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IMPLEMENTATION COMPLETION REPORT

REPUBLIC OF TUNISIA

ECONOMIC COMPETITIVENESS ADJUSTMENT LOAN

(LOAN 4069 – TUN)

December 29, 1998

Social and Economic Development Group
Middle East and North Africa Region

CURRENCY EQUIVALENTS

(Unit of Currency = Tunisian Dinar)

	1993	1994	1995	1996	1997
Tunisian Dinar per US$, period average	1.004	1.012	0.946	0.973	1.106
Tunisian Dinar per US$, end-of-year	1.047	0.991	0.951	0.999	1.148

FISCAL YEAR OF BORROWER

January 1 - December 31

ABBREVIATIONS AND ACRONYMS

CTN: *Compagnie Tunisienne de Navigation*
ECAL: Economic Competitiveness Adjustment Loan
EEC: European Economic Commission
ECU: European Currency Unit
EU: European Union
FTA: Free Trade Agreement
GDP: Gross Domestic Product
GOT: Government of Tunisia
IBRD: International Bank for Reconstruction and Development (World Bank)
IMF: International Monetary Fund
OC: *Office des Céréales*
ONH: *Office Nationale de l'Huile*
OPNT: *Office des Ports Nationaux de Tunisie*
STAM: *Société Tunisienne d'Acconage et de Manutention*
TD: Tunisian Dinar
UNO: United Nations Organizations
US: United States
VAT: Value Added Tax
WTO: World Trade Organization

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PREFACE

This is the Implementation Completion Report (ICR) for the Economic Competitiveness Adjustment Loan (ECAL) for Tunisia. The loan (loan 4069-TUN) was in the amount of US$75 million equivalent, approved on July 25, 1996 and made effective on December 6, 1996. The loan was closed on June 30, 1998, compared with the original closing date of December 31, 1997. The ECAL consisted of two tranches, one equal to US$37.5 million and the other equal to FRF193.9 million. The first tranche, released upon effectiveness, was fully disbursed by December 31, 1996; the second tranche was released on June 3, 1998, and the loan was fully disbursed by June 30, 1998. Parallel financing for the reform program was provided by the European Union in the amount of ECU100 million and disbursed in two tranches of ECU40 million and ECU60 million respectively.

The ICR was prepared by Auguste Tano Kouamé, Economist (MNSED), and reviewed by Ms. Daniela Gressani, Sector Leader (MNSED) and Mr. Paul Moreno-Lopez, Senior Country Economist (MNCMG). Useful comments were received from Ms. Marisa Fernandez-Palacios, Portfolio Manager, Mr. Hassan Fazel, Senior Country Economist, and Ms. Fatma Felah, Operations Analyst (MNCMG). The Task Managers for the operation were Ms. Miria Pigato, Senior Economist (DECPG) and Ms. Linda Likar, Principal Economist (MNSHD).

Preparation of this ICR is based on material in the project file and information collected through interviews of Staff and Government Officials. The Borrower contributed to the preparation of the ICR by commenting on the draft. The draft ICR was also discussed with the European Union.

IMPLEMENTATION COMPLETION REPORT

REPUBLIC OF TUNISIA

ECONOMIC COMPETITIVENESS ADJUSTMENT LOAN (LOAN 4069 – TUN)

EVALUATION SUMMARY

i. **Introduction.** Tunisia signed an Association Agreement with the European Union (EU) in July 1995. The Agreement entailed trade liberalization by a gradual phasing out of tariffs. Since the signing of the Association Agreement, the authorities have placed a stronger emphasis on improving the efficiency and international competitiveness of the economy with a view to easing its integration with Europe and the global economy. At the time this loan was prepared, many aspects of the international competitiveness of the Tunisian economy were in need of improvement. Though the real exchange rate has remained fairly stable, competitiveness has been hindered by high production and transportation costs, inadequate telecommunications services, labor market rigidities, limited and costly access to credit, and inadequate legal and incentives regimes.

ii. **Project Objectives.** The main objective of the Economic Competitiveness Adjustment Loan (ECAL) was to improve the international competitiveness of the Tunisian economy in the aftermath of the signing of the Association Agreement with the European Union, with a view to achieving a sustainable increase in the rate of economic growth. The ambition of the program was not to tackle every single issue relating to competitiveness, but to focus on key areas suitable for immediate policy actions, and leave other areas for future operations.

iii. The program supported five broad areas of policy reforms: a) Maintenance of a stable macroeconomic framework and fostering of a stable business environment; including by introducing fiscal measures to replace revenue losses from the expected tariff reforms; b) Acceleration of the implementation of the Association Agreement, including the elimination of tariff surcharges; thus easing domestic firms' access to capital and semi-finished goods used as inputs; b) Acceleration of the pace of privatization in competitive sectors and the opening up of new sectors to private capital so as to reduce inefficiencies and increase the role of the private sector in the economy; d) Reduce transaction costs and improve the regulatory and administrative environment in which enterprises operate, through lower transport costs, trade facilitation and an improved legislative framework; and e) Reduce labor costs by increasing flexibility in the labor market, particularly in lay-off procedures, while protecting workers and containing labor costs.

iv. The initial timeframe for the operation appeared to be rather tight in view of (i) the need for the Tunisian authorities to build broad support for some of the structural reforms (i.e. liberalization of maritime activities and adoption of a new Company Code), and (ii) Tunisia's preference for gradual and cautious implementation of reforms that could have adverse social impacts or weaken government control in key sectors of the economy.

v. **Implementation Experience and Results.** Overall, the program outcome is satisfactory. Key areas of major success include the maintenance of a good macroeconomic framework especially on the external front; the fast implementation of the free trade agreement included in the Association Agreement signed with the European Union; and the big push given to privatization in late 1997 to early 1998 which resulted in the successful privatization of two large cement companies.

vi. On the macroeconomic front, Tunisia confirmed its commitment to macroeconomic stability and consolidated its reputation of a soundly managed economy. Current account deficits were lower than program targets in 1996 and 1997. The 1996 outcome may not necessarily be conducive to the improvement of long-term competitiveness as it was brought about by a slowing of investment-related imports. The 1997 outcome is more promising as it originated in a fast growth of exports and a strong services account. Tunisia also maintained external reserves worth more than 3 months of imports, a historical high. The sound external position commanded confidence in Tunisia's economy. The country was able to raise significant amounts of capital on international financial markets at favorable rates in 1997, and to attract a relatively large amount of foreign direct investment in 1998. To improve economic competitiveness in a durable manner, the macroeconomic achievements on the external front will need to be accompanied with strong actions geared at improving fiscal balances, reducing inflation and improving employment.

vii. On the trade liberalization front, Tunisia started implementing the Association Agreement two and a half years before the ratification of the Agreement in all EU countries. This move signaled strong commitment on the part of Tunisia. The authorities managed to partially offset the short-term losses of fiscal revenues due to the lowering of tariffs, by introducing other revenue measures (e.g. broadening of the VAT coverage and upward adjustment of some VAT rates) as well as some expenditure restraint measures (e.g. reducing food subsidy and controlling capital expenditures). On the privatization front, Tunisia made a big leap forward in 1998 after a decade of slow and inconsequential privatization, raising its cumulative privatization receipts since 1987 from 400 million dinars to over 830 million within a year. This impressive result was achieved largely through the sale of two large cement companies.

viii. Despite the program's large success, a number of policy actions envisaged to lower enterprises' cost of doing business -- increasing the efficiency of maritime transport, introducing some flexibility in the organization of dock labor, and adopting a new Company code -- were still to be completed though at an advanced stage at the time the loan was closed. Two technical waivers and a partial waiver were granted to allow for the release of the second tranche of the loan. However, the financing arrangements and the cost of implementing the project did not change as a result of the delays.

ix. **Key factors that affected achievement of the major objectives.** In 1996, abundant rainfalls boosted agricultural output by 29 percent after two years of negative growth, and tremendously helped GDP growth which reached 7 percent that year. In 1997, Tunisia succeeded in raising funds on international capital markets at very favorable conditions, which allowed the country to exceed the target for foreign exchange reserves set in the ECAL program. On the other hand, the need for, and difficulties in, building broad support for deregulation of maritime activities and the revision of the Company Code slowed program implementation.

x. **Performance of the Bank.** The Bank showed flexibility during program preparation and reached an agreement with the authorities to postponing the banking sector reform component initially envisaged in the operation in order to arrive at a fully satisfactory policy package for the sector. This change entailed a reduction of the loan amount by half. During program implementation, while recognizing Tunisia's preference for gradual implementation of reforms, the Bank pressed for fast reforms where there was a strong case to do so. For example, through the program, a large-scale privatization was successfully undertaken for the first time in Tunisia. In addition, the Bank closely coordinated its loan preparation and supervision with the European Union, and worked closely with the IMF on the macroeconomic framework for the operation.

xi. **Performance of the Borrower.** Tunisian officials were actively involved in the design of the program and took full ownership thereof. During program implementation, the borrower experienced some delays in meeting some loan covenants because of the political sensitivity of the measures involved and the need to build broad support before implementing them. In other areas – such as macroeconomic management and privatization, the Tunisian authorities occasionally implemented measures that went beyond program targets. During program supervision, Tunisian officials responded to Bank's requests for information dissemination, although, at the initial stage of program implementation, information on the status of the privatization program was not made public.

xii. **Project sustainability.** Macroeconomic stability is likely to be sustained, given the track record and the generally good initial conditions; however, inflexibility of budgetary expenditures (essentially due to a heavy wage bill), worsening external financing conditions, and in general a deteriorating international scene, constitute factors of risk. Regarding trade reforms, much progress has been made, and there is momentum. It is unlikely that reversals will take place. However a much more severe deterioration in the world economy could cause demand for Tunisian exports to stagnate, worsen the trade balance, and perhaps slow down further tariff reductions. A much worse international situation would also have effects on the ability of the Tunisian economy to reduce unemployment. Lastly, improvements on the regulatory and labor market fronts are likely to proceed slowly, in part because of the need to generate broad support.

xiii. Working closely with the authorities, the Bank has just appraised a second Economic Competitiveness Adjustment Loan (ECAL II) that will consolidate progress made under the first ECAL. The second ECAL will primarily aim at strengthening the banking sector by improving banking regulation and settling bad loans owed by public and semi-public enterprises.

xiv. **Key lessons learned.** The first lesson learned through the program supported by this loan is that there are gains to be made in fast, yet orderly implementation of structural reforms as seen with privatization and trade reforms. The Tunisian authorities and the Bank should continue to seek ways to speed up structural reforms in other areas of the economy. The second lesson is that collaboration with other development partners such as the EU and the IMF can greatly leverage Bank's resources and enhance the impact of Bank's intervention.

IMPLEMENTATION COMPLETION REPORT

REPUBLIC OF TUNISIA

ECONOMIC COMPETITIVENESS ADJUSTMENT LOAN

(LOAN 4069 – TUN)

PART I – PROJECT IMPLEMENTATION ASSESSMENT

A. BACKGROUND

1. From independence in 1956 to the mid-1980s, Tunisia's development process was essentially government-led. Government undertook large public investment programs whose rationale was not always to provide services of a public good nature. Government also felt the need to supplement private investment deemed insufficient, and to ensure adequate levels of investment in areas of strategic national interest. In 1986, oil prices fell markedly and caused a fall in oil related revenues for the Government. This added to the effects of the large public outlays and rigid current public expenditures to cause a near balance of payments crisis.

2. Since then, Tunisian authorities have consistently pursued a program of economic adjustment and structural reforms aimed at instilling macroeconomic stability, introducing market determined incentives, and improving the outward orientation of the economy. Sound macroeconomic management has helped withstand the impact of adverse developments, such as drought, the Gulf war, and slow economic growth in Europe in the early 1990s. Annual real GDP growth increased from an average of 3 percent during the 1980-86 period to more than 4 percent during 1987-97, and growth rate of per capita income doubled to 2.4 percent per annum, which, combined with enlightened policies for human resources development, helped to significantly reduce the share of the population living in poverty. From 9 percent in 1980-86, the average annual rate of inflation declined to 6 percent in 1987-97 mainly as a result of a gradual reduction in the fiscal deficit (from an average of 5.5 percent to 4.2 percent), and a better control of monetary aggregates. The country's external position has improved tremendously, with end-of-year gross foreign reserves increasing from the equivalent of 1.3 months on imports on average during 1984-86 to 2.2 during 1987-1995 and to over 3 during 1996-98. Furthermore, the cautious implementation of economic measures has helped minimize social disruptions and conflicts.

3. Economic adjustment, and therefore securing stable macroeconomic environment for private investment, took place in a very dynamic global economic environment, particularly in countries -- in Asia and Eastern Europe -- competing with Tunisian products in international markets (especially in the European Union). In Tunisia, the process was slow and piecemeal. The authorities implemented a partial trade liberalization, the thrust of which was to give trade protection to import competing firms and tax advantages to enterprises producing exclusively for exports under subcontracting agreements in low skill activities such as garment assembly. The

former hindered an efficient utilization of capital resources and the latter may have introduced labor market biases towards unskilled labor. Many of Tunisia's competitors increased their comparative edge; achieving higher labor productivity (either through low wages or through higher technical skills, or both), and lower costs of transportation of goods and services.

4. Tunisia signed an Association Agreement with the EU in July 1995. The Agreement, which was the first to be signed between the European Union and a country of the Middle East and North Africa region, entailed trade liberalization by a gradual phasing out of tariffs. Since the signing of the Association Agreement, Tunisian authorities have placed a stronger emphasis on improving the efficiency and international competitiveness of the economy with a view to easing its integration with Europe and the global economy. As an indication of the authorities resolve to open up the economy, the implementation of the Association Agreement started in Tunisia two and a half years before its ratification by all EU countries; and the privatization of public enterprises received a big push in late 1997 and early 1998.

5. At the time when this loan was prepared, many aspects of the international competitiveness of the Tunisian economy still needed improvement. Though the real exchange rate had remained fairly stable, international competitiveness was hindered by high production and transportation costs, slow and inefficient port and customs procedures, inadequate telecommunications services, labor market rigidities, limited and costly access to credit, and inadequate legal and incentives regimes.

6. Whilst in the 1970s and early 1980s, the Bank's lending program to Tunisia was in support of investments in infrastructure, social development and agriculture, since the beginning of Tunisia's adjustment process in 1986, the Bank has also supported broad economic reforms through seven adjustment operations for a total of US$989 million. The latest adjustment operation is the Economic Competitiveness Adjustment Loan.

B. PROGRAM OBJECTIVES

7. The main objective of the Economic Competitiveness Adjustment Loan (ECAL) was to improve the international competitiveness of the Tunisian economy in the aftermath of the signing of the Association Agreement with the European Union, with a view to achieving a sustainable increase in the rate of economic growth. The program was expected to increase the efficiency of resource allocation in the economy and the productivity of the private sector; strengthen Tunisia's balance of payments and consolidate its access to private capital markets; and facilitate the integration of Tunisia with world markets.

8. The program supported five broad areas of policy reform: a) Maintain a stable macroeconomic framework and foster a stable business environment; including by introducing fiscal measures to replace revenue losses from the expected tariff reforms; b) Acceleration of the implementation of the FTA; including the elimination of tariff surcharges, thus easing domestic firms' access to capital inputs and intermediate goods; c) Acceleration of the pace of privatization in competitive sectors and the opening up of new sectors to private capital so as to increase the role of the private sector in the economy and reduce inefficiencies; d) Reduce transaction costs and improve the regulatory and administrative environment in which enterprises operate, through lower transport costs, trade facilitation and an improved legislative framework; and e) Reduce labor costs by increasing flexibility in the labor market, particularly in lay-off procedures, while protecting workers and containing labor costs.

9. The ambition of the program was not to tackle every single issue relating to competitiveness, but to focus on key areas suitable for immediate policy actions and leave other areas for future operations. The initial timeframe for the operation appeared to be rather tight in view of (i) the need for the Tunisian authorities to build broad support for some of the structural reforms (i.e. liberalization of maritime activities and the adoption of a new Company Code), and (ii) Tunisia's preference for gradual and cautious implementation of reforms that could have adverse social impacts or weaken government control in key sectors of the economy.

C. ACHIEVEMENT OF PROGRAM OBJECTIVES

10. Overall, the program outcome is satisfactory. Key areas of major success include the maintenance of a good macroeconomic framework especially on the external front; the fast implementation of the free trade agreement included in the Association Agreement signed with the European Union; and the big push given to privatization in late 1997 and early 1998 which resulted in the successful privatization of two large cement companies. Despite the program's large success, a number of policy actions envisaged to lower enterprises' cost of doing business -- increasing the efficiency of maritime transport, introducing some flexibility in dock labor, and adopting a new Company code -- were still to be completed though at an advanced stage at the time the loan was closed. Two technical waivers and a partial waiver were granted to allow for the release of the second tranche of the loan.

11. **Macroeconomic Management**. On the macroeconomic front, the major achievement of the program was Tunisia's improved external position and enhanced access to foreign capital both through international capital markets and foreign direct investment. The 1996 current account deficit was lower than program target owing to low investment related imports in 1996, which may not be promising for future competitiveness. Investment related imports picked up in 1997; exports also grew fast – albeit slightly less so than program target – and the services account showed a strong turnout. Hence a current account deficit in 1997 lower than program target. The external debt to GDP ratio improved considerably, declining from 58 percent in 1995 to 54 percent in 1997. Foreign reserves ended up at a higher level than targeted -- at historical high cushions of 3.2 and 3.3 months of imports in 1996 and 1997 respectively. The stronger reserves position is a reflection of Tunisia's improved ability to raise funds on international capital markets at favorable conditions. In 1997, the authorities were able to tap the US dollar euromarket for the first time, raising US dollars 400 million at very favorable rates of 140 basis points above US Treasury for 10-year notes, and 180 basis points above US Treasury for 30-year bonds. They also raised Yen 12.5 billion in 20-year Samurai bonds with a coupon of 4.35%.

Table I : Program macroeconomic targets and results

	1996 Program targets	1996 Actual	1997 Program targets	1997 Actual
Exports (Good and non factor services)	4.7	0.5	7.3	6.9
Manufac. Exports % Share of GDP	4.4	-11.8	8.2	7.5
Fiscal Balance	-3.8	-4.0	-3.0	-3.4
Current Account	-3.8	-2.7	- 3.8	-3.4
Reserves (months of imports)	3.0	3.2	3.1	3.3
Debt outstanding	53.1	55.6	52	54

12. Though good, the macroeconomic achievements on the domestic front were less impressive. At 3.4 percent of GDP, the 1997 fiscal deficit of the central government was an improvement over the 1996 level of 4.0 percent. But in both years the fiscal deficit missed the program targets. The 1996 fiscal slippage was due to a steeper drop than expected in trade-related fiscal revenues during the first year of the implementation of the FTA. Behind the 1997 fiscal slippage were rigidities in current expenditures (particularly the wage bill), lower than expected oil revenues, and a slower than expected impact of the new revenue measures designed to compensate for declining trade related revenues in the second year of the implementation of the free trade agreement. The authorities confirmed their commitment to macroeconomic stability and made great strands at limiting fiscal slippage by implementing expenditure restraint measures not foreseen in the program. The inflation rate was 3.7 percent in 1996 as in 1997, lower than the projected level of 4.5 percent in 1996 but higher than the projected level of 3.3 percent in 1997. There is room for further reduction in inflation as it remains higher than in major European trade partners -- EU inflation averaged 2.1 percent per year in 1996-98.

13. **Tax measures**. The implementation of the FTA with the EU has a short-term adverse impact on government revenues due to the forgone trade related fiscal revenues. The issue of ensuring tariff reduction with fiscal revenue neutrality was then a major concern of the program, and new compensatory revenue measures were introduced under the program in order to avoid that implementation of the FTA cause a deviation from government's fiscal stance in the short-term. The compensatory measures included an increase of the value added tax rate from 6 percent to 10 percent for certain petroleum products and to the standard rate of 17 percent for others – such as unleaded gas and heavy fuels; an increase of the minimum rate of taxation for income profits from 10 percent to 15 percent; and the inclusion of imported capital goods in the 10 percent VAT rate category. VAT related revenues increased by 160 million dinars between 1996 and 1997, that is an increase of 16 percent, compared to an increase of 12 percent a year earlier.

14. The increase in VAT revenues was however insufficient to compensate for the decline in trade related fiscal revenues caused by the implementation of the free trade agreement. To limit the fiscal slippage, the authorities implemented expenditure restraints measures consisting in increasing the administered prices for subsidized food products (mainly flour, semolina, oil, and milk), and thus limiting government transfers to the *Caisse Générale de Compensation* or the fiscal cost of food subsidies to 1.7 percent of GDP as foreseen in the program. As part of their efforts to limit fiscal slippage in 1997, the authorities took additional expenditure restraints measures by freezing certain expenditures in 1997 (especially in the capital expenditure category) for a total of about US$120 million.

15. The 1997 revenue measures were consolidated in 1998 – with an increase of the (standard) VAT rate from 17 percent to 18 percent for most products (and decrease of the rate from 29 percent to 18 percent for some products); an increase of VAT rate on petroleum products from 10 percent to 18 percent; and an increase of VAT rate on electricity for domestic users from 6 percent to 10 percent. The 1997 and 1998 measures are now yielding substantial revenue increases, with an increase of nearly 32 percent in VAT related revenues in the first 10 months of 1998 over the same period in 1997. The authorities consider these reforms as structural and have no plan to modify the VAT structure in the near future.

16. The program also introduced some transparency in the allocation of subsidies to the public agencies in charge of commercializing cereals and oil. Government policy to fix the prices of cereals and oil to consumers contributed to operating deficits of the *Office des Céréales* and *Office Nationale de l'Huile*; and budgetary transfers proved inadequate to cover those deficits. The above agencies financed their deficits through borrowing from the banking system. Under the program, government decided to repay the arrears that those agencies had built up vis-à-vis banks, namely the *Banque Nationale Agricole*. To settle the arrears, the government received an advance of 960 million dinars from the Central Bank to be repaid through the budget over 12 years without interest. Moreover, the Government decided to make adequate budgetary transfers to the *Caisse Générale de Compensation* in order to ensure that no further arrears develop vis-à-vis the banking system.

17. **Trade Policy.** The Association Agreement signed with the European Union in July 1995 includes a phased creation of a free trade area. Under the Agreement, tariffs on import of goods (excluding agricultural goods) will be progressively eliminated over a 12-year period (1996-2007), starting with those on capital and intermediate goods. The program supported by this loan helped accelerate the implementation of the FTA by incorporating the phased tariff reduction in the 1997 budget and by helping to expedite the ratification of the FTA by the Chamber of Deputies. The implementation of the free trade agreement in Tunisia began roughly two and a half years prior to its ratification in all EU countries. The early start at implementing the FTA signaled strong commitment on the part of Tunisia. Other major achievements of the program are the removal of all trade surcharges, and the harmonization of tariffs on capital good imports from outside the EU.

18. Despite possible short-term costs that may arise from increased competition faced by domestic firms, the program has helped confirm that the FTA represents a unique opportunity for sustained growth. With the implementation of the FTA, Tunisian firms will have easier and less costly access to intermediate goods on international markets, which should contribute to improving their competitiveness. They will also have access to a larger market for their products. Imports of machinery and semi-finished products have accelerated in 1997 and 1998 with a potential positive effect on the productivity of firms; and manufacturing exports have already shown signs of accelerated growth in 1997 and 1998. In order to further reduce tariffs, the Government aims at streamlining the rates and reducing the average tariff rate from 43 percent in 1997 to 25 percent in 2001. The Government also concluded negotiations with the World Trade Organization on the complete elimination of quantitative import restrictions (mainly on cars) by 2001, and has negotiated tariff harmonization arrangements with a number of countries outside the EU.

19. **Reducing the Role of the State in Competitive and Commercial Sectors.** Until late 1997-early 1998, the Tunisian privatization program, launched in 1987, had proceeded rather slowly. With the program supported by this loan, the privatization program made an important leap forward. In 1998 alone, privatization yielded revenue of 435 million dinars for government's budget, more than the combined privatization proceeds of the previous 10 years. The 1998 balance of payments also greatly benefited from Government's renewed privatization effort in the form of increased foreign direct investment, a boon at a time when borrowing from international capital markets was made difficult for emerging market economies due to the financial crisis in Asia and Russia.

20. The success of the privatization program in 1998 was however slow in coming. During the preparation of the ECAL, Tunisian authorities compiled a list of 63 public enterprises to be privatized. The Bank and the authorities agreed upon that list. Tunisian officials subsequently informed the Bank that some small companies had been removed from the list for reasons having to do with political sensitivity or strategic interest. This, and delays in receiving technical assistance to strengthen the Privatization Unit in the Ministry of Economic Development, delayed the implementation of this component of the program.

21. The government willingly substituted the public enterprises removed from the original list with other public enterprises in order to meet program target of bringing to the point of sale at least 51% of the capital of a number of enterprises corresponding to 50% of net assets of the agreed list of 63 public enterprises. This allowed for the privatization of the *Société des Ciments d'Enfidah* and the *Cimenteries Jebel Ouest*, which generated over 400 million dinars in foreign investment.

22. With the successful privatization of these two large cement companies, Tunisian authorities achieved more than the privatization targets foreseen in the program. They brought to the point of sale more than 51 percent of the capital of enterprises, corresponding to 54 percent of the net assets of the selected enterprises. The Government hired a renowned international investment firm as advisor for the privatization of the cement companies, and the sale was made under international competitive bidding procedures. All participants have praised the Government for the transparency of the process. Moreover, under the program, the Government began publishing sale outcomes and articles on the results and impact of the privatization program in local economic journals and newspapers. The recent success of privatization is perceived as a key asset in moving forward the privatization agenda in coming years.

23. **Deregulation of Maritime Activities and Trade Facilitation**. This is an area where progress has been slow under the program. To improve competitiveness, this component of the program was aimed at reducing the cost, and increasing the speed, of shipping. Areas of progress were accompanied by areas were program objectives remain to be achieved. Going beyond the mere submission of a draft legislation as planned in the program, the Government has approved a law abolishing the privileges granted to Tunisian ship-owners in chartering, a big step towards the liberalization of maritime activities. A draft law on commercial port activities is currently being reviewed by the Chamber of Deputies and its adoption is expected in the near future. However, little progress was made in incorporating the redefinition of the functions of OPNT and the new regime of maritime domain. The authorities need to shift to a more rapid reform stance in maritime transports if the competitiveness of Tunisian exporters is to be markedly improved.

24. Progress was slow and partial in introducing flexibility and competition in working conditions of dock labor. Negotiations between the government and workers' union were protracted and decision making was politically sensitive. A draft law was presented to the Chamber of Deputies but had not been approved, let alone published in the Official Gazette, at the time of the release of the second tranche of the loan, and a technical waiver was granted.

25. Progress was made in restructuring the *Compagnie Tunisienne de Navigation (CTN)*, the state maritime company. However there is no indication of progress towards its privatization. The restructuring of the *Société Tunisienne d'Acconage et de Manutention (STAM)* lagged. A consulting firm prepared a restructuring plan, but the Government found the work unsatisfactory,

and another plan will be prepared. At the time of the release of the second tranche of the loan, a partial waiver was issued because of delays in adopting the restructuring plan of STAM.

26. Under the program, a trade facilitation committee composed of all concerned groups in Tunisia, produced the single trade document (*liasse unique*) envisaged in the Association Agreement with the EU. The *liasse unique* was published as decree in the Official Gazette in December 1997. The decree simplifies the documentation and ports procedures and brings the customs code up to date and in conformity with the EU code. This is expected to reduce the time required for custom claims processing and clearance.

27. **Telecommunications.** In Tunisia, entry of private capital in the telecommunications sector is tightly controlled although global experience suggests that, thanks to recent technical progress, the telecommunications sector can no longer be viewed as a natural monopoly sector. Many countries have indeed privatized their national monopolies and allowed the emergence of new private service providers. Tunisian authorities presented to the Bank an agenda for the liberalization of the telecommunications sector in Tunisia. The proposed plan was slow and fell short of Bank's expectations; it proposed selling just 10 percent of *Tunisie Telecom* – the public monopoly – only by 2002, and liberalizing mobile telephone and paging services only in 2000. The slow development of telecommunications may put a break on the development of the Internet in Tunisia, and deny firms expanded and affordable access to information, a key input and a key element of their efficiency and international competitiveness. The authorities have invoked the strategic character of telecommunications to justify the overly cautious approach to its liberalization.

28. **Business Environment and Labor Cost**. To improve competitiveness of enterprises, one of the objectives of the program supported by this loan was to adapt the legal framework, increase flexibility of the labor market, and decrease the cost of labor while improving workers' protection. A new company code was drafted under the program. The new draft represents important progress; among other innovations, it enables mergers and acquisitions -- previously not possible. The drafting of the new company code took longer than anticipated at program formulation stage, and its submission to the Chamber of Deputies – a key condition for the release of the second tranche of the loan – was delayed because the Government used a broad consultative process to prepare the draft. The draft was submitted to all Ministries concerned as well as to the private enterprises organization for comments. At the time of the release of the second tranche of the loan, a technical waiver was granted on this component of the program in order to allow the Government enough time to complete the consultative process and possibly facilitate the approval of the new Company Code by the Chamber of Deputies upon its submission by the Government.

29. Reforms were introduced to increase the flexibility of the labor market and reduce labor costs. Procedures for lay-offs for economic reasons were eased; a draft law was submitted to the Chamber of Deputies creating a limited severance scheme to cover the separation packages paid to workers laid-off for economic reasons; and measures were taken to reduce the burden of social security contributions for employers in the non-agricultural private sector.

D. MAJOR FACTORS AFFECTING THE LOAN

30. **Factors not generally subject to Government's control**. In 1996, abundant rainfalls boosted agricultural output by 29 percent after two years of negative growth in the sector. This tremendously helped GDP growth that year. In 1997, Tunisia succeeded in raising funds on international capital markets at very favorable conditions, which allowed the country to exceed the target for foreign exchange reserves set in the program. The situation has changed somewhat in 1998. Because of the Asian financial crisis, foreign investors who do not have enough information to differentiate between emerging market economies, are asking for very high spreads or withdrawing funding. Under the circumstances, despite Tunisia's good records of macroeconomic management, the financing of its external capital needs may prove expensive in 1998 and 1999. For 1998, the situation is eased by good inflows of foreign direct investment owing to the success of the privatization program.

31. **Factors generally subject to Government's control**. Program implementation was slowed by the need for, and difficulties in, building broad support for deregulation of maritime and port activities, and for reforming the business environment. The disbursement of the second tranche was delayed by six months. At the time of the release of the second tranche of the loan, the deregulation of dock labor, the adoption of a new company code, and the restructuring plan of STAM were lagging. Two technical waivers and one partial waiver were granted to take account of substantial progress made in other program areas.

E. PROGRAM SUSTAINABILITY

32. Progress made under the program appears sustainable to a large extent. The authorities are committed to moving forward on key program components such as the deepening of trade liberalization and privatization – with two other large cement companies expected to be privatized in 1999. They are also prepared to make headway in areas where reforms were deemed premature under the program supported by this loan. The authorities are thus deepening reforms in the financial sector, improving banks portfolio, introducing new instruments for government borrowing, facilitating the emergence of a secondary market, and deepening the interbank foreign exchange market. These reforms will contribute to the efficiency of the financial system and help sustain progress made in the real sector under this loan. The authorities are also looking to reforming the civil service. Such reform will contribute to (i) reducing the weight of the public sector wage bill on public resources therefore making the fiscal stance sustainable, and (ii) strengthening the administration's capacity to support the private sector in upgrading international competitiveness.

33. A number of factors may however change the perceived sustainability of important program components. *Macroeconomic stability* is likely to be sustained, given the track record and the generally good initial conditions; however fiscal inflexibility mainly due to the wage bill, contingent liabilities due to enterprises or banks that may not sustain competition from European firms, worsening external financing conditions, and in general a deteriorating international scene constitute factors of risk. In Tunisia, many university graduates prefer to wait two to three years for a Government job rather seek employment or self-employment in the private sector because of low wage at entry levels and job insecurity in the latter sector. Because job creation in the formal private sector is inadequate, the public sector continues to absorb a large number of new graduates. For social reasons, a continuation of weak job creation by the private sector may

make it difficult for the government to reduce intake of new graduates in the civil service, reduce the share of the wage bill in the budget, and maintain its fiscal stance.

34. Much progress has been made in *trade reform*. There is momentum, and it is unlikely that reversals will take place. Tunisian trade is still highly concentrated with Europe. If the resilience shown by European countries so far to the crises affecting Asia, Russia, and Japan fades out, demand for Tunisian exports may stagnate, affecting the sustainability of external balance. This could inspire non-market responses to restore external balances, with risks of slowing the implementation of trade liberalization.

35. Owing to Tunisia's tradition of public enterprises and public provision, the *privatization* drive is still not comprehensive. Notwithstanding the success of the 1998 privatization, there is some uncertainty as to how the country will manage to expedite the sale of some other public enterprises previously identified for privatization. If privatization lags behind trade reforms, and efficiency in the production of goods and services continues to be constrained by non-competitive public enterprises in the manufacturing and services sectors, domestic producers may not be able to compete with imports. This may usher in some company closures, slow down the development of the manufacturing and formal services sectors of the economy, and could inspire some pressure for protective measures.

F. BANK PERFORMANCE

36. The Bank maintained an active dialogue and cooperation with the Tunisian authorities during program design and implementation. The Bank showed flexibility during program preparation and reached an agreement with the authorities to postponing the banking sector reform component initially envisaged in the operation in order to arrive at a fully satisfactory policy package for the sector. This change entailed a reduction of the loan amount by half. The authorities are now addressing the banking sector reform in a second ECAL where the Bank has put more effort at helping to design policies to strengthen banks' portfolio and banking regulation.

37. Some program components were rather ambitious and the initial timeframe for program implementation rather tight. However, during supervision, the Bank took into account Tunisia's preference for gradual and cautious implementation of reforms, while encouraging fast and vigorous reforms where appropriate. This accommodating yet determined approach paid off. For example, through the program, a large-scale privatization was successfully undertaken for the first time in Tunisia. The Bank also persuaded the authorities that the dissemination of information on the privatization process to the public was critical to improving the image of privatization and to maintaining its public acceptance. The Bank closely coordinated its loan preparation and supervision with the European Union, which provided parallel financing to the reform program, and worked closely with the IMF on the design and monitoring of the macroeconomic framework of the operation.

G. BORROWER PERFORMANCE

38. Tunisian officials were actively involved in the design of the program and took full ownership thereof. During program implementation, the borrower experienced some delays in meeting some loan covenants because of the political sensitivity of the measures involved, the need to build broad support before implementing them, and the time required for the Chamber of

Deputies to discuss and pass draft law presented them by the Government. In some program areas – such as macroeconomic management and privatization, the Tunisian authorities successfully implemented measures that went beyond program targets. During program supervision, Tunisian officials responded to Bank's requests for information dissemination, although, at the initial stage of program implementation, information on the status of the privatization program was not made public.

H. ASSESSMENT OF OUTCOME

39. Through policy actions taken under the program, significant progress was made towards achieving the development objective of improving the international competitiveness of the Tunisian economy. The program helped maintain a stable macroeconomic environment in Tunisia. Real GDP growth was strong -- though aided in 1996 by a strong recovery of the agricultural sector thanks to abundant rains. Tunisia's external position was soundly managed in 1996-1998, and the level of foreign exchange reserves was adequate to cover three months of imports of goods. During its 1998 article IV consultations, the IMF expressed confidence in the Tunisian macroeconomic framework. To markedly improve international competitiveness, inflation will need to be reduced further in 1999 and beyond.

40. With strong trade liberalization and a successful privatization program, Tunisia has advanced its reform agenda and confirmed its readiness to undertake the changes necessary to ensure macroeconomic stability and compete in the global economy in the 21st century. The implementation of the FTA with the European Union was speeded up and is on track. The privatization of two of the largest cement companies was decisive and successful. The momentum should be maintained and privatization moved forwards throughout other sectors of the economy. Program achievements were less than comprehensive in terms of improving the regulatory and administrative environment in which enterprises operate.

I. FUTURE OPERATIONS

41. Working closely with the authorities, the Bank has already appraised a second Economic Competitiveness Adjustment Loan (ECAL II) that will consolidate progress made under the first ECAL. The second ECAL will attempt to reform the banking sector by, among other things, strengthening banking regulation and cleaning banks' portfolio of bad loans owed by public and semi-public enterprises. The new operation incorporates the recommendations made by a government-sponsored Banking Commission created in January 1997. The Bank is also undertaking a private sector assessment which will help gain a broader understanding of the private sector in Tunisia, its needs, the remaining impediments it faces in improving its competitiveness, and whether and when domestic firms are likely to provide the supply response to the implementation of free trade agreement with the EU. A trade promotion and facilitation project is under preparation, which, in addition to improving international marketing and export guarantee, will help put in place a trade facilitation system (including an electronic data interchange system) that would improve the efficiency of Tunisian ports and thus help improve international competitiveness. Also, a transport sector loan under preparation will help consolidate reforms in maritime transport initiated under the ECAL.

J. KEY LESSONS LEARNED

42. The first lesson learned through the program supported by this loan is that there are gains to be made in fast, yet orderly implementation of structural reforms. In the two program components that had the greatest success -- trade liberalization and privatization -- the speed of reform has been faster than in other reform areas. Faster implementation did not however mean that Tunisian authorities analyzed and implemented reforms with less caution than is traditionally the case. The Tunisian authorities and the Bank should continue to seek ways to speed up structural reforms in other areas of the economy.

43. During program preparation and throughout implementation, the Bank, the IMF and the EU agreed on a common macroeconomic framework and worked together on policy measures. The second lesson learned through the operation is that this type of coordination greatly enhances the relationships between the institutions at the operational level, and can be highly appreciated by Tunisian authorities -- in fact, the authorities indicated that any follow-up to ECAL should also be coordinated with the EU. The lesson is heeded in the ECAL II under preparation; the Bank, the EU and the African Development Bank are working jointly on the Government's reform program to be supported with loans or grants from these institutions.

PART II: STATISTICAL ANNEXES

Table 1: Summary of Assessments

A. Achievement of Objectives	Substantial	Partial	Negligible	Not Applicable
Macro Policies	X			
Sector Policies		X		
Financial Objectives		X		
Institutional Development		X		
Physical Objectives				X
Poverty Reduction				X
Gender Issues				X
Other Social Objectives		X		
Environmental Objectives				X
Public Sector Management		X		
Private Sector Development	X			
Other (Trade Liberalization)	X			
B. Project Sustainability	**Likely**	**Unlikely**	**Uncertain**	
	X			
C. Bank Performance	**Highly Satisfactory**	**Satisfactory**	**Deficient**	
Identification		X		
Preparation Assistance		X		
Appraisal	X			
Supervision	X			
D. Borrower Performance	**Highly Satisfactory**	**Satisfactory**	**Deficient**	
Preparation	X			
Implementation		X		
Covenant Compliance		X		
E. Assessment of Outcome	**Highly Satisfactory**	**Satisfactory**	**Unsatisfactory**	**Highly Unsatisfactory**
		X		

Table 2: Related Bank Loans/Credits

Loan/Credit Title	Purpose	Date of Approval	Status
Loan 2754 ASAL Agricultural Sector Adjustment Loan US$150 M	To support Government's agricultural sector reform program, focussing on increasing producer prices, reducing subsidies on inputs, strengthening extension and research and increasing interest rates.	September 1986	Closed June 30, 1989
Loan 2781 ITPAL Industrial Trade and Policy Adjustment Loan US$150 M	To support the initial phase of Government's adjustment program for the industrial sector, including price and trade liberalization and fiscal reform.	February 1987	Closed in December 1989, one year behind schedule. The fulfillment of certain conditions (concerning labor issues, the introduction of a VAT tax and the design a foreign exchange risk system) took longer than expected.
Loan 2962 SALI Structural Adjustment Loan US$150 M	To support the medium-term macroeconomic adjustment program of the Government and continue the trade liberalization and foreign exchange risk coverage reforms initiated under the ITPAL; reform of taxation through introduction of VAT and simplification of income	June 1988	Closed in June 1991, 26 months behind schedule. The delay was due to slow implementation of liberalization measures, because of a severe drought, rising unemployment and declining investment.
Loan 3109 PERL Public Enterprises Reform Loan US$130 M	To support the government's public enterprise reform, including legal and institutional reforms; to reinforce the Government's program of divestiture and restructuring.	July 1989	Closed in June 1993, 2 years later than planned because of slow progress in privatization (for fears of social unrest), and delays in the preparation of performance contracts.
Loan 3078 ASAL II Agricultural Sector Adjustment Loan US$84 M	To support the reforms of the marketing, institutional and price framework in agriculture, reorienting public investment in agriculture and improving the management of natural resources.	June 1989	Closed in June 1995, 6 months later than planned.
Loan 3424 EFRSL Economic and Financial Reform Support Loan US$250 M	To support efforts to achieve higher growth and employment creation, restoring internal and external balances, after the Gulf war, strengthening private sector development and existing access to commercial borrowing.	December 1991	Closed in December 1994 as scheduled

Table 3: Project Timetable

Steps in Project Cycle	Date Planned	Date Actual/Latest Estimate
Pre-Appraisal	11/27/95	11/27/95
Appraisal	2/27/96	2/27/96
Negotiations	5/2/96	5/2/96
Letter of development policy	6/12/96	6/12/96
Board Presentation	7/25/96	7/25/96
Signing	8/2/96	8/2/96
Effectiveness	12/6/96	2/2/97
First Tranche	8/31/96	12/31/96
Second Tranche	6/30/97	6/3/98
Loan Closing	12/31/97	6/30/98

Table 4: Loan Disbursements: Cumulative Estimates and Actual

	FY 1997	FY 1998
Appraisal Estimate (US$ millions)	75	75
Actual (US$ millions)	37.5	75
Actual as % of Estimate	50	100
Date of Final Disbursement	12/31/1996	6/3/1998

Note: IBRD fiscal year ends on June 30

Table 5: Indicators of Project Implementation

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Macroeconomics				
Acceleration in economic growth to a 5-6% a year while improving macroeconomic balances and economic competitiveness	During the last 5 years, GDP increased at an annual rate of 4.3%, but only 3.4% in 1994, because of a decline in agricultural production. In 1994, both the inflation rate (4.7%) and the budget deficit (2.7% of GDP) remained under control. 1995. GDP growth was only 2.5% in 1995, due to continued poor results in the agricultural sector; inflation reached 6.3% because of price increases in food products. The Fiscal deficit (4.2% of GDP) was higher than planned. After a significant improvement in 1994, the current account deficit deteriorated to 4.0% of GDP. The external debt to GDP ratio was 54.7%, down from an average of 62.8% during 1987-94.	Adopt a satisfactory medium-term macroeconomic framework, including targets to be monitored: - reserves, external debt, export growth and fiscal deficit.	Satisfactory implementation of macroeconomic program.	Tunisia maintained strong GDP growth of 6.9%, 5.4% and 5.1% in real terms in 1996, 1997 and 1998 respectively Inflation remained around 3.7% in 1996 and 1997, and will be slightly lower in 1998. Export earnings expanded by 6.9% in 1997 and the growth rate for manufacturing exports was strong at 7.5%.. The current account deficit was lower than the ECAL target by 0.4%.. Foreign direct investment in 1996 and 1997 were close to US$300 million or 1.5% of GDP, most of which took place in the energy sector. In 1998, foreign direct investment soared to US$800 million thanks to the privatization of two cement companies that jointly generated US$410 million in foreign direct investment. Reserves were higher than the ECAL target, reaching 3.3 months of imports in 1997 thanks to increased grants from the EU and better than expected access to foreign capital. Tunisia issued Yen 12.5 billion in 20-year Samurai bonds with a coupon of 4.35%, as well as notes and bonds on the Yankee market amounting to US$400 million under exceptionally good terms. Although the debt to GDP ratio was slightly higher than the program target, it has improved considerably, declining from 58% of GDP in 1995 to 54% in 1997.

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Fiscal				
Ensure sustainability of medium-term fiscal framework.	VAT was introduced in 1988; a new Personal and Corporate Income Tax Code was promulgated in 1990; a unified Investment code was approved in Dec. 1993 (Law n° 93-120).	Introduction of fiscal measures to compensate the loss in revenues resulting from tariff and surcharge reductions; extension of VAT to the retail sector, suppression of VAT exemptions for imported equipment goods; revision of list of activities subject to VAT rate of 6% (action taken in the 1996 Finance law).	Introduction in the 1997 Finance Law of fiscal measures to compensate losses in revenues due to the implementation of FTA;	The authorities increased the value added tax rate from 6 percent to 10 percent for certain petroleum products and to 17 percent for others (notably, unleaded gas and heavy fuels), the minimum rate of taxation for income profits from 10 percent to 15 percent, and included imported capital goods in the 10 percent VAT rate category. The 1997 revenue measures were consolidated in 1998 – with an increase of the VAT rate from 17 percent to 18 percent for most products (and decrease of the rate from 29 percent to 18 percent for some products); an increase of VAT rate on petroleum products from 10 percent to 18 percent; and an increase of VAT rate on electricity for domestic users from 6 percent to 10 percent.
		Agreement on a sustainable fiscal program including (a) fiscal measures to compensate losses in revenues due to the implementation of FTA; (b) the reimbursement by the State of the accumulated debts of the Office des Céréales (OC) and the Office National de l'Huile (ONH) vis-à-vis the banking system; (c) a mechanism through which the State will reimburse at the at the end of each year the accumulated debts of these offices vis-à-vis the banking system.	Repay the accumulated debts of the OC and the ONH vis-à-vis the banking system during 1996; limitation of the budgetary allocations to the Caisse Générale de Compensation to 1.7% of GDP. Reduction of budgetary expenditures (net of debt service) in relation to GDP, without prejudice to social expenditures, on the basis of a public expenditure review, before the end of October 1996, which will include the revision of the wage bill. Submission to the Bank of a study and action plan to harmonize incentives in the Investment code on the basis of the new commitments made under the WTO and FTA.	Government decided to repay the arrears that the *Office des Céréales* and *Office Nationale de l'Huile* had built up vis-à-vis the *Banque Nationale Agricole*. The government received an advance of 960 million dinars from the Central Bank to settle the arrears. The amount will be repaid through the budget over 12 years without interest. The authorities also increased the administered prices for subsidized food products (mainly flour, semolina, and milk), and limited the fiscal cost of food subsidies to 1.7 percent of GDP. Action plan submitted to the EU and the Bank

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Trade				
Promote greater integration in the world economy.	Signing of Free Trade Agreement (FTA) with the European Union (EU), in July 1995.	Submission to the Chamber of Deputies of a draft law concerning the FTA with the EU.	Publication in the official Gazette of the law ratifying the FTA with the EU.	Law no. 96-49 of June 1996 ratified the free trade agreement with the EU.
	Elimination of quantitative restrictions (QRs) on imports corresponding to 85% of domestic production. (All remaining QRs will be eliminated with the implementation of the FTA).	(a) Implementation of the tariff reductions included in list No. 1 of the FTA and their extension to the rest of the world (action taken in the 1996 finance law); (b) publication in the official Gazette of a decree reducing by 10 percentage points all tariff surcharges on imports; (c) agreement on a schedule to eliminate the remaining tariff surcharges in equal installments in the Finance laws of 1997 and 1998.	Inclusion in the 1997 finance law of the tariff reductions scheduled up to the second year of application of the FTA and of the scheduled elimination in surcharges. Implementation and publication of the tariff reduction program.	Article 21 of the 1997 Finance Law (no 96-113 of December 30, 1996) introduced the progressive removal of tariffs for the period 1996-2007 and considers January 1, 1997 as the beginning of the second year of application of the FTA. Article 20 of the same law removed all tariff surcharges.
			Agreement on a plan to harmonize the structure of tariffs imposed on non-European imports.	The GOT also concluded negotiations with the World Trade Organization on the complete elimination of quantitative import restrictions (mainly on cars) by 2001. Government also initiated several bilateral agreements to extend the changes in trade policy under the FTA to its other non-EU trading partners.

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Disengagement of the States				
Increase the role of the private sector in the economy; improve efficiency and competitiveness; strengthen fiscal balance; deepen capital markets.	Set up legal and institutional framework for privatization including; Law 89-9 (definition of public enterprises, rationalization of institutional responsibility of selling stocks in blocks through bids with specifications). Privatization of 43 enterprises (between 1987 and 1994) worth TD 156 million (about 1% of the book value of public enterprises producing goods and services).	Government brings to the point of sale (i.e. evaluation completion, bidding documents and their publication) at least 51% of the capital of a number of public enterprises corresponding to 50% of net assets of the agreed list of public enterprises producing goods and services (amounting to TD 1.413 billion). Public offering of more than 10% in the capital of at least one public enterprise (not included in the above-mentioned list of public enterprises). Prepare indicators on the size of public enterprises and their weight in the economy, distinguishing; (i) public enterprises in the competitive sector, (ii) strategic public enterprises, and (iii) public institutions. The indicators should also included, for each public enterprise; total and banking debt, budgetary transfers, profits or losses.	Government brings to the point of sale at least 51% of the capital of a number of enterprises corresponding to 50% of net assets of the agreed a list of public enterprises producing goods and services (amounting to TD 1.413 billion) Public offering of a minimum of 10% in the capital of at least 5 public enterprises (*Offre publique de vente, OPV)* where the State has a majority holding (not included in the above-mentioned list where the total net assets correspond to TD 1.413 million) Presentation of the program to privatize the remaining 50% of the agreed list of public enterprises and other actions to reduce the role of the State in the medium-term.	Towards the end of 1997 GOT hired a renowned international investment firm to prepare two large publicly-owned cement companies for sale under international competitive bidding procedures. To reach the goal of bringing to the point of sale 5 1 % of the capital of enterprises corresponding to at least 50% of the net assets from the list, the GOT placed *Jebel Ouest and Enfidah,* the two biggest cement companies on the list, up for sale in December 1997 and February 1998. As a result, the GOT was able to fulfill this condition by early February 1998, bringing to the point of sale much more than 51% of the capital of enterprises corresponding to 54% of the net assets of the selected enterprises. In addition, the Bank worked closely with the authorities to make the privatization process more transparent. As a result of discussions during supervision missions, the GOT has begun publishing sale outcomes and has begun systematically preparing published articles on the results and impact of the privatization program in local economic journals and newspapers. 20% of Tunisair shares were offered to the public before loan approval. After loan approval, at least 10% of shares of two public enterprises were offered to the public through *Offre publique de vente, OPV).* Government earmarked three other companies for *OPV* as soon as conditions on the stock market were conducive.

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Deregulation				
Maritime Transport and Ports Increase competitiveness of maritime transport	The maritime transport monopoly of CTN has been eliminated and private ship-owners have been authorized.		Submission to the Chamber of Deputies of the legislation modifying Articles 6 and 7 of the Law 77-13 with the purpose of eliminating the chartering privileges given to Tunisian ship-owners.	The Government approved law no. 97-69, published on October 31, 1997 in the Official Gazette, abrogating articles 6 and 7 of law 77-13 of March 1997, thereby abolishing the privileges granted to Tunisian ship-owners in chartering.
Improve competitiveness ports.	Adoption of Law 95-33 concerning deregulation of cargo handling in ports. As an exception, Article 10 allows the continuation of the monopoly situation by STAM in the ports of Tunis, La Goulette & Rades.		Submission to the Chamber of Deputies of the modifications to Article 10 of Law 95-33 dated April 14, 1995 in order to eliminate the monopoly of the STAM in the ports of Tunis, La Goulette and Rades and put it in competition with other stevedores.	A draft law was presented to the Chamber of Deputies. While the loan covenant requires only a modification of the 1949 decree "rendering the working conditions of the dockers less complex, more flexible . . .", the authorities proposed in the draft law the abrogation in its entirety of the 1949 decree and thus removing the monopoly of dock workers in the Tunis ports. The law has neither been passed nor published in the Official Gazette
			Labor regulations on port operations: publication in the Official Gazette of law modifying Decree of February 17, 1949, concerning working conditions of dock labor to render them less complex and more flexible and adapted to the requirements of modern ports.	
	Completion of a study to evaluate the CTN group.	Start up of the valuation process of STAM		The restructuring plan for CTN is under implementation and progressing satisfactorily. Four cargo boats have already been sold to private companies ' 300 employees have been laid off, and some of CTN's lines have been closed to better focus its activities.
		Starting of a study to prepare a strategy for restructuring the CTN.	Implementation of the plan to restructure STAM. Implementation of the plan to restructure CTN.	Restructuring plan for STAM was delayed due to the lengthy discussions with the dock workers unions. Restructuring study started only in December 1997. Initial draft submitted end-April 1998 was considered incomplete by the Tunisian authorities and a revised report is to be submitted.

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Maritime Transport and Ports (cont'd)	Completion of a study concerning the fluidity of maritime transport.	Possibility to grant concessions (applicable to ports, roads, handling operations etc.) for up to 30 years (action taken with Law 95-73 dated July 95	Publication of the regulation concerning port concessions specifying the pricing and the management system applied to the stevedores in each port of the country.	Regulation, pricing, and new tariffs published in a ministerial bylaw
	A ministerial bylaws (arrêté) published on September 15, 1995 (in application of the laws 95-32 & 95-33 of April 14, 1995), indicated the specifics with which all participants in maritime transport should comply.	Begin study on the reform of port regulation reserving for OPNT the role of public authority and specifying its attributes as manager of public land, guardian of security rules and protector of the port environment.	Ministry of Transport publishes a ministerial bylaws with the new maximum tariff list for cargo handling. Presentation to the Chamber of Deputies of draft legislation on new port regulations and incorporating the redefinition of functions for OPNT and the new regime of maritime domain.	A law introducing new port regulations and redefining the new regime of maritime domain was submitted to the Chamber of Deputies along with the bill concerning OPNT.
			Submission to the Chamber of Deputies of a draft law on multimodal transport.	Law approved by the Chamber of Deputies in 1998
Trade Facilitation Ensure rapid and cheap transit of cargo in the ports.	Preparation of a decree to establish the composition of the Facilitation Committee. A representative of UTICA has been nominated as this head of the Committee.	Setting up the technical Facilitation Committee (Decree of February 5, 1996). Issuance of a ministerial decision establishing the composition of the commission preparing the draft revisions of the Customs Code.	Publication of decree introducing a "*unique document*" for customs declaration on imports and exports according to UNO/EEC norms (as proposed by the technical committee).	The Government created a national facilitation committee composed of all concerned groups. The committee produced the single trade document *(liasse unique)* published as decree no. 97-2470 of the Official Gazette on December 30, 1997.
Harmonize Tunisian customs regulations with those of the EU.	Presentation of the terms of reference for the revision of the Customs Code.		Submission to the Council of Ministers of a draft law revising the Customs Code.	A decree was signed which simplifies the documentation and ports procedures and brings the customs code up to date and in conformity with the EU code. GOT adopted standardized formats for electronic data exchanges in external trade operations.

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Telecom Facilitate the development of telecommunications services and infrastructure to enhance the competitiveness of the economy in the future.		Presentation of the orientations of the Government for the development of the telecom sector in the medium-term.	Presentation of a strategy note, including proposed measures, for the development of the telecom sector in the medium-term.	The authorities presented a liberalization agenda to the Bank. The plan proposes selling 10 percent of Tunisie Telecom – the public monopoly –by 2002; liberalizing mobile telephone and paging services in 2000. The authorities have pointed to the strategic character of telecommunications to justify the overly cautious approach to its liberalization.
Legal System Adapt the legal framework to encourage and support economic competitiveness of enterprises.	Government progress in reforming legislation includes the new law on rehabilitation of enterprises in difficulty, law on national and international arbitration, leasing, etc. Begin studies to define priorities concerning legislative reform and implementation with a view to adapting relevant laws and regulations to new national and international economic practices.	(a) Submission for signature of the decree and preparation of the ministerial bylaws (arrêté) introducing legal changes necessary to the structure of the "Centre d'études judiciaires et juridiques" so that the Centre provides an open forum to better establish the legal framework supportive of competitiveness and to include measures to promote and publicize the work of the Center; (b) submission of the terms of reference and hiring of the consultants to prepare a "Legal reform Strategic Action Program".	Submission to the Chamber of Deputies of a draft law regarding a new Company Law. Submission to the Chamber of Deputies of a draft law regarding Private international Law; Submit an agreed "Legal Reform Strategic Action Program".	The authorities prepared a new draft Company Code and hired an international consulting firm to review an earlier draft prepared by Tunisian legal experts. The draft Company Code is a vital piece of legislation encompassing over 500 articles which will enable mergers, acquisitions, and other corporate groupings, not foreseen. which under the previous Tunisian Company law. The Council of Interministerial Ministers discussed the draft agreement in May 1998. This measure was combined with condition relating to adoption of a new companies code and is included in the new draft companies code yet to be adopted

Objectives	Actions Taken Before or During Preparation	Actions Before Board Approval	Actions Before Second Tranche	Implementations Status
Labor Market Flexibility				
Increase flexibility of the labor market.	Revision of the Labor Code (February 1994) in the areas of collective agreements, representation of workers in the enterprise, regulatory frame-work for conflicts, fixation of fines (*dommages et intérês).*	Agreement on revision to the Labor Code in order to reduce the time frame concerning lay-off procedures for economic reasons.		
Social Charges				
Decrease the cost of labor while improving workers' protection.	Increase of the contribution rates paid by workers for both the private and public sectors to contain the financial deterioration of the social security system.	Carry out quantitative analysis of costs and required contribution for a guaranteed fund to finance the separation packages paid to workers laid off for economic reasons.	Submission to the Chamber of Deputies of a draft law concerning a limited severance scheme to cover the separation packages paid to workers laid of for economic reasons.	Bylaw 97-1925 of September 29, 1997 introduced social measures for laid off workers
	Tighter controls on early retirement for the public sector; merging the schemes for self-employed workers in the non agricultural and agricultural sectors; revision of the validation system for both the private and public sectors and revision of the contribution base.	Presentation of measures to create limited system to cover these separation packages.	Agreement to contain the social security contribution rates for the non-agricultural private sector of the general scheme, over 1997-1999, in the context of the ongoing social security reform (the non-agricultural private sector represent 25.75% of the wage bill)	Bylaw 97-4 of February 3, 1997 on social security fulfilled the condition by fixing the rate of social security contribution for the employer at 13 per cent of the wage bill.

Table 6: Key Indicators for Project Operation

Key Operations Indicators in President's Report	Rating	Comments
Macroeconomic indicators:		
- Budget deficit	Satisfactory	
- International reserves	Satisfactory	
- Exports growth	Satisfactory	
- Current account	Satisfactory	
Trade liberalization:		
- Ratification of Free Trade Agreement with EU	Satisfactory	
- Reduction of tariff surcharges	Satisfactory	
Privatization		
- Privatization of agreed share of public enterprises	Satisfactory	
Deregulation/privatization of Maritime transport and Trade Facilitation :		
Deregulation of maritime transport	Unsatisfactory	Report prepared by first consulting firm was deemed incomplete by government. A new plan will be prepared.
Deregulation of ports handling	Unsatisfactory	Negotiations with dockers union was protracted. Chamber of Deputies requires time to discuss and approve draft laws before publication in Official Gazette.
New customs regulation	Satisfactory	
Liasse unique	Satisfactory	
Code des Sociétés	Unsatisfactory	Government adopted a consultative and therefore lengthy process to draft the new code. The draft new code is now before the Chamber of Deputies.

Table 7: Studies Included in Project

Study	Purpose	Status	Impact of Study
Draft company code	To replace old company code and improve the legal and incentive structure for firms	Draft submitted to, discussion in, the Chambers of Deputy	
Review and evaluation of the draft company code.	To evaluate draft code against international best practice.	Completed	Recommendations helped revise the draft new company code.
Telecommunications sector reform strategy	To lay down plan to liberalize telecom sector	Completed	Minimal impact so far; as plan is slow
Labor market study	To propose measures to make the labor market more flexible and reduce labor cost while protecting workers rights.	Completed	Helped design reforms included in policy matrix of program.
Study of port handling	To propose measures to introduce flexibility in port and maritime activities and improve incentive structure of dock workers.	Completed	Laws have been submitted to Chamber of Deputies based o study's recommendations
Study on private commercial activities in port.	To introduce more competition.	Completed	Laws have been submitted to Chamber of Deputies based on study's recommendations.
Revised Customs Code	To revise customs laws so as to make them more flexible.	Completed	Approved Implemented
Restructuring plan of CTN	To propose measures to restructure CTN with view to privatization at a future date.	Complete	Plan has been partially implemented.
Restructuring plan of STAM	To propose measures to restructure STAM with view to privatization at a future date.	First study prepared by consulting firm was deemed incomplete by government. Another study to be prepared.	Study to be completed and implemented.
Privatization in Tunisia	To provide a picture on the status of privatization in Tunisia since 1986; as well as information on existing public enterprises.	Completed	Informed policy measures in the area of privatization.
Review of private international law in Tunisia.	To re-evaluate existing law and incentive structures.	Completed	Conclusions informed the drafting of the new company code.
Study of the impact of the free trade agreement with the EU	To quantify the potential impacts of the FTA	Completed	Helped design reform measures included in the policy matrix (on trade reform and fiscal measures).
Harmonization of trade tariff regimes with non EU countries	To provide ground for trade negotiations with non EU countries	Completed	Helped reach agreements on tariff harmonization with a number of non EU countries
Liasse Unique normalisée a l'importation et l'exportation des marchandises	To propose a single document for import and exports formalities.	Completed	Implemented

Table 8A: Project Costs
(US$ millions)

	Appraisal Estimate			Actual/Latest Estimate		
	Local Costs	Foreign Costs	Total	Local Costs	Foreign Costs	Total
Item						
Balance of Payments Support		75	75		75	75
TOTAL		75	75		75	75

Table 8B: Project Financing
(US$ millions)

	Appraisal Estimate			Actual/Latest Estimate		
	Local Costs	Foreign Costs	Total	Local Costs	Foreign Costs	Total
Source						
IBRD		75	75		75	75
Parallel Financing Institutions						
European Union		120	120		120	120
TOTAL		195	195		195	195

Table 9: Economic Costs and Benefits

Not applicable

Table 10: Status of Legal Covenants

Agreement	Section	Covenant type	Present status	Description of covenant	Comments
Loan 4069 - TUN	3.01(a)	9	C	The Borrower and the Bank shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program and the actions specified in Schedule 3 to this Agreement	No Comment
Loan 4069 - TUN	3.01(b)	9	C	Prior to each such exchange of views, the Borrower shall furnish to the Bank for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Bank shall reasonably request.	No Comment
Loan 4069 - TUN	3.01(c)	9	C	Without limitation upon the provisions of paragraph (a) of this Section, the Borrower shall exchange views with the Bank on any proposed action to be taken after the disbursement of the Loan which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program, including any action specified in Schedule 3 to this Agreement	No Comment
Loan 4069 - TUN	3.02(a)	1	C	Upon the Bank's request, the Borrower shall have the Deposit Accounts audited in accordance with appropriate auditing principles consistently applied, by independent auditors acceptable to the Bank.	No Comment
Loan 4069 - TUN	3.02(b)	1	C	Upon the Bank's request, the Borrower shall furnish to the Bank as soon as available, but in any case not later than six (6) months after the date of the Bank's request for such audit, a certified copy of the report of such audit by said auditors, of such scope and in such detail as the Bank shall have reasonably requested.	No Comment
Loan 4069 - TUN	3.02(c)	1	C	Upon the Bank's request, the Borrower shall furnish to the Bank such other information concerning the Deposit Accounts and the audit thereof as the Bank shall have reasonably requested.	No Comment
Loan 4069 - TUN	2.02(d-1)	9	C	Continued maintenance of a satisfactory macroeconomic framework, consistent with the objectives of the Program, as determined on the basis of macroeconomic indicators acceptable to the Borrower and the Bank.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-2)	12	C	Publication in the Official gazette of the law ratifying the Free Trade Agreement.	See Table 5 on Implementation Status

Covenant Type	Covenant Type (contd.)	Present Status
1= Accounts/audits	8 = Indigenous people	C = Covenant complied with
2= Financial performance/ revenue generation from beneficiaries	9 = Monitoring, review, and reporting	CD = Complied with after delay
3 = Flow and utilization of project funds	10 = Project implementation not covered by categories 1-9	CP = Complied with partially
4= Counterpart funding	11 = Sectoral or cross-sectoral budgetary or other resource allocation	NC = not complied with
5= Management aspects of the project or executing agency	12 = Sectoral or cross-sectoral Policy/regulatory/institutional action	
6= Environmental covenants	13 = Other	
7= Involuntary resettlement		

Table 10 (cont'd): Status of Legal Covenants

Agreement	Section	Covenant type	Present status	Description of covenant	Comments
Loan 4069 - TUN	2.02(d-3)	12	C	Publication in the Official Gazette of the Borrower's 1997 finance Law including satisfactory provisions on tariff reductions scheduled up to the second year of application of the Free Trade Agreement and the related scheduled reductions in surcharges.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-4)	12	CD	Bringing to the point of sale at least fifty-one percent (51%) of the capital of a number of enterprises corresponding to fifty percent (50%) of the net assets of public enterprises producing goods and services established in a list agreed upon between the Borrower and the Bank.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-5)	120	C	Submission to the Chamber of Deputies of a draft law amending Articles 6 and 7 of the Borrower's law No. 77-13 dated March 7, 1977, so as to abrogate existing chartering privileges extended to Tunisian ship-owners.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-6)	12	CP	Publication in the Official Gazette of a Law modifying the Borrower's Decree dated February 17, 1949 concerning working conditions of dock labor so as to render them less complex, and more flexible and adapted to the requirements of modern ports.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-7)	12	CP	Submission to the Chamber of Deputies of a draft law introducing new port regulations, and incorporating the redefinition of the functions of the Office des Ports Nationaux Tunisiens and the new regime of maritime domain.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-8)	12	CP	Implementation of the plan satisfactory to the Bank to restructure the Borrower's Société d' Acconage et de Manutention and the Compagnie Tunisienne de Navigation.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-9)	12	C	Publication in the Official gazette of a Decree mandating the use of, and setting forth the standard format for, an unique document (document unique) for customs declaration on imports and exports.	See Table 5 on Implementation Status
Loan 4069 - TUN	2.02(d-10)	12	C	Submission to the Chamber of Deputies of a draft law introducing a Company Code.	See Table 5 on Implementation Status

Covenant Type	Covenant Type (contd.)	Present Status
1= Accounts/audits	8 = Indigenous people	C = Covenant complied with
2= Financial performance/ revenue generation from beneficiaries	9 = Monitoring, review, and reporting	CD = Complied with after delay
3 = Flow and utilization of project funds	10 = Project implementation not covered by categories 1-9	CP = Complied with partially
4= Counterpart funding	11 = Sectoral or cross-sectoral budgetary or other resource allocation	NC = not complied with
5= Management aspects of the project or executing agency	12 = Sectoral or cross-sectoral Policy/regulatory/institutional action	
6= Environmental covenants	13 = Other	
7= Involuntary resettlement		

Table 11: Compliance with Operational Manual Statements

Statement Number and Title	Description and comment on lack of compliance
No significant lack of compliance with applicable Bank Statements in Operational Manual was observed under the project	

Table 12: Bank Resources: Staff Inputs

Stage of Project Cycle	Planned		Revised		Actual	
	Weeks	US$ (Thousands)	Weeks	US$ (Thousands)	Weeks	US$ (Thousands)
Preparation to appraisal					152.5 (*)	578.4 (*)
Appraisal-to Board					20.7	70.8
Negotiations through Board Approval					6.0	16.0
Supervision	20.0	101.5	2.4	115.2	74.3	248.5
Completion	6.0	29.0	6.0	29.0	6.0	29.0
TOTAL					259.5	942.7

Source: World Bank Management Information System.
Note: (*) Preparation time and cost reflected here include work done before September 1995 but not incorporated in the ECAL.

Table 13: Bank Resources: Missions

Stage of Project Cycle	Month/ year	No. of Persons	Days in the Field	Specialized Staff Skills Represented	Performance Rating		Type of Problems
					Implementa-tion Status	Development Objectives	
Pre-Appraisal	11/95	11	110	Economists (3) Privatization Specialists (1) Financial Sector Spec. (2) Maritime Transport Spec. (2) Labor Market Specialist (1) Legal Reform Specialist (2)			
Appraisal	2/96	8	56	Economists (2) Privatization Specialists (2) Financial Sector Spec. (2) Telecom Specialist (1) Maritime Transport Spec. (1)			
Supervision	5/97	2	22	Economists (2)	S	S	
	11/97	4	20	Economists (2) Financial Sector Spec. (1) Maritime Transport Spec. (1)	S	S	
	12/97	2	8	Maritime Transport Spec. (1) Privatization Specialist (1)	S	S	
	5/98	1	5	Economist (1)	S	S	