department
<ul style="list-style-type: none"> • Direct refinancing of commercial banks by the CBT: breakdown by bank. 	m	14	CBT
<ul style="list-style-type: none"> • NPLs: stock of banking sector NPLs and breakdown by commercial banks. 	q	60	CBT
<ul style="list-style-type: none"> • 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			
<ul style="list-style-type: none"> • 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
<ul style="list-style-type: none"> • Petroleum: price structure of the petroleum products and the needed data to monitor the automatic adjustment mechanism (formulas and data). 	d	15	Min. of Energy

**Statement by Mr. Jafar Mojarrad, Executive Director for Tunisia,
Mr. Cyrus Sassanpour, Senior Advisor, and Ms. Monia Saadaoui. Advisor
July 6, 2018**

Our Tunisian authorities extend their great appreciation to staff for the constructive dialogue and sound policy advice, and a well-written and balanced report, and to the Executive Directors and Fund management for their continued support.

Overview

Program implementation gained momentum in 2018 and has improved since the Second Review, despite the persistence of a challenging external environment, including spillover of the regional refugee crisis, greater risk aversion, and rising oil prices. Domestically, the difficulty of maintaining public support for the program should not be discounted as “reform dividend” is slow to emerge and austerity measures continue to squeeze the purchasing power of low to mid-income Tunisians and tax their patience.

Despite the unfavorable conditions, all Quantitative Performance Criteria (QPCs) for end-March were met; all Quantitative Indicative Targets were observed; all Quantitative Prior Actions for the Third Review were completed; and significant progress was made on structural reforms. Three of the nine of Structural Benchmarks (SBs) were met; two were not met on time, but one (on Banque Franco Tunisienne—BFT) will be met with delay in August; one was dropped as it was no longer important for the success of the program (elaborated below); and the remaining three were reprogrammed as the authorities sought to rationalize the number of SBs and prioritize their effective implementation. The authorities are requesting waiver of applicability for all end-June QPCs since relevant data will only be available after the Board discussion.

The authorities recognize that 2018 is a pivotal year for the turnaround of the Tunisian economy and are determined to stay on course with program implementation to address the economy’s vulnerabilities and restore sound macroeconomic fundamentals, despite risks to the outlook. They are in broad agreement with staff on the sources of risks to the outlook, but are of the view that the staff’s Risk Assessment Matrix could be better presented by not duplicating the refugee problem and risks to global growth and trade, which appear in the Matrix as both domestic and external risks.

Macroeconomic stabilization, ensuring adequate social protection during adjustment, and promoting private sector-led growth and job creation continue to be the pillars of the program. It is a home-grown-and-owned program and maintaining public support and political consensus for the program ultimately hinges on the conviction that there is indeed light at the end of the tunnel and that there are significant reform dividends for all Tunisians.

Recent Economic Development

Economic recovery has found traction, and real GDP growth in 2018 is now expected at 2.4 percent—the highest rate since 2014—benefiting from the revival of tourism, higher phosphate production, and growing exports due to gains in competitiveness and robust EU demand. Inflation, however, accelerated to 7.7 percent in May, the highest level since 1991, reflecting a number of one-off factors, as well as a combination of demand-pull and cost-push elements, including the pass-through of a sizable exchange rate depreciation, robust credit growth, past public-sector wage awards, and rising international oil prices. The fiscal deficit remained unchanged at 5.9 percent of GDP in 2017, largely due to higher subsidies and transfers, notwithstanding higher revenue. Recovery of tourism and higher exports and remittances narrowed the current account deficit, despite higher oil imports, but foreign reserves fell, reflecting large debt amortization. Both public debt and external debt ratios increased in 2017, which also reflected the impact of exchange rate depreciation.

Fiscal Policy

Fiscal retrenchment is at the core of macroeconomic stabilization, and the authorities are fully committed to the program's fiscal consolidation path that envisages a 1 percent of GDP per year reduction in the overall deficit to 2.5 percent of GDP by 2020, and anchors public debt on a firm downward path. In 2018, despite a 12 percent increase in tax receipts and a 9 percent cut in the wage bill during the first quarter, the deficit target of 5.2 percent of GDP came under pressure due to larger-than-anticipated international oil prices; lower-than-anticipated number of civil servants taking advantage of government's voluntary departure and early retirement schemes; higher transfers to the public pension fund to meet its larger-than-anticipated liquidity deficit; and higher social transfers.

To put the program back on track, the authorities are making additional fiscal effort—mainly through expenditure cutting measures—equivalent to 2 percent of GDP during the second semester of 2018 or 4 percent of GDP on an annual basis. Specifically, the bulk of higher energy subsidies (0.8 percent of GDP) will be met through monthly adjustments in prices of automobile fuels starting in July on top of the June price hike; increases in gas and electricity tariffs for corporate consumers; and by controlling leakages. The authorities are prepared to make further fuel price adjustments in October should the subsidies exceed projections. The adjustment in June, the subsequent monthly adjustments, and the possible additional adjustment in October have already been publicly announced. Social transfers will increase by 0.1 percent of GDP to partially defray the impact of fuel price increases.

Containing the government wage bill—currently around 14 percent of GDP—is another key element of fiscal consolidation plans. Applications for voluntary departure and early retirement so far have been lower than expected. To reach the wage bill target of 12.4 percent of GDP by 2020, the government has called for a second round of voluntary departures next month and strict limits on new hires this year and next. The government is further committed

not to grant any wage increases in 2018, and to consider increases in 2019 only if growth surprises on the upside, but even then, the 2020 target will remain the focus.

The government also adopted a comprehensive reform on June 20, 2018 to reduce the financial imbalances of the two pension funds (public CNRPS and private CNSS) and the medical insurance fund (CNAM). Parliamentary approval is expected by end-September, effective retroactively from July 1. As mentioned earlier, the government will make an additional transfer of 0.4 percent of GDP in 2018 to CNRPS to meet part of its liquidity shortfall, with the remaining shortfall as well as the deficit of the CNSS to be covered by greater effort to collect contribution arrears, including from state-owned companies.

Looking beyond 2018, stronger focus will be placed on revenue generation. The authorities plan to converge the “onshore” and “offshore” tax regimes with the 2019 budget and to raise the VAT rate for liberal professions (including lawyers, doctors, accountants). Tax administration will be also strengthened, modernized and be made more efficient by merging the two ministry of finance departments dealing with tax assessment, accounting and collection along the French model. Since the reforms will serve the same purpose, the SBs on the new Large Taxpayers Unit were no longer deemed necessary and dropped.

Social Protection

The authorities believe that adequate social protection to alleviate the economic hardship of adjustment is critical for maintaining public acceptance of reforms. With that in mind, the program has a floor on social spending for vulnerable groups—mostly in the form of cash transfers, healthcare support, education scholarships and job training programs—which in fact was exceeded at end-March. Further, as a reflection of their strong commitment to social protection, the authorities intend to elevate the current indicative target on social spending to a QPC from September. They have already broadened the coverage of vulnerable families and are planning to finalize improvements in data base and targeting by end-2018, with the assistance of the World Bank.

Monetary and Exchange Rate Policy

Fighting inflation continues to be the main priority of the Central Bank of Tunisia (CBT), consistent with its mandate. Although, the key policy interest rate was increased twice in 2018 for a total of 175 basis points, money market rates remain negative in real terms, and private sector credit fueled by central bank refinancing is still growing, jeopardizing price stability. The authorities feel it is prudent to tighten monetary policy to avoid unhinging inflation expectations and eroding central bank credibility, and to that end, are determined to raise policy rates until the real money market rates are firmly in the positive territory, which would also help reduce central bank refinancing. The effectiveness of monetary policy will be further enhanced through better public communication and strengthening the monetary transmission mechanism by gradually relaxing interest rate caps on business loans, more

frequent updating of effective lending rates, and encouraging commercial banks to fund their lending operations in the interbank market, instead through central bank refinancing.

The Tunisian dinar has depreciated substantially in recent years in terms of REER (13 percent since the start of the program) and NEER (30 percent), with the latter largely reflecting the depreciation of the dinar versus the euro. REER depreciation has helped improve the current account deficit, but the authorities recognize that greater exchange rate flexibility—especially in view of the increasing inflation differential with the main trading partners—would help achieve a more sustainable current account position and improve foreign reserves coverage. Strict observance of program targets on net foreign exchange sales by the CBT in April and May helped keep the dinar on a flexible path and preserve foreign reserves. The CBT intends to begin to set up the framework for conducting more competitive foreign exchange auctions—with the help of Fund TA—and gradually limit its interventions to smoothing excessive market volatility. The authorities reaffirm their commitment to remove the restrictions on financing of non-priority imports by end-2018.

Financial Sector Stability

Financial sector indicators and bank profitability have improved, and the authorities are committed to accelerating financial sector reforms to underpin the success of the program and facilitate economic and financial inclusion. Addressing the high level of NPLs is a key issue, and recent parliamentary adoption of a set of laws placing NPL restructuring of public banks on the same footing as private banks is expected to facilitate NPL resolution of public banks. Further, the banking resolution committee in its first meeting on June 28 began reviewing the situation of the BFT with the vote on its orderly resolution expected by August. The Ministry of Finance and the Financial Sector Reform Committee intend to publish a comprehensive report on NPL resolution by end-2018, and have also made significant progress towards developing a national strategy for financial inclusion. In the context of rising interest rates and the rapid growth of private sector credit, the CBT is committed to ensuring financial sector soundness by strengthening its supervisory capacity, and will be working closely with METAC to develop tools for monitoring market and interest rate risks and assessing bank capital adequacy. The authorities are also reinforcing their AML/CFT framework and are making good on their commitments under the action plan agreed with FATF in November 2017, including a set of preventive measures adopted in 2018 (¶21 MEFP) that should help facilitate Tunisia’s exit from the FATF-enhanced surveillance list at an early date.

Supporting the Private Sector

Government support for the private sector has many dimensions, including facilitating investment, cutting administrative red tape, encouraging public-private-partnerships, and strengthening governance and fighting corruption. The new Tunisian Investment Authority has been set up as a “one-stop shop” for investors to ease burdensome administrative

procedures and speed up approvals. A government decree in May significantly reduced the number of authorizations required for investment by establishing an eight-sector negative list where prior authorization is mandatory, but even then, authorization is granted after the lapse of 60-90 days on a “silence is consent” basis. For all other sectors, no prior authorization is required. Fighting corruption is another important government priority and, to that end, the High Anti-Corruption and Good Governance Authority will become functional once its board members are appointed by Parliament following consultations among political parties—expected by September.

Conclusions

The challenging domestic conditions and heavy global and regional headwinds have not weakened the authorities’ resolve to press ahead with macroeconomic stabilization and structural reforms to secure sustainable high levels of growth with widespread benefits for all Tunisians. Maintaining political consensus and public support for the program is critical to its success. Tunisia is pressing at the limits of its program absorption capacity, and any further hardening or frontloading of the program in sensitive areas runs the risk of its rejection by the public. Tunisia has already benefitted greatly from, and will continue to rely on, Fund policy advice and technical assistance, for which the authorities are thankful. They also express their appreciation for the financial and technical assistance provided by their partners during this crucial transition and look forward to their continued support. The authorities will be thankful for Board approval of completion of the Third EFF Review, and waiver of applicability and modification of performance criteria.