Faced with persistently high unemployment, particularly among college graduates, Tunisia has been working with IBRD to improve its global competitiveness and accelerate economic growth. Since the late 1990s, Tunisia has become one the leading economies in Africa in terms of competitiveness and between 1996 and 2007 saw a doubling in exports of goods and services.

The Challenge

In the half century since independence, Tunisia country has made major economic and social advances, reflected in the combination of a quadrupling of per capita gross domestic product (GDP), the increase in life expectancy to near developed-country levels, and the drop in poverty to less than four percent of population.

The creation of an offshore regime in 1971 to reduce the anti-export bias inherent in the strict import-substitution policy of the 1960s significantly contributed to economic performance. The offshore regime grants several fiscal and financial incentives to exporting firms, including duty-free imports of raw materials and equipments entering the production, 10 year tax holiday and free repatriation of profits. It allowed Tunisia to attract foreign direct investments, break into global manufacturing chains and create massive jobs in the clothing as well as other manufacturing sectors.

It was evident, however, that a hybrid trade policy stance combining heavy protection and control of the domestic economy with an “enclave” (or offshore) business climate was inconsistent with robust long term-growth and job creation. As students leaving university began to struggle to find work in the early 1990s, the unemployment rate began climbing, reaching 15 percent in 1999. The jobless rate declined slightly since then but remained around 14 percent. Given the rapid pace at which young university graduates enter the labor market, it became evident that beyond foreign investment in the offshore sector, the country needed to enhance the efficiency and competitiveness of the domestic economy to avoid a significant deterioration of the employment situation.

Approach

The Association Agreement signed with the European Union (EU) in 1995 offered a key instrument to lock private sector development and trade reforms in. The government established a plan to gradually reduce the protection of the onshore sector but accompanied it with reforms to adjust to heightened competition and to enhance the competitiveness of Tunisian firms.
The reforms thus encompassed trade and logistics reforms, administrative and regulatory reforms to enhance the investment climate, the creation and empowerment of a competition council, reform of the banking and insurance sectors to increase access to finance and liberalization of key backbone services such as maritime transport, port and telecommunication sectors to reduce transaction costs and the attractiveness of the country to investors.

The Bank supported these reforms through five successive policy-based lending programs as seen below.

Results

Through a range of development policy loan programs with IBRD, Tunisia has boosted its global competitiveness and seen exports double over a little more than 10 years.

The best illustration of Tunisia’s improved competitiveness is its total factor productivity growth, which often drives investment. Total factor productivity rebounded from a negative rate in the 1980s to 1.24 percent in the 1990s and 1.40 percent in 2000–2006. While productivity growth in 2000–2006 remained below South Korea’s and Malaysia’s, it represented one of the best performances in the Middle East and North Africa region. Furthermore, exports of goods doubled in value between 1996 and 2007, while annual foreign direct investment (FDI) flows increased steadily, averaging 2.2 percent of GDP in 1996–00, 2.6 percent in 2002–05 and 5 percent in 2006–2008. Tunisia ranked as Africa’s most competitive country in Davos’ 2009 Global Competitiveness Report. All this translated into a 5 percent growth since the mid-1990 despite recurrent internal (e.g., droughts) and external shocks.

The outputs of the bank-supported programs that have directly contributed to the enhanced competitiveness include:

- Strengthening the competition law and creation of a competition council.
- Simplification of procedures for business start-up, including the establishment of a one-stop licensing system and the reduction of “prior-authorization” from over 400 activities to 60.
- Elimination of the restriction on foreign participation in capital of insurance firms.
- Partial liberalization of the telecommunications sector, which led to a significant increase in access and lower prices for telecom services.
- Law granting the insurance regulator administrative and financial autonomy.
- Simplification of the tariff regime by progressively reducing the number of tariff bands from the initial 54 to five.
- Adoption of standards and quality norms applicable to all Tunisian imports.
- Reduction in average port clearance time to three from six days and of the time to approve an industrial zone to six months from 44 between the early 2000 and 2008.

Additional outputs expected in the immediate future include:

- Putting online the registry of commerce and making it accessible to anyone.
- Expediting import control through adoption of risk-based selection methods.
Further reducing the number of prior authorizations required to start a business.

Enhancing transparency and revenue by introducing a unique identifier for all firms.

Reducing non-performing assets of the banking system.

Enhancing access of minority investors to financial information, through improved disclosure, a new legal and accounting framework, and improving the stock market.

World Bank Contribution

Mindful of the need for greater openness of the economy, the government requested World Bank support to buttress reforms for greater internal competitiveness and for simplification and improvement of trade policies. IBRD responded through a series of analytical work that underpinned five successive development policy loans (DPL). In addition to supporting policy reforms through DPLs, IBRD approved two successive investment loans to assist reforms in the area of trade facilitation and export promotion (Export Development Projects 1 and 2).

The first four DPLs were called Economic Competitiveness Adjustment Loans (ECAL). The fifth, approved in 2009, is instead termed Integration and Competitiveness Loan, to signal the completion of Tunisia’s “adjustment” and the opening of the new chapter of “deepening integration with Europe and the other regions”.

The Bank approved the first in the series of Economic Competitiveness and Adjustment Loans (ECAL I) in July 1996, for an amount of US$75 million. The five main policy areas in the ECAL I were: (a) a sound macroeconomic and fiscal framework; (b) acceleration of the implementation of the free trade agreement with Europe; (c) acceleration of the privatization program; (d) greater flexibility in the labor market; and (e) administrative and regulatory reforms.

The second ECAL (ECAL II) was approved in April 1999, for an amount of US$159 million. It aimed to support a program of reform in the financial sector to supplement on-going reforms in the real sector.

The third ECAL (ECAL III) was approved in 2000 for an amount of €281 million with the aim of maintaining a stable macroeconomic framework, promoting private investment, strengthening the financial sector, and liberalizing the information and communication technology sector.

The fourth ECAL (ECAL IV), was approved in June 2005 for an amount of US$150 million aimed to support mutually reinforcing development objectives: (a) maintaining a sound and reactive macroeconomic framework, in particular by promoting fiscal consolidation and strengthening the medium term fiscal framework; (b) improving Tunisia’s private investment climate and increasing private investment opportunities; and (c) reinforcing the financial sector’s capacity to finance growth, by supporting initiatives to reduce the level of non-performing loans, further strengthening the regulatory framework for bank intermediation, and fostering development of contractual savings, especially in the insurance sector.

The first Integration and Competitiveness Loan (ICL 1), approved in March 2009 for an amount of US$250 million supported policy actions in the following areas: (i) reducing trade transaction costs and deepening Tunisia’s global economic integration; (ii) further improving the business climate to enhance competitiveness of Tunisian firms, including services; and; (iii) strengthening the financial sector to increase its capacity to finance private investment.

The EDP I sought to foster export competitiveness of Tunisian firms through activities clustered around three components: (i) export market access which included a matching grant fund to cover up to 50 percent of the cost of consultant services required to enter export markets; (ii) pre-
shipment export finance guarantee which encouraged financial institutions to provide pre-shipment financing to small enterprises medium enterprises and emerging exporters with viable export contracts and (iii) a trade facilitation component which supported investments and technical assistance required to reduce the number of procedures and transaction costs involved in trading activity.

The EDP II was approved in 2005 for an amount of US$42 million. Its objectives were to consolidate the results achieved by the EDP I project focusing on two components: (i) improve access to export markets and finance and (ii) further enhance the efficiency and performance of trade clearance processes (customs operations and technical controls).

Partners

IBRD has maintained close partnerships with other donors, especially the European Union and the African Development Bank. This trilateral cooperation has worked steadily and especially well to assist the sustained efforts made by the Tunisian government to reduce the economic distance between the country and its major trade partners.

However, the major reason for the successful results of World Bank support has been the close cooperation with the Tunisian government, which views the partnership with the Bank as playing “an important role in Tunisia’s development,” according to Tunisia’s Prime Minister in December 2009. When first beginning to move away in the mid-1980s from the tightest forms of state control of the economy, Tunisia asked the World Bank for financial support and advice on difficult reforms. The unusually good collaboration during the reforms of 1986–90 set a positive tone which has been critical to sustaining a constructive partnership, even during candid dialogues on sensitive issues such as governance and distortions of internal competition.

Next Steps

Tunisia needs to further boost private investment and productivity growth in order to reach 6–7 percent growth and to reduce unemployment. While FDI inflows have been continuously flowing in, domestic private investment has increased only from 12.3 percent of GDP in 1997 to 14.2 percent of GDP in 2007. This level of private investment is below that attained by other successful emerging countries and is insufficient to sustain the productivity growth that has driven recent economic expansion. The world's fastest growing economies have indeed displayed high investment rates. Thus there is much scope in further enhancing the business climate and trade integration through reforms that the Bank could support through policy-based lending. Reforms that target competition issues, such as anti-competitive practices and unfair competition that continue to hinder investment will be particularly important.

However, beyond strengthening the enabling environment for growth, Tunisia needs to improve the quality of growth by supporting innovation. Indeed, as shown in a Bank new report (“Tunisia’s Development Policy Review: Towards Innovation-Driven Growth”), the economy is still largely dominated by low-skilled, low value-added activities, especially in manufacturing. Indeed, Tunisia’s economic sectors are intensive in low-skilled workers and only 15 percent of currently employed people have a university degree. More than 90 percent of workers in textiles and clothing and the mechanical and electrical sectors (which together account for 60 percent of Tunisia’s exports) are low-skilled workers. Thus, the “economic space” for absorbing university graduates that now constitute 60 percent of new entrants in the labor market is extremely limited. This partly explains the high and growing unemployment rate of this category of job-seekers. A key challenge is therefore to promote a gradual transformation of traditional sectors into higher-value-added, knowledge-
intensive sectors as well as increased investments in new and emerging technology-intensive sectors. If Tunisia succeeds in transitioning to a productivity-driven growth approach, it could reduce unemployment in two mutually reinforcing ways: by raising productivity and GDP growth (which will benefit all types of workers) and by increasing the scope for hiring highly-educated workers. As agreed in the new Country Assistance Strategy for Tunisia, the World Bank is committed to supporting the government’s new growth model through analytical work, technical assistance, and development policy loans in the years to come.

SUGGESTIONS FOR RECENT READING: