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## INTERNATIONAL DEVELOPMENT ASSOCIATION

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REPORT AND RECOMMENDATION  
OF THE  
PRESIDENT  
TO THE  
EXECUTIVE DIRECTORS  
ON A  
PROPOSED CREDIT  
TO THE  
REPUBLIC OF TUNISIA  
FOR A  
SECOND WATER SUPPLY PROJECT

June 9, 1970



INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT AND RECOMMENDATION OF THE PRESIDENT

TO THE EXECUTIVE DIRECTORS ON A

PROPOSED CREDIT TO THE REPUBLIC OF TUNISIA

FOR A SECOND WATER SUPPLY PROJECT

1. I submit the following report and recommendation on a proposed credit in an amount in various currencies equivalent to \$10.5 million to the Republic of Tunisia. The proposed credit would be relent to the Société Nationale d'Exploitation et de Distribution des Eaux (SONEDE), to finance a second water supply project.

PART I - HISTORICAL

2. In March 1966, the Government requested the Bank's assistance in identifying and preparing a water supply project. On the Bank's advice it engaged the services of consultants, drew up the "1968-1973 National Water Program", and created an independent national water corporation, Société Nationale d'Exploitation et de Distribution des Eaux (SONEDE), which in 1968 took over the existing government water supply services.

3. In January 1969 the Bank made a loan of \$15 million (No. 581-TUN) to SONEDE, with the guarantee of the Republic of Tunisia. The Kingdom of Sweden, through the Swedish International Development Authority (SIDA), simultaneously granted a credit of \$5 million equivalent to the Republic of Tunisia which was relent to SONEDE. This joint operation financed high priority works whose preliminary study was completed. At that time, a further group of works called the "Second Project" was already identified. The present project includes these works, as well as additional works not foreseen at the time, mainly in tourism regions. The present project will be implemented during approximately the same period (1970-1973) as the first project. The Kingdom of Sweden, through SIDA, has again participated in the appraisal of the project and negotiated at the same time as the Association a \$3.5 million credit on IDA terms.

4. Negotiations took place in Washington from May 11 to 19, 1970. The Government was represented by Mr. Moncef Belhadj Amor, Director of the Budget, Mr. Zine Mestiri of the Secretariat of State for Planning and Mr. Habib Ben Yahia of the Tunisian Embassy. Mr. Taieb Ben Ghanem, Director General of SONEDE, represented the Beneficiary. The Kingdom of Sweden was represented by Messrs. Sven Ohlund and Tor Kvarnback of SIDA and Mr. Björn Elmer of the Swedish Embassy in Washington.

5. Following is a summary statement of loans and credits to Tunisia as of April 30, 1970:

Loan or Credit Number	Year	Borrower	Purpose	Amount (US\$ million)		
				Bank	IDA	Undisbursed
29	1962	Republic of Tunisia	Education		4.9	-
380	1964	Republic of Tunisia	Port Development	7.0		-
449	1966	Société Nationale d'Investissement	Development Finance Co.	5.0		.4
94	1966	Republic of Tunisia	Education		13.0	5.7
484	1967	Republic of Tunisia	Cooperative Farms	12.0		8.1
99	1967	Republic of Tunisia	Cooperative Farms		6.0	4.0
512	1967	Société Nationale d'Investissement	Development Finance Co.	10.0		4.8
573	1968	Office des Ports Nationaux Tunisiens	Port Development	8.5		7.3
581	1969	SONEDE	Water Supply	15.0		14.8
606	1969	SNCF	Railways	8.5		8.5
150	1969	Republic of Tunisia	Railways		8.5	8.4
S2	1969	Republic of Tunisia	Highway Engineering	.8		.7
648	1969	Société Nationale d'Investissement	Development Finance Co.	10.0		10.0
Total (less cancellations)				76.8		
of which has been repaid to Bank and others				1.7		
Total now outstanding				75.1		
Amount sold				1.2		
of which has been repaid				.4		
Total now held by Bank and IDA				74.3	32.4	
Total undisbursed				54.6	18.1	72.7

6. Only about a third of Loan No. 484-TUN and Credit No. 99-TUN (Cooperative farm project) has so far been disbursed. After a rather slow start the project has been seriously affected by changes in the Government's agricultural policy (cf. para. 25 below). These changes have raised serious doubts as to the extent to which the project can be implemented as originally envisaged. A Bank supervision mission visited the country in October 1969 and again in March 1970. Its findings are being reviewed and will be reported to the Executive Directors in the near future.

7. Disbursements on Credit No. 94 (Education II) have been delayed, but most expenditure under this project has now been made and requests for reimbursements will be sent to the Association shortly. Initial delays in the preparation of bidding documents account for low disbursements under Loan No. 573 (Ports II), but a number of contracts have now

been awarded and an acceleration in disbursement is expected. Disbursements under Loan No. 581 (Water Supply I) will accelerate during the coming months when all major construction work will start. Disbursement on the Railroad project (Loan No. 606-TUN and Credit No. 150-TUN) has hardly started because the damages caused by serious floods last autumn had first to be repaired. The second loan to SNI (No. 512-TUN) has been totally committed and disbursements are proceeding satisfactorily. The third loan (No. 648-TUN) became effective on May 5, 1970.

8. In 1962, IFC invested \$2.0 million in NPK-Engrais, a phosphate fertilizer company. In 1966, IFC made an investment of D 300,000 (about \$571,500) in Société Nationale d'Investissement (SNI). On June 2, 1970, IFC's Executive Directors approved a second investment of \$630,000 in SNI which will allow IFC to maintain its 20 percent participation when SNI will soon double its share capital. In 1969 IFC made an investment of \$9.9 million (\$8 million as a loan and \$1.9 million in share capital) in COFITOUR, a tourism development and holding company.

9. The Bank and IDA are at present considering a gas pipeline project, a family planning project, a highway construction project, an agricultural credit project and a tourism infrastructure project.

PART II - DESCRIPTION OF THE PROPOSED CREDIT

10.       BORROWER:               Republic of Tunisia

          BENEFICIARY:           Société Nationale d'Exploitation et de  
                                  Distribution des Eaux (SONEDE)

          AMOUNT:                 US\$10.5 million in various currencies

          PURPOSE:                To finance the second project under Tunisia's  
                                  National Water Program for 1968-1973

          AMORTIZATION:         In 50 years, including a 10-year period of  
                                  grace, through semi-annual installments of  
                                  1/2 of 1 percent from November 15, 1980  
                                  through May 15, 1990, and 1-1/2 percent from  
                                  November 15, 1990 through May 15, 2020.

          SERVICE CHARGE:      3/4 of 1 percent

          RELENDING TERMS:      Amortization over 25 years, including a  
                                  5-year period of grace, with interest of  
                                  7 percent per annum.

11.       The Swedish credit of \$3.5 million equivalent will be extended to the Republic of Tunisia on IDA terms and will be relent to SONEDE on the same terms.

PART III - THE PROJECT

12. A report entitled "Appraisal of the Second Water Supply Project - Tunisia" (No. PU-37a) is attached.

13. Tunisia's water resources are limited and are located at considerable distance from the main population centers and the principal tourist areas. The urban population is increasing twice as rapidly as total population and the rate of increase in water consumption is even higher. Tourism, mainly from Western European countries, has become a major foreign exchange earner for Tunisia, and can be expected to continue to develop rapidly. Water supply in certain cities and tourist areas is becoming a serious problem.

14. The total cost of the National Water Supply Program for the period 1968-1973 is presently estimated at about \$58 million. It can be divided into three parts:

- a) The first part (\$28.4 million) for which the Bank and Sweden have jointly lent \$20 million, consisting mainly of priority supply works in the most populated areas (Tunis, Cap Bon and Sahel).
- b) The second part (\$19.2 million) to be financed in part by the proposed credit and a new Swedish credit, consisting mainly of supply works for industrial centers not covered by the first project, and for tourist areas in southern Tunisia, the Sahel and Cap Bon.
- c) The third part (\$10.6 million), consisting of miscellaneous works and renewal operations which SONEDE is executing mainly with its own funds and some foreign bilateral assistance.

This program will cover water supply needs in the areas concerned at least up to the end of the 1970's. Further works will be needed in the areas of Djerba, Sfax and Lake Ischkeul and will be started after 1973. Engineering studies for future water supply projects are included in the proposed IDA/Swedish financing.

15. SONEDE, the beneficiary of the proposed IDA credit, is a water supply organization owned by the State, with a large degree of autonomy in its operation. It was formed in 1968 in agreement with the Bank and the Swedish Government and has been operating efficiently. Its management and staff are competent; SONEDE is introducing new salary scales which should help retain its qualified staff.

16. The Government had agreed to provide \$20.3 million to SONEDE as its contribution to the 1968-1973 National Water Supply Program. However, the Government is now facing substantial additional financial requirements

to repair the damages caused by the severe floods of last autumn. In the circumstances it would seem appropriate to reduce the total government contribution to the program to \$15.7 million, part of which has already been paid to SONEDE. This contribution, together with the IDA/Sweden financing and SONEDE's own cash generation should be adequate to finance the program. Should the need arise, however, the Government remains committed to provide additional financing as required.

17. The project includes eight sub-projects to expand and strengthen water supply systems in four regions and four cities of Tunisia comprising the country's fast growing tourism and industrial centers. It will mainly consist of constructing and reinforcing water transmission pipelines which will connect existing distribution systems to ground-water resources in the interior of the country. Seventy percent of the project will benefit tourism areas. The internal rate of return of the project is expected to be at least 11 percent; in addition the project will reduce the danger of water-borne diseases. No adverse repercussion on the ecology are expected from it.

18. The total estimated cost for the project is \$19.2 million, including \$11.3 million in foreign exchange. The financing to be provided by the Association and the Kingdom of Sweden would total \$14 million, so that some \$2.7 million (or 19 percent) of the IDA/Swedish financing would be devoted to local expenditures. Tunisia's investment requirements are large and its development program requires external assistance in excess of the foreign exchange component of development projects suitable for international financing. Hence Bank Group assistance at an adequate level could not reasonably be provided if it were restricted to foreign exchange expenditure only. In these special circumstances, I believe that the financing of some local currency expenditures is justified.

19. For this project, as for the first one, international competitive bidding would be used for all major supply and construction contracts. The margin of preference for local suppliers for purposes of bid comparison would be 15 percent or the customs duty, whichever is lower. The IDA and Swedish credit would be simultaneously disbursed at a ratio of 3:1 for actual foreign exchange expenditures and -- on an agreed percentage basis -- for expenditure on construction contracts and goods locally produced or procured.

20. Water rates were raised from an average of 32 millimes to 60 millimes in 1968 as a condition of the Bank loan. After completion of the project SONEDE should earn a minimum rate of return of 5 percent in the years 1973 to 1975 and of 6 percent thereafter. This target would require one further rate increase to 70 millimes in 1973 on the basis of present sales forecasts. SONEDE and the National Electricity and Gas Corporation (STEG) have now negotiated a plan for discharging liabilities existing between them and mainly stemming from the previous collection of water charges by STEG. The agreement is to be executed before the Credit Agreement would become effective.

PART IV - LEGAL INSTRUMENTS AND AUTHORITY

21. The Draft Joint Financing Agreement between the Republic of Tunisia, the Kingdom of Sweden, the Association and SONEDE, the draft Credit Agreement between the Republic of Tunisia and the Association, the Recommendation of the Committee provided for in Article V, section 1(d) of the Articles of Agreement and the text of a Resolution approving the proposed Credit are being distributed to the Executive Directors separately.

22. The contents of the various agreements conform substantially to the pattern of agreements used for water supply projects, and in particular that of the Loan Agreement for the Water Supply I Project (Loan No. 581 TUN). To reflect the joint financing arrangements, matters of common interest to the Association and Sweden are contained in a Joint financing agreement: the draft Association Development Credit Agreement and the Swedish Credit Agreement contain the financial terms and other matters of primary interest to the Association and to SIDA respectively.

23. Particular attention is drawn to the provisions of the Joint Financing Agreement requiring Tunisia: (i) to take all necessary steps to acquire or enable SONEDE to acquire the ownership or the right of occupancy of all land needed for the Project (Section 5.05); and (ii) to ensure to SONEDE the use of ground water resources in certain areas (section 5.07).

PART V - THE ECONOMY

24. An economic mission visited Tunisia in January/February 1970 and reviewed the current position and prospects of the economy. Its report was circulated to the Executive Directors on May 5, 1970 (EMA-22a).

25. At the beginning of 1969, the Government decided that all agricultural land should be incorporated in production cooperatives. Private land was included into new cooperatives or adjacent ones, changing the area and development plans of existing cooperatives. Skilled manpower already scarce was spread even more thinly in an attempt to manage the enlarged program. As the new cooperatives were created, discontent amongst farmers grew rapidly and, in September 1969, the Government reversed its policy. Former landowners were permitted to withdraw with their land from the cooperatives, and a large number of cooperatives was dissolved. These changes in policy disorganized the agricultural sector. While the potential burdens on public finance and skilled manpower has been removed, the problem of modernizing Tunisia's agriculture remains.

26. Weather conditions and floods also affected the economy adversely in 1969, and the increase in gross domestic product in real terms was only 4.5 percent. However, expansion in the petroleum, manufacturing and tourist sectors was satisfactory. Domestic savings rose as a result of an improvement in Government finance. The over-all balance of payments showed a

surplus, despite an increase in the trade deficit, as public capital inflow rose substantially. The projected growth of GDP in 1970 is about 7.5 percent. A balance of payments surplus is expected to result again from high public capital inflow.

27. The internal and external financial position calls for further efforts to improve economic performance, particularly to raise domestic savings, exports and investment productivity. Some measures have been initiated to strengthen financial control in the Government and preliminary steps have been made towards re-organizing a number of state-owned enterprises. Projects for which investment decisions had not yet been taken are being re-examined.

28. The external debt burden remains high. About 25 percent of export receipts on goods and services were devoted to the service of external debt in 1969 including 21 percent on public and publicly guaranteed debt alone. Payments on the present debt in the coming ten years will be large and limit the scope for assuming further debt service obligations. External assistance on concessionary terms should be maintained at least at the present level, and Tunisia's short and medium borrowing should be reduced further, in order to prevent the debt service burden from becoming excessively large. Repayments on short and medium term debt (18 months to 10 years) will total \$40 million in 1970 while, under its current stand-by agreement with the IMF, the Government has undertaken to contract during the same period not more than \$36 million of new debt in this category. In these circumstances Tunisia's creditworthiness is limited, and assistance from the Association appropriate and justified.

#### PART VI - COMPLIANCE WITH ARTICLES OF AGREEMENT

29. I am satisfied that the proposed Credit would comply with the Articles of Agreement of the Association.

#### PART VII - RECOMMENDATION

30. I recommend that the Executive Directors of the Association approve the proposed credit.

Robert S. McNamara  
President