

AFRICAN DEVELOPMENT BANK



TUNISIA

FINANCIAL SECTOR MODERNISATION SUPPORT PROGRAMME II - (PAMSFI II)

RDGN/PIFD DEPARTMENTS

April 2019

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CURRENCY EQUIVALENTS

January 2019

UA1	=	4.17 Tunisian dinar (TND)
UA1	=	EUR 1.22
UA 1	=	USD 1.39

FISCAL YEAR

1 January to 31 December

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ACRONYMS AND ABBREVIATIONS

ACM	Microfinance Control Authority
AFD	French Development Agency
AfDB	African Development Bank
AFMI	African Financial Markets Initiative
ARP	Assembly of People's Representatives
ATIC	Tunisian Capital Investors Association
BCT	Central Bank of Tunisia
BDR	Regions Bank
BIAT	Banque internationale arabe de Tunisie
BTS	Tunisian Solidarity Bank
BVMT	Tunis Stock Exchange
CGA	General Insurance Committee
CM	Council of Ministers
CMF	Financial Markets Council
CSP	Country Strategy Paper
CwA	Compact with Africa
DGGDCF	Directorate-General for Debt Management and Financial Cooperation
EBRD	European Bank for Reconstruction and Development
EU	European Union
FCPR	Risk Mutual Fund
FDI	Foreign Direct Investments
FIPA	Foreign Investment Promotion Agency
FTUSA	Tunisian Federation of Insurance Companies
GBS	General Budget Support
GDP	Gross Domestic Product
HAICOP	High Commission for Public Procurement
IMF	The International Monetary Fund
ITCEQ	Tunisian Institute of Competitiveness and Quantitative Studies
KfW	Kreditanstalt für Wiederaufbau
LF	Finance Law
MAS	Ministry of Social Affairs
MCA	Micro Credit Association
MDICI	Ministry of Development, Investment and International Cooperation
MENA	Middle East and North Africa
MFI	Microfinance Institution
MFPE	Ministry of Vocational Training and Employment
MoF	Ministry of Finance
MTND	Million Tunisian Dinars
NDP	National Development Plan
NIS	National Institute of Statistics
OECD	Organisation for Economic Cooperation and Development
PADRCE	Skills Development and Job Creation Support Programme.
PAGDI	Governance and Inclusive Development Support Programme
PAMSF	Financial Sector Modernisation Support Programme
PARDI	Economic Recovery and Inclusive Development Support Programme
PBO	Programme-based Operation
PDAI	Integrated Agricultural Development Programme
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
PNAFN	National Assistance Program for Vulnerable Families
SBS	Sector Budget Support
SFL	Supplementary Finance Law

SICAR	Venture Capital Investment Company
SICAV	Open-End Investment Company, or Mutual Fund
SME	Small and Medium-Sized Enterprises
SMT	Société monétique tunisienne (E-Banking Company of Tunisia)
SVT	Primary Dealers
TFP	Technical and Financial Partners
TND	Tunisian dinar
UA	Unit of Account
UTICA	Tunisian Confederation of Industry, Trade and. Handicrafts
VSMEs	Very Small and Medium Sized Enterprises
WB	World Bank

PROGRAMME INFORMATION

INSTRUMENT:	Sector Budget Support (SBS)
PBO DESIGN TYPE:	Programme-Based Operation in two Stand-Alone programmes (2016/2017 and 2018/2019)

LOAN INFORMATION

Client Information

BORROWER	:	Republic of Tunisia
EXECUTING AGENCY	:	Ministry of Finance (MoF)

Financing Plan

Source	Amount (UA)	Amount (EUR)	Instrument
AfDB	98 million	120 million	Loan
TOTAL COST	98 million	120 million	

ADB's Key Financing Information

Loan Currency	Euro
Loan Type	Fully flexible loan
Maturity	As indicated in the loan agreement
Deferred depreciation	As indicated in the loan agreement
Weighted average maturity **	As indicated in the loan agreement
Reimbursements	As indicated in the loan agreement
Interest rates	Base rate + Cost of financing margin + Loan margin + Maturity premium (this interest rate must be greater than or equal to zero)
Base rate	Floating rate 6-Month EURIBOR revised on February 1st and August 1st. A free option is available to fix the base rate
Financing cost margin	The Bank's margin on financing costs revised on 1st January and 1st July and applied on 1st February and 1st August with the base rate
Margin of Loan	80 basis points (0.8%)
Maturity premium	0% if weighted average maturity <= 12.75 years

Timeframe – Main Milestones (expected)

Completion of Phase 1 and dialogue	April 2018
Preparation	September 2018
Appraisal	December 2018
Programme Approval	March 2019
Effectiveness	April 2019
Disbursement	April 2019
Completion	December 2019
Closing Date:	December 2019

PROGRAMME EXECUTIVE SUMMARY

<i>Programme Overview</i>	<p><u>Programme Name:</u> Financial Sector Modernization Support Programme II - (PAMSFI II)</p> <p><u>Overall Implementation Schedule:</u> Sector Budget Support - Programme-based Operation - Phase 2 - 2018/2019 (Phase 1 covered 2016/2017)</p> <p><u>Programme Cost:</u> UA 98 million (EUR 120 million)</p>
<i>Programme Objectives</i>	<p>The goal of PAMSFI II is to create the necessary conditions for accelerated, resilient and inclusive economic growth by strengthening the financial sector's role in financing the economy and vulnerable segments of the population. In particular, it aims to support the emergence of a new development model for Tunisia, in which the private sector can develop and generate employment throughout the country, and where disadvantaged segments of the population can contribute to, and benefit from, growth. PAMSFI II is also strongly aligned with Tunisia's commitment matrix under the Compact with Africa (CwA), which complements and enhances the measures of Pillar 3 on the financing framework. The Programme's specific objectives are to strengthen and deepen financial sector governance by improving access by the population and businesses to diversified financial services.</p>
<i>Alignment with Bank Priorities</i>	<p>The Programme will contribute to the objectives of financing industrialization, improving the population's quality of life and agriculture in the context of the High 5 Priorities. It is aligned with the Country Strategy Paper 2017-2021, the first pillar of which, "Industrialisation and development of value chains", focuses on policies and reforms to reduce the cost of production factors and strengthen the competitiveness of financial services. The programme is also aligned with the second pillar "Improving the quality of life of populations in priority regions" by supporting the development of micro, small and medium-sized enterprises (MSMEs) through improved access to financial services. It is also aligned with the two pillars of the Bank's Financial Sector Development Policy Paper and Strategy 2014-2019, which focus on increasing access to financing for partially and unserved populations; and on expanding and deepening financial systems.</p>
<i>Needs Assessment and Rationale</i>	<p>By improving access by the population and businesses to financial services, diversifying the latter and improving the stability of the financial system, the Programme will help to address the main challenges facing Tunisia, namely weak growth, high unemployment and wide regional and social disparities. The Bank's assistance is justified by the need to support the priority reforms of the banking sector embarked upon by the Government with a view to achieving the structural transformation of the economy. It also provides crosscutting support to Tunisia's other priority reforms. It will contribute, through better financing of the economy, to supporting growth and improving the macroeconomic framework, it will also help to improve the business climate by facilitating access to financial services. It will also support reforms related to social protection by fostering the financial inclusion of the most vulnerable social groups.</p>
<i>Harmonization</i>	<p>Under Pillar 3 of the CwA, the Bank is in continuous dialogue with Tunisia's main technical and financial partners (TFPs) to ensure that interventions are complementary. The measures supported are complementary to the ongoing and planned interventions by the TFPs in relation to the financial sector, in particular the World Bank, the International Monetary Fund (IMF), the French Development Agency (AFD), the European Bank for Reconstruction and Development (EBRD), the German Development Bank (KfW) and the European Union (EU). KfW provided its financial sector budget support in close collaboration with the Bank and based on the results of PAMSFI I.</p>
<i>Bank's Value Added</i>	<p>PAMSFI II is a vehicle for support to the Bank's other operations in Tunisia. Therefore, its impact will consolidate the achievements of PAMSFI I and other policy-based programmes aimed at improving regional development and job creation. Indeed, these programmes support regional structures, the business framework in the regions as well as youth employability, whereas PAMSFI will provide complementarity on the supply side of financing by targeting project proposers and VSME. PAMSFI II also complements investment projects in the infrastructure sector supported by the Bank. The Bank is coordinating Pillar 3 on financing the Compact with Africa matrix. This matrix is of special interest right up to the helm of State.</p>
<i>Contributions to Gender Equality and</i>	<p>One of PAMSFI II's objectives is to strengthen the micro-credit sector by improving its governance, and by preparing a strategic vision for financial inclusion. 57% of micro-credit beneficiaries in Tunisia are women. They borrow from micro-credit associations to finance</p>

<i>Women's Empowerment</i>	small productive projects in the agricultural and handicraft sectors, usually in rural areas. Thus, the impact of the measures contained in PAMSFI II to increase financial inclusion (specific financing products for women entrepreneurs) and promote microcredit will be greater among Tunisian women, whose participation in the development process will be increasingly strengthened.
<i>Policy Dialogue and Related Technical Assistance</i>	The Bank has maintained close policy dialogue with the Tunisian Authorities on financial sector reforms whose broad lines were set out in the key reform programmes. The themes covered focused on SME financing, microfinance sector restructuring and private equity, as key drivers of inclusive growth. The Bank has also enriched the design of this programme with the outcomes of PAMSFI I and the conclusions of workshops organized by the sector over the past two years. In the context of this programme, this dialogue will continue with a view to monitoring the agreed reforms, but also in terms of guidance and technical assistance particularly concerning financial inclusion, and the establishment of a debt agency with support from the African Financial Markets Initiative (AFMI).

Results-Based Logical Framework

Country and Project Name: Tunisia - Financial Sector Modernization Support Programme II - (PAMSFI II)						
Programme Goal: Contribute to the Tunisian Government's efforts to create conditions for accelerated, resilient and inclusive growth through financial sector development and the improvement of the financing of the economy.						
		PERFORMANCE INDICATORS			MEANS OF VERIFICATION	RISKS MITIGATION MEASURES
		Indicators (including ISC)	Baseline	Target		
IMPACT	Accelerated growth thanks to better financing of the economy	Real GDP Growth Rate	2.5% in 2018	More than 3.4% in 2020	Economic budget, MDICI	
	OUTCOMES	I. Financial inclusion is improved	Financial inclusion ratio	36% in 2015	38% in 2020	Report of SNIF, MoF
Proportion of women beneficiaries of microcredit (in relation to total number of beneficiaries)			48% in 2018	55% in 2020	ACM	
II. Financial sector governance is enhanced		Credit to the private sector, % of GDP	83.8% in 2018	86% in 2020	Annual Report of BCT	
		Contribution of the financial market to the financing of gross fixed capital formation in the private sector	8% in 2018	11% in 2020	Annual Report of CMF, MoF	
COMPONENT I - REDUCTION OF SOCIAL AND REGIONAL DISPARITIES THROUGH BETTER FINANCIAL INCLUSION						<p>Risk Declining pace of reforms as elections approach</p> <p>Mitigation measures: PAMSFI II aims to consolidate the reforms initiated in the first phase</p>
OUTPUTS	I.1. Financial Inclusion					
	Development of accountable microfinance	Publication of the Order on the doubling of the microcredit ceiling	Microcredit ceiling limited to DT 20,000	Ceiling raised to TND 40,000	MoF	
		Transmission by the Minister of Finance of the draft decree setting out the administrative and financial penalties imposed by the Microfinance Supervisory Authority on MFIs, together with the opinion of the ACM Board of Directors to the President of the Government)	Regulatory framework governing microfinance without a system of administrative and financial sanctions	Order for administrative sanctions against MFIs issued before the end of the programme	ACM	
	Financial services and products (digital finance, micro-insurance, natural disaster compensation and social housing, index insurance)	Launch of the digital payment product for public education students' enrolment	Few digital financial products for citizens	100% of students conduct their enrolments on line	SMT	
		Publication of the Decree on the Real Estate Loan Guarantee Fund for the population with irregular income	Inadequate offer of housing-related financing products for women and the irregular income population	Decree published before the end of the programme	MoF	
	I.2. Financing of VSMEs					
Financing of SMEs in the regions	Adoption by the Council of Ministers of the draft law establishing the Bank of the Regions (BDR)	No vehicles devoted to the financing of SMEs in the regions.	BDR established before end 2019	MoF		

Guarantee products	Signing of the agreement between the MoF and SOTUGAR for the Dhamen Express guarantee product for SMEs, in order to revitalise the national guarantee system and facilitate SMEs' access to credit.	Current guarantee ineffective VSMEs have little equity and collateral to offer as guarantee for their loans.	Agreement signed before programme end	MoF	
Support to SMEs	Publication of the decree establishing the SME Restructuring Fund	No funds to support SMEs in difficulty	The decree establishing the fund is published in 2019	Ministry of Industry and SMEs	
Strengthening of equity	Adoption by the Council of Government of the draft law on crowdfunding	No instrument governing Crowdfunding	Draft law adopted by the CM before end 2019	MoF	
Financing innovation	Signing of agreement between the Ministry of Finance, the Ministry of ICTs and SOTUGAR	No incentive framework for financing innovative start-ups	Agreement signed in 2019	MoF	
COMPONENT II - STRENGTHENING OF FINANCIAL SECTOR RESILIENCE AND DEVELOPMENT OF CAPITAL MARKETS FOR EFFICIENT FINANCING OF THE ECONOMY					
II.1. Financial Sector Governance					
Adoption of international standards in the fight against illicit financing	Submission to the FATF of the CTAF report on the status of the Action Plan drawn up with FATF and confirming implementation of all the actions	Listing of Tunisia in the FATF observation list	Report on the implementation of the action plan for exit of the FATF observation list is submitted before the end of 2019	CTAF	
	Publication of the law on the fight against terrorism and suppression of money laundering	Legislation requiring revision to incorporate FATF recommendations	Law published before end 2019		
Modernisation of the legal and regulatory framework governing the insurance sector	Forwarding by the Minister of Finance to the Council of Ministers of the draft law on the Insurance Code	Current law does not allow the development of the sector in particular, life insurance and structurally loss-making risk insurance activities	Insurance Code forwarded to the Council of Ministers before the end of 2019	MoF	
Strengthening banking sector resilience	Publication of the law on the policy of waiving outstanding receivables, in order to improve the situation and reduce the rate of outstanding receivables	Current code of waiver of receivables very restrictive and requiring the maintenance of non-recoverable debts on banks' balance sheets	Law is published before the end of the programme	MoF	
Strengthening the integrity of public banks' procurement systems	Separation between the procurement commission and the commission in charge of complaints from bidders at the level of public banks	No separation between the procurement commission and the commission in charge of complaints from bidders at the level of public banks	Launch of the work to separate the commissions	MoF	
II.2 Deepening of Financial Markets					
Deepening and improving the efficiency of the public debt market and the efficient management of public debt	Submission by the DGDPP to the Minister of Finance of the draft law establishing the Tunisia Debt Management Office	No centralized and dynamic management of public debt	The draft law is submitted before the end of 2019	MoF	

	Facilitating access to SME financing via the capital market	Publication of amendments to the Stock Exchange General Regulations relating to the restructuring of the regulatory framework for the Alternative Market	Lack of dynamism in the alternative market	Greater access to the equity market for SMEs	CMF	
	Mobilizing savings and boosting capital markets	Publication of the decree on monetary SICAVs	No decree on monetary SICAVs	Decree published before programme end	MoF	
	Key Activities - Signing of the loan agreement and fulfilment of the conditions agreed during appraisal. Implementation of reforms selected				Financing: AfDB Loan: EUR 120 million	

I. INTRODUCTION: THE PROPOSAL

1.1. **Management hereby submits the proposal for a EUR 120 million loan to the Republic of Tunisia to finance the Financial Sector Modernisation Support Programme II (PAMSFI II).** PAMSFI II will be implemented over the period 2018-19, and aims to accelerate the modernisation of the Tunisian financial sector through the implementation of new generation reforms. This sector is a priority focus of the Tunisian authorities' reform programme, as described in the 2016-2020 Strategic Development Plan (SDP), aimed at implementing a new development model that will position Tunisia on a new path of more inclusive and job-creating growth. PAMSFI II contributes to the objectives of financing agriculture, industrialisation and improving the quality of life of the population within the framework of the Bank's High 5 Priorities. PAMSFI II should be an opportunity for the Bank to initiate a liquidity programme for commercial banks and leasing institutions, to meet the challenge of liquidity shortage in the Tunisian financial system and to strengthen the financial base of financial institutions. The actions of this programme are consistent with the efforts of the Central Bank of Tunisia (BCT) to contain the volume of refinancing of banks, promote de-cashing and Fintech, and guarantee financial stability.

1.2. **PAMSFI II is a continuation of PAMSFI I, which has been satisfactorily implemented. Even if the two operations are separate, they maintain the same objectives and components through the selected measures.** It should be noted that the political context in Tunisia was unstable, with three governments alternating between 2016 and 2018. In addition, the Bank's financial exposure in Tunisia created a financing constraint in 2018. To this end, it has been difficult to implement a fully programme-based approach. It has been more appropriate to set up interventions in successive phases over two years to take into account the political dynamics of this emerging democracy, while maintaining sustained dialogue on the financial sector. This is in line with the Bank's policy on programme-based support operations considering this type of intervention.

1.3. **The option of budget support to be disbursed in a single tranche is justified by two major considerations.** First, it will provide the Government with the necessary resources to maintain its reform efforts in the sector in a context of significant financing needs. Second, it will help to lower transaction costs for Tunisia and for the Bank, while guaranteeing the country's commitment by using a considerable number of reform measures prior to Board presentation. The choice of the sector budget support instrument is justified by the size of the authorities' reform programme in the financial sector and its crucial role in economic recovery. From this point of view, the programme has a crosscutting dimension, providing support for Tunisia's other priority reforms. It will contribute, through better financing of the economy, to supporting growth and improving the macroeconomic framework; it will also help to improve the business climate by facilitating access to financial services. It will in addition support reforms related to social protection by fostering the financial inclusion of the most vulnerable social groups.

II. COUNTRY CONTEXT

2.1. *Political Situation and Governance Context*

2.1.1. Tunisia's successful and peaceful political transition was widely hailed by the international community and earned it the Nobel Peace Prize in April 2015. The main stages of this transition were the adoption of a new Constitution in 2014, the holding of transparent parliamentary and presidential elections in October and December 2014, the establishment of the Assembly of the Representatives of the People (ARP) and the formation of a coalition government since early 2015. It should be noted that the country organized in 2018 the first municipal elections since 2011.

2.1.2. **The current government's efforts have focused on achieving the priorities set out in the Carthage Pact**, in particular the fight against terrorism, stimulating economic growth and development, seeking balances in public finances, and implementing a specific policy for local authorities. Since August 2016, three government formations have succeeded each other.

2.1.3. **Regarding political and institutional governance, Tunisia has made remarkable progress since 2011.** Tunisia has improved its ranking on the Mo Ibrahim Index of African Governance, ranking 9th out of a total 54 countries in 2017. In terms of public management, it was ranked 7th in 2017. In March 2016, the country adopted an organic law on access to information, which represents a step forward with respect to transparency and accountability.

2.1.4. **The country, however, continues to face significant economic governance challenges.** Transparency International's latest ranking (2017) on corruption perception ranks Tunisia 74th out of 180 countries, slightly higher than the previous year. Nevertheless, Tunisia is continuing its institutional progress following the adoption by the ARP, on 17 July 2018, of Law No. 2018-82 on the declaration of assets and the fight against illicit enrichment. This law is a tool to help the State to fight corruption and to enshrine the principles of transparency and integrity. As at 31 Dec 2018, 119,000 people had made their declarations within the regulatory deadlines, which was a success.

2.2. Recent Economic Developments, Macroeconomic and Fiscal Analysis

2.2.1. **Real growth in the Tunisian economy remains moderate with an upward trend.** It has reached 2.5% in 2018 compared to 2% in 2017, it is projected to reach 3,1% in 2019.¹ This growth is mainly driven by the agriculture sector, with a bumper harvest, and tourism, which has also generated a spillover effect on other sectors such as air transport, telecoms, agriculture, and crafts.

2.2.2. **Inflation remains relatively high.** It has reached 7.3% in 2018 compared to 5.3% in 2017; and is projected at 7% in 2019. However, inflation is under control below the initial forecast of 7,8% in 2018, resulting from a tightening of monetary policy marked by an increase in the key interest rate on the BCT and a deceleration in food price inflation. It should be noted that between 2017 and 2018, the Tunisian economy faced an unexpected supply shock following the rise in global energy prices. The energy bill has weighed heavily on energy subsidy spending and has put pressure on the value of the dinar against the dollar and the Euro. This context has led to an acceleration of inflation and has fuelled wages demands.

2.2.3. **Tunisia's external position has improved but remains fragile.** The current account deficit has reached 9.5% of GDP in 2018 compared to 10.3% in 2017. It is projected at 8.9% in 2019 thanks to improved control of the trade deficit.

2.2.4. **Fiscal consolidation is improving while recording cyclical difficulties due in particular to the rise in oil prices.** The budget deficit has reached 4.9% of GDP in 2018 compared to 6.1% in 2017 and projected at 3.9% in 2019. Tax revenue has increased relatively from 21.8% of GDP in 2017 to 23,1% of GDP in 2018 and could reach 23.2% in 2019, thanks to improved collection. Operating expenditure increased from 22% of GDP in 2017 to 22.3 in 2018; and is projected to reach 21.6% in 2019.² The share of investment expenditure in total expenditure fell slightly from 16.7% in 2017 to 15.7% in 2018 and is projected to reach 15.05% in 2019.

2.2.5. **The public debt stock continues to grow but remains at a sustainable level.** It rose from 62.42% of GDP in 2016 to 70.35% in 2017. The domestic public debt stock fell significantly from 21.78% of GDP in 2016 to 21.9% in 2017. The external public debt stock

¹ African Economic Outlook (2019), International Monetary Fund, October 2018

² Economic budget 2019, MDICI

remains on an upward trend: at 40.65% of GDP in 2016 and then 48.45% in 2017, with 50.59% expected in 2018. This increase reinforced the dominance of external debt, which accounted for 70.6% of public debt in 2018.

2.2.6. The various satisfactory reviews of the IMF programme and the related disbursements indicate that the country is on a positive macroeconomic path. The economic downturn and delays in the implementation of structural reforms have led to significant macroeconomic imbalances. Their scale has compelled the Tunisian authorities to request IMF support. A first programme of USD 1.73 billion was signed in June 2013 and closed in December 2015, and a second US\$ 2.9 billion program was signed in May 2016. The IMF and the Tunisian authorities reached an agreement on 17 April 2019 on the fifth review of the economic reform programme under the Extended Fund Facility arrangement.

Table 1 Key Macroeconomic Indicators

	2016	2017	2018(e)	2019(e)	2020(e)	2021(e)	2022(e)	2023(e)
Real GDP Growth (%)	1.1	2.0	2.6	3.1	3.4	3.6	4.0	4.0
Inflation (period average, %)	3.7	5.3	7.3	7.0	5.7	5.2	4.5	4.0
Current deficit in % of GDP	-8.8	-10.2	-9.7	-8.5	-7.8	-7.0	-6.5	-6.0
Net Foreign Direct Investment (USD, million)	695	810	742	936	--	--	--	--
Official Reserves (USD, billion)	5.9	5.9	6.3	7.3	7.8	8.0	8.9	9.5
Official Reserves (months of imports)	3.6	3.3	3.4	3.8	4.0	4.0	4.3	4.6
Revenue in % of GDP	21.2	24.2	24.9	25.7	25.8	25.9	25.9	26.1
Budget deficit excl. grants in % of GDP	-5.9	-5.9	-5.2	-3.7	-2.5	-2.2	-2.2	-2.2
Central government debt in % of GDP	62.3	70.3	72.0	71.8	70.8	69.8	68.0	66.7
External debt in % of GDP	68.8	82.6	89.4	91.7	93.0	91.6	90.2	88.7
Credit to the economy (% of change)	9.7	12.7	10.1	6.9	7.0	7.1	7.4	7.0

Source: MDICI (for actual data) and International Monetary Fund (for projections), October 2018

2.3. Competitiveness of the Economy

2.3.1. The delays observed in implementing structural reforms and the difficult security and social context have negatively affected Tunisia's competitiveness. The country has dropped several places in international rankings since 2011, such as the *Doing Business* ranking where Tunisia, in 2019, occupies the 80th position, by gaining eight spots compared to *Doing Business 2018*, without however regaining the 45th rank it occupied in 2011. The country is also heavily dependent on Europe, which accounts for 70% of its trade and has experienced declining productivity since 2011. Similarly, despite a degree of sophistication of Tunisian exports over the past two decades, this complexity remains **insufficient to ensure strong, resilient and inclusive growth.**

2.3.2. The problems of access to financing and constraining labour market regulations represent the main constraints to growth and private investment in Tunisia³. However, Tunisia has many assets and factors of resilience. Its advantages include an open and fairly diversified economy, a level of human development above the average for the MENA region (0.7 for Tunisia compared to 0.64 for the MENA region), infrastructure quality which meets the current needs of the economy and a strategic geographic location.

2.4. Public Finance Management

2.4.1. According to the most recent public finance management assessment reviews (PEFA 2015), the Tunisian national public finance management system allows for acceptable preparation and execution of the annual budget and has an adequate mechanism for internal expenditure control and verification. Multi-year budget planning has been consolidated since

³ Results of a growth diagnosis carried out using the HRV method. AfDB 2013 Report and IMF Country Report N.16/47, February 2016.

2015 through the preparation of a development plan complete with a medium-term expenditure framework. However, priority areas of intervention remain, in particular: (i) the streamlining of internal control bodies; (ii) modernization of the accounting system and its convergence towards international standards; (iii) reduction of the timeframes for accounts the presentation of accounts; and (iv) strengthening of judicial control. In the wake of the revolution, Tunisia embarked upon comprehensive public finance management (PFM) reforms. In January 2019, the ARP adopted the Organic Budget Law (LOB), which provides for budgeting based on equal opportunities for men and women, and equality between the various social groups.

2.5. Inclusive Growth, Poverty Situation and Social Context

2.5.1. Eight years after the revolution, Tunisia is still faced with wide regional disparities and the problem of unemployment, the main factors of fragility that triggered the 2011 revolution. The employment situation remains a challenge for the country. After peaking at 18.9% in 2011, the unemployment rate levelled off at 15% since 2013. At the end of 2017, the level of unemployment remained high. There were 618,000 unemployed, or 15.4% of the estimated working population of four million people. Unemployment is almost twice as high for women (22.6%) as for men (12.5%). Unemployment among higher education graduates (28.6%) remains a concern and the current level of economic growth does not absorb the approximately 60,000 new higher education graduates entering the labour market each year.

2.5.2. The Tunisian authorities have made significant efforts to reduce poverty and inequalities but weaknesses remain. The 2019 budget provides for social measures consisting of: (i) improving the quality of educational services by strengthening human resources and infrastructure; (ii) strengthening human and material resources to improve the quality of health services and consolidating strategic stocks of medicines; (iii) operationalizing the public health support fund; (iv) increasing the tax allowance on the value of housing built by property developers, by exempting registry fees; (v) extending the scope of consumer tax exemption for cars used by persons with disabilities. Similarly, the government has increased by 35,000 the number of beneficiaries of the National Assistance Programme for Vulnerable Assistance Families (PNAFN) to a total of 285,000 families by 2019. The government also decided to increase the welfare allowance amount. Lastly, it should be noted that in 2019, the organic law on the creation of the "Social Amen" program for the promotion of poor and low-income social categories was adopted.

2.5.3. Regarding gender equity, the 1956 Personal Status Code places Tunisia at the vanguard of the Arab world with regard to women's situation in society. However, from standpoint of economic inclusion and human capital, and despite efforts made, some disparities persist. At the level of basic education, the illiteracy rate in 2014 was 25.6% for girls against 12.8% for boys.

2.6. Financial System, Constraints and Challenges

2.6.1. In spite of the reforms achieved to-date in the Tunisian financial sector, major challenges remain, which must be tackled in order for the sector to play its expected role in financing the economy and in fostering the economic inclusion of the most disadvantaged segments of the population (Technical Annex 4). With bank credit provided to the private sector representing 85.6% of GDP in 2018, the Tunisian banking sector is recording a significant performance, relative to the Maghreb countries. However, this sector is expected to increase its contribution to the financing of the productive fabric and to successfully provide banking services to low-income people.

2.6.2. The banking sector is characterized by a triple paradox. First, the banking landscape comprises a fairly high number of banking institutions (23 in 2018). Second, despite the lack of competition, the sector's average profitability is low, particularly reflecting

weaknesses in the management of some institutions' operating costs, in particular those of public banks. It should be noted that the share of credit to the private sector in Tunisia is relatively the highest (81% of total credit against 65% in Morocco and 75% in Jordan)⁴. However, surveys point out that even though the majority of businesses have outstanding bank credit, they consider access to financing to be a major constraint to their expansion. **Another challenge of the Tunisian banking system is its structurally very high rate of non-performing loans, which reached 13.9% in 2017.** It stood at 12% before the revolution (15% at the end of 2013), significantly higher than that of Morocco (5%) and Jordan (8.5%). These non-performing loans are a sign of shortcomings in the mechanism and conditions of credit allocation. However, it is important to note that the authorities are making significant efforts to address these deficiencies, in particular through consolidation of the banking sector, improvement of the guarantee mechanism and diversification of financing instruments, particularly in the regions. These efforts shall be the subject of support measures agreed upon under this programme. Another major constraint for the Tunisian banking sector is the liquidity shortage it faces.

2.6.3. Financial inclusion weaknesses also limit the economic opportunities available to vulnerable and rural segments of the population and rural communities allowing them to emerge from unemployment through entrepreneurship and self-employment. Adults reporting to have a bank account represent 27%. This average masks gender disparities: 20.7% of women have an account compared to 34.3% of men. Financial exclusion is more pronounced in rural areas, with only 22.4% of adults holding an account in a formal institution. This limited access to financial services is a barrier to investment, particularly for small businesses. Moreover, formal savings collection remains low (18.3% of GDP in 2017), although it is higher in the Maghreb region and the Arab world. Banks are struggling to collect national savings and significantly improve the level of financial inclusion of Tunisians. Yet saving is the basic financial service for people in precarious situations and the driving force behind financial inclusion.

2.6.4. Regarding financial stability, it should be noted that Tunisia faces a major challenge in reducing the overall refinancing volume of banks, which reached a record level of TND 16 billion in August 2018. In fact, banks face a chronic and structural liquidity problem related to autonomous liquidity factors, including net foreign currency assets. These fell, particularly due to the widening energy balance deficit⁵, lower tourism revenue and falling phosphate sales. The other important dimension that has negatively affected bank liquidity is the massive use of cash in transactions.

2.6.5. There are shortcomings in payment infrastructure. There are two payment platforms, the Post Office (e-Dinar) and the banks, where interoperability is partial. In this context, telephone operators have had to duplicate their mobile financial service offers in order to provide their customers with products that have greater interoperability between the Post Office's ecosystems and banks. In April 2018, however, the Tunisian Post announced that it had established a switch between its platform and that of Société Monétique Tunisie in order to achieve greater compatibility between the country's two major payment platforms. This development was closely monitored as part of dialogue under PAMSFI, given that the national switch was a precondition.

2.6.6. Historically, the Government has always followed a policy encouraging investment capital activities based on fiscal incentives, but the sector remains underdeveloped. Since the revolution, real progress has been made in the sector, fostered in

⁴ Figures relate to the year 2017, source : <https://donnees.banquemondiale.org/indicateur/fs.ast.prvt.gd.zs>

⁵ As a result of the combination of several effects: a decrease in local oil production, the increase in domestic energy consumption and the rise in the oil price per barrel during the years 2012, 2013, 2017 and 2018.

particular by the adoption of the 2011 Decree-Law. The private equity sector is dominated by banks: the latter provided more than 60% of the capital raised in 2017 and SICARs and FCPRs (S&Fs) account for about 2/3 of the investments made in terms of approval amounts. The contribution of venture capital to the financing of private investment remains very limited with a strong focus on development capital activity⁶. This limited increase mainly reflects the rigidity of the regulations governing the sector.

2.6.7. The insurance sector is also poorly developed in Tunisia with a volume of policies equivalent to 2.2% of GDP at end-2017 against 1.9% in 2015, despite a fairly high number of actors (22 companies) mainly concentrated in mandatory non-life insurance activities (Technical Annex 15). Although Tunisia posted an average annual growth rate of collected premiums of 10.2% between 2013 and 2017, the sector is still below its potential. The insurance density (average premium per capita), which is around TND 182, remains low compared to other emerging economies. Analysis of the situation highlights the following main observations: (i) Tunisian insurance does not make use of the immense existing potential, (ii) the automobile sub-sector dominates and is loss-making, (iii) mandatory insurance is not complied with, (iv) life insurance is poorly developed and (v) regulation is inadequate.

2.6.8. Despite positive progress, capital markets do not fully play their role as a financing force for the Tunisian economy⁷ (Technical Annexes 12 and 13). The contribution of the financial market to the financing of gross fixed capital formation in the private sector has been established at 8% in 2018. The Tunisian financial market is aligned with international standards, has advanced technical structure and expertise in financial engineering. Despite the delay in the substantial revision of the 1994 law governing the Tunisian financial market, stakeholders have broadened the listing of the Tunis Stock Exchange (BVMT) and improved financial literacy. The Tunindex index recorded a performance of 15.76% in 2018 compared to 14.45% in 2017. However, the equity market does not contribute enough to the financing of long-term investments and has limited participation by institutional investors, depriving the economy of significant financing resources. Lastly, the alternative market created to attract SMEs is still very unattractive. The alternative market could be improved by stronger requirements for the quality of financial information. Also noteworthy is the need for new products to mobilize private and institutional savings. The sovereign debt market meets the minimum size requirements for inclusion in global indices, but remains narrow and lacks liquidity. The authorities' efforts to deepen this market, improve its efficiency and promote efficient public debt management need to be continued. In particular, the Bank had supported the establishment of specifications for Primary Dealers (SVTs) and engaged dialogue with the authorities as part of the work to create a yield curve and set up a Tunisia Debt Management Office.

2.6.9. In view of the elements presented, the Tunisian financial sector could play a much more important role in financing the economy and in providing support for greater inclusiveness in the country if the necessary reforms are implemented.

III. GOVERNMENT'S DEVELOPMENT AGENDA

3.1. Government's Medium-Term Development Strategy and Reform Priorities

3.1.1. The reform of the Tunisian financial sector is of major importance in the National Reform Programme 2016-2020. Improving the financing of the economy is one of the 5 pillars of the National Major Reforms Programme. The components identified for this pillar are: (i) improving the regulatory and governance framework, (ii) strengthening banking supervision,

⁶ However, this rate is above the average for the MENA region.

⁷ Summary diagnosis of the financial sector in Tunisia: Review of the current situation, main challenges and opportunities for reform (June 2014).

(iii) strengthening the resilience of the banking sector, (iv) improving financial inclusion, (v) improving access to finance for microenterprises, SMEs, innovative risk enterprises, and (vi) deepening the capital market.

3.1.2. The Government's strategy is described in a guidance note published in August 2015, which provides the basis for the 2016-2020 Strategic Development Plan approved by Parliament. This note underscores the need for the country to implement a new development model that will place Tunisia on a new, more inclusive and job-creating growth trajectory. To achieve these objectives, the following five strategic thrusts were retained: (i) improved efficiency of central government and public institutions through good governance; (ii) economic diversification through a favourable business climate and improved access to financing; (iii) stronger human development and social inclusion; (iv) development of the regions by accelerating public investment in order to develop adequate infrastructure and improve access to financing; and (v) a green economy to ensure the sustainability of the growth generated. Obviously, the achievement of the objectives described in the guidance note and sector reform strategies will depend on Tunisia's ability to mobilise the appropriate financial and technical resources.

3.1.3. Tunisia's technical and financial partners are providing sustained support to Tunisia to help the country implement its strategy, address the challenges that are blocking growth and speed up the implementation of priority reforms. The IMF is more focused on supporting public finance balances and macroeconomic consolidation, the World Bank supports improvement of the business climate, while the European Union provides substantial support for social protection. Bilateral partners also supplement this support through programmes to reform technical assistance and investment projects. The Bank's intervention through the financial sector aims to meet the challenge of financing the economy, but also to provide responses, in a cross-cutting manner, to other priority reform areas, such as macroeconomic consolidation (de-cashing to facilitate the mobilisation of domestic revenues), the investment climate (guarantees, innovation financing) and the strengthening of social safety nets (financial inclusion).

3.2. Obstacles to Implementing the Strategic Development Plan

3.2.1. Overall, the investment allocation retained for the plan covering the period 2016-2020 (120000 million TND) seems insufficient and does not make it possible to raise the investment rate to levels that would help to meet, or at least mitigate, social challenges. Investment in the agricultural and manufacturing sectors appears inadequate and does not help to consolidate the country's economic base and its export potential, which is struggling to turn around⁸. Recurrent changes in government formations doesn't favour the conditions for wide appropriation of the reform program and optimal management of the implementation of the planned measures.

3.3. Consultation and Participation Process

3.3.1. To strengthen ownership of the reforms, it will be necessary to establish consultation and participation frameworks expanded to all citizens. In a bid to find solutions to the regional disparities and expectations of young people, women and other vulnerable groups, the Government has mainstreamed these dimensions in its strategic orientations, reflected in the SDP 2016-2020, which was implemented using a participatory process involving 292 regional and local committees.

3.3.2. As regards PAMSFI II, it should be noted that during the preparation and appraisal missions, more than 30 working sessions were held with the Tunisian authorities and other stakeholders in the Tunisian financial sector in order to identify major reforms likely to meet

⁸ Plan de développement 2016-2020 : « Réformes, investissements, commerce extérieur et emploi. Une lecture critique, 2016, Solidar-Tunisie

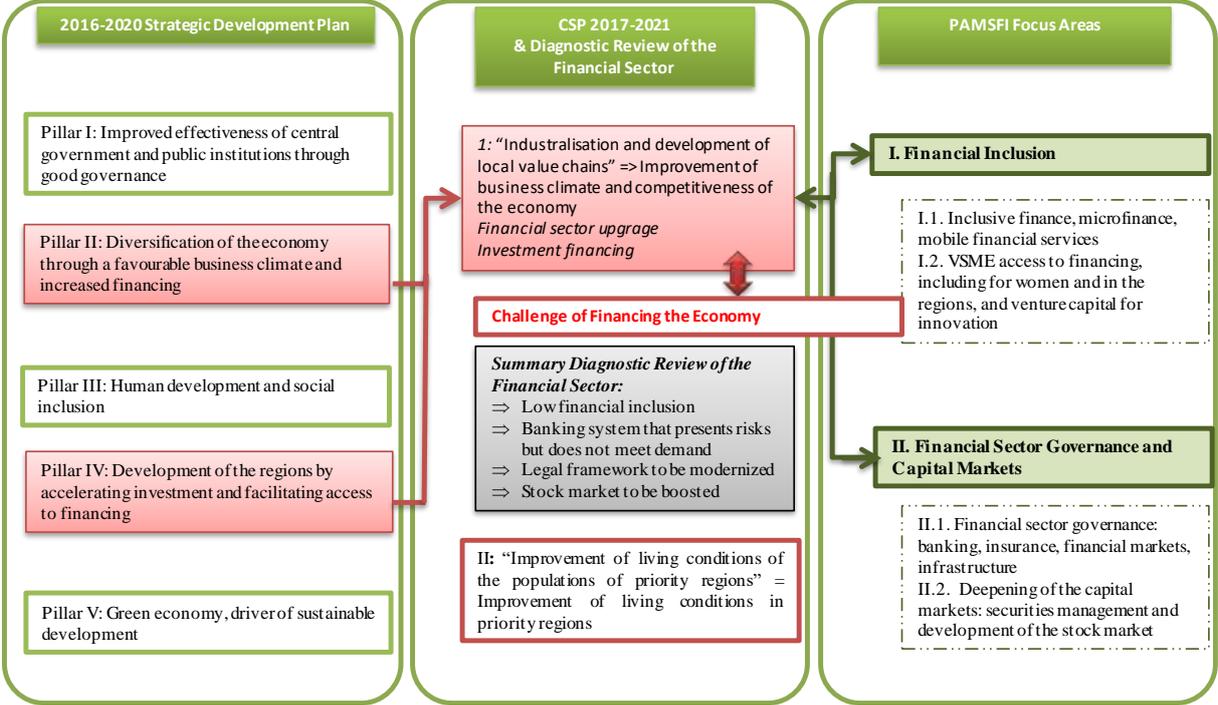
the challenges of the sector as a whole and consolidate the achievements of PAMSFI I (2016-2017). The proposed programme was prepared after broad-based consultations with key financial sector actors. The Bank engaged in dialogue not only with the authorities but also with banking sector operators, the stock exchange as well as professional insurance associations, private equity investors and microfinance institutions. This approach was adopted to garner the views of the different stakeholders on the constraints to the development of the Tunisian financial sector and to assess the relevance of the measures agreed upon with the authorities within the context of this operation. The Bank has also enriched the design of this programme with the outcomes of PAMSFI I and the conclusions of workshops organized by the profession over the past two years.

IV. BANK SUPPORT TO THE GOVERNMENT STRATEGY

4.1. Linkage with the Bank's Strategy

4.1.1. **The Programme will contribute to the objectives of financing industrialization, improving the population’s quality of life and agriculture in the context of the High 5 Priorities.** It is aligned with the Country Strategy Paper 2017-2021, the first pillar of which, "Industrialisation and development of value chains", focuses on policies and reforms to reduce the cost of production factors and strengthen the competitiveness of financial services. The programme is also aligned with the second pillar "Improving the quality of life of populations in priority regions" by supporting the development of micro, small and medium-sized enterprises (MSMEs) through improved access to financial services. It is also aligned with the two pillars of the Bank's Financial Sector Development Policy Paper and Strategy 2014-2019, which focus on increasing access to financing for partially served and unserved populations; and on expanding and deepening financial systems. The Bank’s assistance is justified by the need to support the priority reforms of the banking sector embarked upon by the Government with a view to achieving the structural transformation of the economy. In addition, PAMSFI II represents a key activity planned in the Bank's CSP. The financial sector emerges as a common driver for the two pillars of the CSP (1. Industrialisation and Development of Value Chains; 2. Improvement of the quality of life of the populations in the priority regions).

**Table 2
Linkages between the PND, CSP and PAMSFI II**



4.2. Meeting the Eligibility Criteria

4.2.1. Tunisia meets the eligibility criteria for Sector Budget Support (SBS)

Criterion 1. Macro-economic Stability: Despite these difficulties in the transition phase, Tunisia's macro-economic outlook in the medium term remains positive. The country has a stable and sustained macroeconomic framework. It is continuing its programme with the IMF, supported by the IMF's Extended Credit Facility (ECF) Instrument, approved in 2016, in a satisfactory manner. In addition, the Government undertook, in the 2019 Finance Law, to reduce the budget deficit to 3.9% of GDP and to reduce the public debt ratio in the medium term. Such a prospect should make it possible to control inflation in the medium term and preserve the purchasing power of citizens.

Criterion 2. Political Stability: Tunisia has undergone a successful transition, in particular with the adoption of a new constitution laying the foundations for multi-party democracy and is working to establish independent constitutional bodies such as the Constitutional Court.

Criterion 3: Harmonization with Partners: By way of coordination mechanisms, it should be noted that the various donors supporting Tunisia meet periodically within the framework of thematic working groups to review the problems of the sector, share financial information on their operations, and identify synergies. This coordination was strengthened within the framework of CwA.

Criterion 4. Fiduciary Framework: Tunisia's fiduciary risk assessment was conducted under the 2017-21 CSP on the basis of the most recent PFM assessment (PEFA 2015,) concluded that the risk level is moderate. It follows that the Tunisian public finance management system allows for acceptable preparation and execution of the annual budget and has an adequate mechanism for internal expenditure control and verification.

Criterion 5. Commitment to a Poverty Reduction Strategy: Tunisia has made remarkable progress in poverty reduction and improved access to services (water, sanitation and hygiene) in recent decades. Between 1990 and 2012, access to an improved drinking water source increased from 82% to 97% of the population and this rate rose from 73% to 92% for improved sanitation. More than four million people were able to access improved sanitation between 1990 and 2015, and the same is true for water. Poverty has decreased across Tunisia in recent decades, but its distribution remains uneven. According to recent government estimates, the poverty rate fell from 25% in 2000 to 15% in 2015 and the number of the poor was estimated at 1.7 million people in 2015.

4.3. Collaboration and Coordination with Other Partners.

4.3.1. **The Bank's proposed intervention is part of the donor coordination for implementation of the G20 Compact with Africa (CwA).** As part of coordination, it should be noted that TFPs meet periodically within the framework of thematic working groups to review the problems of the sector, share financial information on their operations, and identify synergies. Thus, the Bank is in continuous dialogue with Tunisia's main TFPs to ensure that interventions are complementary. The measures identified following the preparation mission are complementary to ongoing and planned interventions by TFPs in the financial sector, in particular the World Bank, the International Monetary Fund (IMF), the French Development Agency (AFD), the European Bank for Reconstruction and Development (EBRD), the German Development Bank (KfW) and the European Union (EU).

Box - Tunisia within the Compact with Africa Framework

Tunisia is a key country of the Compact with Africa: an emerging democracy, strategically located in the southern Mediterranean (at the crossroads of major trade and market entry corridors), aiming to create a favourable business climate (key reforms: PPPs, competition, banking sector reforms, ICT deregulation and adequate infrastructure).

The CwA was at the heart of the African Investment Forum (AIF), where Tunisia reflected its experience with the CwA, showcasing to investors a country open for business.

The Bank plays a key role in CwA coordination.

- Streamlining of the approach and thematic groups,
- Mobilisation of technical assistance in support of CwA reforms (PPP, Investia PME, BDR);
- Support to CwA reforms: the Government prioritizes compact actions that focus on strengthening macroeconomic stabilization and stimulating inclusive and sustainable growth. The Bank intervenes in three CwA thrusts (i) Macroeconomic framework; (ii) Business climate and (iii) Financing framework. PAMSFI provides a concrete response to pillar 3 on financing, while contributing to the other two pillars

4.4. Linkages with other Bank Operations

4.4.1. As of 1 January 2019, the active portfolio amounted to nearly EUR 1.2 billion, and included 43 operations, of which 29 were in the public sector (including 11 operations financed by the Technical Assistance Fund for Middle Income Countries), 4 in the private sector, and 14 operations financed by the Transition Support Fund and the MENA Transition Fund (TFT MENA). In addition to lending operations, these technical assistance operations aim to speed up economic diversification, industrialisation, value chain development, public enterprise governance and address the country's priority reform issues. Public sector commitments amount to UA 1,060 million or 91% of the overall portfolio. The private sector, with commitments of UA 93.3 million, accounts for 8.2% of the portfolio, while technical assistance grants (TFT/MENA), with a total amount of UA 8.18 million, represent 0.8% of the total amount of commitments. The sector breakdown of the portfolio was as follows: transport (46.8%), water and sanitation (16.3%), social (13.5%), financial sector (8.2%), agriculture (6.1%), industry/digital (5.4%), energy (3.6%), and multi-sector (0.1%). The overall portfolio disbursement rate is 70%. Overall, the performance of the Bank's portfolio in Tunisia made a qualitative leap during the second quarter of 2018 and is now among the Bank's best performers.

4.4.2. **PAMSFI II is a continuation of PAMSFI I, consolidating the achievements of the first phase.** It aims to create the necessary conditions for accelerated, climate change-resilient, low-carbon and inclusive economic growth in Tunisia. By improving access by the population and businesses to financial services, diversifying the latter and improving the stability of the financial system, the Programme will help to address the main challenges facing Tunisia, namely weak growth, high unemployment and wide regional and social disparities. It is estimated that an increase of 10 percentage points in Tunisian financing to the economy would help to raise USD 19 billion that would benefit investment and job creation. This Programme will supplement the Inclusive Regional Development Support Programme, which was approved in 2017. The latter aims to remove constraints on public and private investment in the most disadvantaged regions, improve the business climate and governance in these regions and the employability of young graduates. For its part, PAMSFI II aims to improve the offer of financing, including in disadvantaged regions, for young entrepreneurs and SMEs, in order to stimulate job creation likely to benefit these unemployed graduates and disadvantaged regions. The results of PAMSFI I combined with the measures envisaged in PAMSFI II will also allow to create synergies with the Bank's other operations, including lines of credit and infrastructure strengthening for the benefit of economic operators.

4.4.3. **Linkages with Technical Assistance Projects:** The programme benefited from a strong leverage effect through its linkage with technical assistance operations aimed at: (i) improving SME financing through the Bank's support to the SME Financing Bank (BFPME); (ii) providing support to improving the performance of primary dealers for the debt market; and

(iii) conducting the study on the BTS/MCA financing mechanism, which has benefited the Tunisian Solidarity Bank.

4.4.4. Lessons Learnt from Previous Operations: Since the 2011 revolution, the Bank has financed three policy-based operations in support of democratic transition and growth recovery in Tunisia. The completion reports on these programmes concluded that the country's implementation performance and degree of ownership of the reforms were satisfactory. Consequently, the main lessons learned include the need to allocate adequate time to monitoring the maturing of the reform measures, in particular those presenting potential social and political risks during their implementation. PAMSFI's design has taken these main lessons into account, especially by maintaining the programme over two years (2016 – 2017 and 2019 - 2020). Furthermore, the outcomes and lessons learned from implementing certain reforms supported by the previous programmes informed the design of PAMSFI measures as reflected in Table 3.

Table 3- Lessons Learned from the Bank's Previous Operations

Key lessons learned	Measures taken to reflect lessons in the programme
The need to support the government through technical assistance in the form of budget support	Identify certain measures that could be the subject of technical assistance, such as the preparation and operationalization of the strategic plan of the Central Bank of Tunisia or the establishment of the debt agency.
The difficulty of verifying the large number of measures and indicators in the logical framework arises for the quantified indicators of the short-term programme.	Take some relevant indicators in consultation with the authorities

4.5. Analytical Work Underpinning the Operation

4.5.1. The programme design tapped from several studies and reports prepared by the Bank and other partners. The Growth Diagnostic for Tunisia undertaken by the Bank: Towards a New Economic Model for Tunisia (2013) highlighted the main constraints to investment in Tunisia, including financing difficulties. The Summary of the Diagnostic Review of the Financial Sector carried out by the Bank and World Bank in 2014, also reveals the weaknesses of each of the financial sector components and proposes recommendations for reforms. The Tunisian authorities' survey on financial inclusion published on 18 December 2018 made it possible to take stock of the situation regarding access to financial services for Tunisians. The programme has also benefited from the diagnostic review of capital markets for Tunisia conducted by the Bank and its development partners in the context of the Deauville Initiative and the Arab Debt Market Development Initiative. The programme also drew on the feasibility study on the intermediation of microfinance institutions on behalf of commercial banks and the Tunisian Post Office in the collection of savings published in 2018; conducted as part of the MicroMED programme. It should also be noted that PAMSFI benefited from the conclusions of research papers produced by the Bank⁹.

V. THE PROPOSED PROGRAMME

5.1. Programme Goal and Objective

5.1.1. The proposed operation is in line with the Bank's strong commitment to support the Tunisian Government in the implementation of its general policy vision as set out in the 2016-2020 Strategic Development Plan and in the consolidation of PAMSFI's achievements by pursuing reforms undertaken to improve financial inclusion and to strengthen financial sector development. PAMSFI II thus maintains PAMSFI I's goal to help create the necessary conditions for accelerated,

⁹ Publication on Financial Inclusion in Africa and the working paper on the impact of credit bureaux and registries on SME access to financing.

climate change-resilient, low-carbon and inclusive economic growth by strengthening the financial sector's role in the financing of the economy and vulnerable segments of the population. The banking system is the central pillar of the financial sector strategy. It must fully and effectively play its dual role: (i) intermediation between depositors and borrowers; and (ii) provision of financial services to all economic sectors and strata of the Tunisian society. The banking system must be sound, solid and credible. The other segments of the financial sector, capital markets, insurance and micro-finance must play a role in meeting the demand for loanable funds.

5.1.2. **Thus, the relevance of the Bank's planned intervention in support of Tunisian authorities remains and is justified by the need to continue supporting priority reforms of the financial sector embarked upon by the Government with a view to achieving the structural transformation of the economy.** Indeed, PAMSFI II will help to support the emergence of a new development model for Tunisia in which the private sector can develop and create employment across the country and where disadvantaged segments of the population can contribute to, and benefit from, growth. In addition, Tunisia has engaged in ambitious programmes aimed at supporting SMEs and attracting private investments in the energy sector through the 1,000 MW Tunisian solar programme. PAMSFI II will support the ambitious objectives of this programme by helping to improve the economy's financing.

5.2. Programme Components

5.2.1. **PAMSFI II comprises two complementary components.** The first **component** aims at reducing social, territorial, regional and gender disparities through better financial inclusion. The second **component** aims at building the financial sector's resilience and developing capital markets to ensure efficient financing of the economy. The first component will comprise two sub-components. **Sub-component 1.1** - Improvement of the financial inclusion of vulnerable segments of the population with a gender perspective; and **Sub-component 1.2** - Improvement of access to financing for VSME. The second component will also include two sub-components, namely: **Sub-component 2.1** - Strengthening the Financial Sector Governance Framework; and **Sub-component 2.2** - Deepening of Capital Markets. The various programme-supported measures have been described in the Reform Matrix (see Annex 2).

5.2.2. **Under Component 1**, the improvement of financial inclusion will be achieved through the implementation of certain reform projects aimed, in particular, at developing responsible microfinance by increasing the offer, improving access and quality of financial products provided to vulnerable segments of the population. The improvement of access to financing for VSME will be carried out through reform projects aimed at improving access to financing for VSMEs in the regions, developing support and guarantee mechanisms for VSMEs, promoting private equity activity and financing innovation.

5.2.3. **Under Component 2**, the strengthening of financial sector governance will mainly hinge on the implementation of reforms aimed at accelerating the adoption of international standards on combatting illicit financing and money laundering, modernizing the insurance sector governance and strengthening the banking sector's resilience. The deepening of capital markets will be achieved through the implementation of reforms aimed at deepening the public securities market, facilitating access to SMEs financing by capital markets and diversifying product offer in order to mobilize private and institutional savings.

Component I – Reduction of Social and Regional Disparities through Better Financial Inclusion

Sub-component I.1 – Financial Inclusion

5.2.4. Problems and Constraints:

5.2.4.1. In Tunisia, the offer of inclusive financial services is more developed compared to other countries of the region thanks to the postal network. However, the offer is still less diversified. The

financial inclusion rate stood at 36% of the adult population in 2015. Recent efforts by the sector's players focused on certain types of microcredits without addressing the need for micro-savings, insurance and payment services. Various studies show a demand of from 950,000 to 1.4 million persons for microcredit, but an even greater demand of 2.5 to 3.5 million for a wider range of microfinance services, representing 30% to 40% of the adult population. It is estimated that between 245,000 and 425,000 micro and very small enterprises would need a specific range of services, representing 37% to 65% of enterprises listed in the National Business Register (RNE). The 2014 IFC study estimates that 15,000 SMEs have unmet financial needs. This is due to some inefficiencies inherent in the financial and legal system.

5.2.5. **Recent Measures Adopted by the Government:**

5.2.5.1 To improve the quality of life of the population and expand employment opportunities, in June 2018, the Tunisian authorities adopted the National Financial Inclusion Strategy (SNIF 2018-2022) and its governance model through the creation of a National Financial Inclusion Council. The development of a SNIF action plan to promote digital finance, the refinancing of MFIs, micro-insurance, and the solidarity and social economy. For the first time in Tunisia, a national survey on Financial Inclusion was launched in 2018. The survey results show that 9% of Tunisians are active clients of the financial system, including women (6%), rural people (5%) and people on income (3%). This reflects the financial exclusion of entire segments of the Tunisian population, the gap between urban and rural areas, and the predominance of the exclusive use of cash for daily financial transactions

5.2.6. **Programme Activity:** To address these challenges of improving financial inclusion, it was agreed under this programme to implement the following reform measures to promote financial inclusion: (i) publication of the Minister of Finance's Order on the doubling of the micro-credit ceiling granted by microfinance institutions; (ii) validation of the feasibility study on the establishment of a refinancing vehicle for microfinance institutions by the steering committee; (iii) transmission by the Minister of Finance of the draft decree setting out the administrative and financial penalties imposed by the Microfinance Supervisory Authority on MFIs, together with the opinion of the ACM Board of Directors to the Presidency of the Government; (iv) operationalization of phase 4 of the micro-credit risk register incorporating the APR and basic scoring; (v) launch of the digital payment product for the enrolment of public school students; (vi) launch of at least one digital financial product for State payments to citizens as part of the de-cashing strategy implementation; (vii) Approval by the Minister of Finance of the statute of the professional association of MFIs pursuant to Decree-Law 117; (viii) Signing of the agreement between FTUSA and the professional association of MFIs for the marketing of micro-insurance products; (ix) publication of the implementing decrees on the operationalization of the agricultural damage compensation fund for agricultural damage caused by natural disasters; and (x) publication of the Decree on the Real Estate Loan Guarantee Fund and signing of the agreement with SOTUGAR on guarantee products for real estate loans for irregular income earners.

5.2.7. **Expected Outcomes:** The implementation of these measures will enable the national financial inclusion strategy to achieve its objective of improving financial inclusion from 36% in 2015 to over 38% in 2020 and increasing the penetration rate of mobile financial services from 4% in 2017 to 10% by 2020; doubling of outstanding micro-credit amounts granted by microfinance institutions; and online (payment of related charges) registration of 100% of public school children.

Sub-Component I.2 - Financing of VSME

5.2.8. **Problems and Constraints:** The banking sector does not fully finance VSMEs. Bank are reluctant to loan to VSMEs due to the unprofitable nature of projects, the significant risk associated with asymmetric information and insufficient guarantees. On the part of VSMEs, the lack of cash flow is a crucial handicap when it comes to renewing the stock. Generally, VSMEs do not have current assets

and collateral to pledge as collateral. Secondly, the bank has little information on its customers even with the creation of a credit bureau. Lastly, banks are cautious because of problems related to recovering loans granted, the cumbersome nature of the legal system and the difficulty of making guarantees effective.

5.2.9. Recent Measures Adopted by the Government: To improve the financing of the productive fabric, the country's authorities have undertaken several reforms. Public banks have been restructured through recapitalization and governance reform. Financing in the regions and improvement of the guarantee system, especially for SMEs and young entrepreneurs, have been at the heart of the authorities' concerns. In this context, it was decided that a Bank of Regions be established and that the main mechanisms set up by the State be restructured to finance disadvantaged regions. The BDR institutional and operational model has been adopted where there are specific products for young project leaders who often lack sufficient guarantees. To improve the banks' risk-taking in the financing of enterprises, a relaxation of the framework for the annual percentage rate (APR) has been considered. In terms of venture capital, the exception made in the 2015 Finance Law (FL) at the level of the dedicated framework for making companies in difficulty eligible was extended until 2017 to meet the financing needs of these enterprises.

5.2.10. Programme Activities: The programme will support measures under this sub-component: (i) adoption by the Council of Ministers of the draft law establishing the Bank of the Regions; (ii) inclusion in the State Budget of TND 100 million to enable it subscribe to the capital of the Bank of the Regions; (iii) signing of the agreement between the Ministry of Finance and SOTUGAR, for the development of a guarantee product known as Dhamen Express guarantee product for SMEs; (iv) launch of the study on improving the management method of the National Guarantee Fund covering the agricultural and microfinance sectors; (v) Publication of the Decree establishing the SMEs Restructuring Fund and signing of the agreement between the Ministry of Finance and SOTUGAR for the financial restructuring guarantee product ; (vi) operationalization of SMEs Restructuring Fund through the validation of the first batch of diagnostic reports and proposals of an SMEs safeguard plan; (vii) publication of the three implementing instruments of the law governing collective procedures; (viii) adoption by the Council of Ministers of the Decree issued in application of the law on excessive interest rates for enterprises fixing the new margin; (ix) Finalization and transmission of the draft Crowdfunding Law to the Ministry of Industry and SMEs, and to the Presidency of the Government; (x) signing of the agreement between the Ministry of Finance, the Ministry of ICT and SOTUGAR for the Start-ups Guarantee Fund; and (xi) Establishment of a Public-Private Fund (Anava) for the financing of start-ups and its allocation by the State via the CDC up to 20% of the Fund's size.

5.2.11. Expected Outcomes: Implementation of the programme measures agreed under this sub-component should help to improve the ratio of credit to private enterprises as percentage of GDP from 83.8% of GDP in 2018 to 86% in 2020. Women and young entrepreneurs are expected to benefit from improved access to financing, as well as enterprises established in the country's interior regions.

Component II - Strengthening of Financial Sector Resilience and Development of Capital Markets for Efficient Financing of the Economy.

Sub-component II.1 – Financial Sector Governance

5.2.12. Problems and Constraints: The financial sector's resilience is negatively affected by the cumbersome and inefficient nature of several instruments, the lack of reliable data allowing for the assessment of customer risks in both the banking and insurance sectors, and the need to overhaul the information systems (IS) of all the institutions. In February 2018, Tunisia was included by the Financial Action Task Force (FATF) on a grey list of States likely to be exposed to money laundering and the

financing of terrorism. At the same time, the European Parliament included Tunisia on the list of countries with deficiencies in their anti-money laundering and anti-terrorism financing regimes.

5.2.13. Recent Measures Adopted by the Authorities: To strengthen financial sector governance, several reforms have been initiated. In 2016, the ARP adopted Law 2016-35 on the status of the BCT. It made it possible to ensure the independence of monetary authorities, strengthened prudential supervision of banks and improved the monetary policy operational framework. Similarly, the adoption of Law 2016-48 on credit institutions has resulted in the introduction of a deposit guarantee mechanism and the adoption of international best practices. Another reform undertaken consists in revising the Insurance Code, strengthening the governance of insurance companies, improving the sector's prudential supervision by the General Insurance Committee (CGA); and modernizing the life insurance legal framework. Lastly, the revision of Law 94-117 governing financial markets, following EBRD's technical assistance, should lead to better financial market governance. In this regard, the Minister of Finance in 2018 issued a Decree on the amendment of CMF's regulation on practical measures to combat money laundering and terrorism financing. The new instrument requires stock market intermediaries to take necessary steps and due diligence when concluding a business. Also, intermediaries are required to periodically ensure that the beneficiary is not included in the list of persons or entities subject to targeted financial sanctions.

5.2.14. Programme Activities: Actions retained under this programme aim to modernize the legal and regulatory framework governing the financial sector: (i) Publication of an organic law on the fight against terrorism, the suppression of money laundering (and incorporating provisions against proliferation), repealing and replacing Law 2015-26; (ii) Submission to the FATF of the CTAF report that provides an assessment of the Action Plan developed with FATF and confirming the completion of all the actions; (iii) Publication of the regulatory instruments of the supervisory bodies: BCT, CMF, CGA and ACM, relating to the risk-based supervision of money laundering and the fight against the financing of terrorism; (iv) Transmission by the CGA to the Minister of Finance of the draft law on the Insurance Code; (v) Transmission by the Minister of Finance of the draft law relative to the Insurance Code to the Council of Ministers; (vi) issuance of CGA regulations on the governance of insurance companies and the technical specifications on life insurance contracts; (vii) operationalization of the insurance sector's risk register; (viii) publication of the law on the policy of waiving public banks' outstanding receivables to address the issue of outstanding loans; and (ix) establishment of the Control Committee on Administrative and Structural Reform and Recovery and Audit Policies in Public Banks; and (x) Implementation of the necessary provisions to ensure a separation between the Procurement Board and the Bidders' Complaints Commission at the level of public banks.

5.2.15. Expected Outcomes: Implementation of the programme's measures is expected to yield an increase in the insurance penetration rate from 2% in 2015 to 2,5% in 2020; a decrease in the non-performing loans rate from 13.9% in 2017 to 11.5% in 2020; and Tunisia's removal from the FATF grey list in June 2019.

Sub-component II.2 –Deepening of Capital Markets

5.2.16. Problems and Constraints: Tunisian capital markets are characterized by a lack of depth and liquidity (Technical annex 12), resulting in a low contribution of these markets to the financing of the economy. The drying up of bank liquidity had a negative impact on Treasury bill subscription rates. Public debt management is characterized by a fragmented institutional framework, an illiquid secondary market and the absence of an efficient yield curve, necessary for the valuation of assets at market prices (Technical Annex 13). Regarding the conditions for access to the stock market, there is a lack of adaptation to the needs of SMEs: cumbersome procedures, inadequacy of prospectuses and listing conditions, and lack of support.

5.2.17. Recent measures Adopted by the Authorities: With AfDB technical assistance, the MoF has established new primary dealer specifications that allow for greater transparency and efficiency in

the management of treasury securities. This has made it possible to eliminate inefficient primary dealers. EBRD's technical assistance focused on the construction of a yield curve to serve as a benchmark for asset valuation. To make debt management centralized and dynamic, reforms have been undertaken. To revise conditions for access to the stock market, an order of the Minister of Finance of 27 March 1996 setting the rates and procedures for collecting fees and commissions due to the CMF and the BVMT for stock market transactions was published in 2016.

5.2.18. Programme activities: The actions selected under this programme aim at deepening and improving the efficiency of the public securities market: (i) Tunisie Clearing's publication of a yield curve serving as an efficient benchmark for issues and mark-to-market asset valuation; (ii) operationalization of the electronic platform for the auction of treasury securities by primary dealers; (iii) Submission of a note and draft law by the DGGDCF to the Minister of Finance on the creation of the "Tunisia Debt Management Office"; (iv) Publication of the decree on Sukuks; (v) Adoption by the college of CMF of the regulations on the application of the provisions of the Decrees on Sukuks for the issuance of Islamic bonds to private sector institutions; (vi) Publication of the amendments made to the General Regulations of the Stock Exchange on the review of the Alternative Market's regulatory framework; (vii) Publication of the decree on money market funds; and (viii) BCT's issue of the circular governing the issue of negotiable debt securities (NDS).

5.2.19. Expected Outcomes: The programme is expected to result in an increase in the financial market's contribution to financing of the economy from 9.2% in 2015 to 11% in 2020; and an increase in market capitalization, as well as the subscription rate for public securities.

5.3. Policy Dialogue

5.3.1. During the past four years, the Bank has maintained close policy dialogue with the Tunisian authorities on the financial sector. The themes covered included SME financing, restructuring of the microfinance sector, mobile financial services, private equity and financing of inland regions. Under this programme, this dialogue will continue on the implementation of agreed reforms and on the provision of the necessary advisory services and technical assistance to the authorities. Technical assistance for non-bank financing of SMEs for digital finance within the framework of the Africa Digital Financial Inclusion (ADFI) will be deployed.

5.4. Loan Conditions

5.4.1. Preliminary measures: Dialogue with the Government identified the following measures as actions prior to the submission of PAMSFI II to the Board (see Table 4). These measures were retained because of their degree of maturity, the in-depth dialogue of which they were the subject and their significant impact on the programme's medium- and long-term results.

Table 4 - Pre-requisite measures

Component	Preliminary measures	
Component 1. Improvement of financial inclusion to reduce social and regional disparities		Proof
Measure 1	Transmission by the Minister of Finance of the draft decree setting out the administrative and financial penalties imposed by the Microfinance Supervisory Authority on MFIs, including the opinion of the ACM Board of Directors, to the President of the Government.	P ₁ : Copy of the letter of transmission of the draft decree setting out the administrative and financial sanctions decided by the ACM against MFIs
Measure 2	Publication of the Decree on the Real Estate Loan Guarantee Fund and signing of the agreement with SOTUGAR for the guarantee product for real estate loans for people with irregular incomes.	P ₁ : Copy of Government Decree No. 2018-749 of 7 September 2018, establishing the methods of management of the guarantee fund for housing loans for the benefit of social categories with irregular incomes, and the terms and conditions for the benefit of its interventions P ₂ : Copy of the Agreement on the management of the guarantee fund for housing loans for the benefit of the

		population belonging to the social classes with irregular income
Measure 3	Signing of the agreement between the Ministry of Finance and the guarantee mechanism management company for the creation of the Dhamen Express guarantee product for SMEs.	P ₁ : Copy of the agreement signed by Dhamen Express
Component 2. Building financial sector resilience and developing the capital markets to ensure efficient financing of the economy		
Measure 4	Publication of an organic law on the fight against terrorism, suppression of money laundering (and incorporating provisions against proliferation), repealing and replacing Law 2015-26.	P ₁ : Copy of Law 2019-21
Measure 5	Publication of Law 2018-36 on the policy of waiving public banks' outstanding debts to address the problem of outstanding loans.	P ₁ : Copy of Law No. 2018-36 of 6 June 2018, amending and supplementing Law No. 2015-31 of 21 August 2015, relative to strengthening the financial soundness of "Banque de l'Habitat" and "Société Tunisienne de Banque"
Measure 6	Implementation of the necessary provisions to ensure separation between the Procurement Board and the Bidders' Complaints Commission at the level of public banks	P ₁ : Copy of the letter from the Minister of Finance attesting the start of a process to separate the Procurement Commission from the Bidders' Complaints Commission at the level of public banks
Measure 7	Publication of Decree 2018-7-48 on money market funds	P ₁ : Copy of Government Decree No. 2018-748 of 7 September 2018, supplementing Decree No. 2001-2278 of 25 September 2001 implementing the provisions of articles 15, 29, 35, 36 and 37 of the Code of Collective Investment Schemes promulgated by Act No. 2001-83 of 24 July 2001

5.4.2. **Good practice principles for the application of conditionality: PAMSF1 is consistent with the good practice principles for the application of conditionality on budget support operations:** (i) good government ownership; (ii) close and continuous coordination with other partners (IMF, WB, AFD, EBRD, KfW and EU); (iii) alignment with national priorities and SDP thrusts; (iv) selectivity and parsimony in defining the number of key conditions; and (v) alignment of Bank support with Tunisia's 2019 budget cycle.

5.5. Financing Needs and Mechanisms

5.5.1. **Compared to 2018, the financing needs of the national Budget increased by 4.5% to TND 10,142 million, which will be financed by domestic debt for TND 2,350 million and TND 7,792 million to be financed by external debt.** These financing needs were assessed on the basis of the economic budget. For 2019, total revenues are projected at TND 30,719 million for an estimated total level of expenditure of TND 40,861 million. The financing needs will be met by Tunisia with the support of its TFPs. The Bank will help to meet this financing need to the tune of EUR 120 million (UA 98 million). The consolidation and reinforcement of tax reforms, the streamlining of public expenditure and the improvement of revenue mobilization will improve the budgetary margins that will be generated to maintain the balance of public finances. The basic primary balance will therefore improve from -2.3% of GDP in 2018 to -1.2% in 2019 compared to -3.9% in 2017. Table 5 below presents the structure of the financing gap.

Table 5 Financing Needs of the national budget

	Millions of dinars		Millions of Euro	
	2018	2019	2018	2019
Total revenue and grants	27 966	30 719	8 401	9 125
Total expenditure and net loans	37 666	40 861	11 314	12 138
Of which interest payments	2 755	3 137	827	932
Of which capital expenditure	5 086	6 170	1 528	1 833
Financing needs	9 700	10 142	2 914	3 013
Domestic financing	2 340	2 350	703	698
External financing	7 360	7 792	2 211	2 315
Allocated loans	1 136	820	341	244
*) State projects	937	700	282	208
(**) retroceded loans	198	120	59	36
Unallocated loans (Budget Support + MFI)	5 446	7 919	1 599	2 261

including, ADB	0	403	0	120
including, IMF	1 603	1 500	469	439
including, WB	1 453	1 336	425	391
including, EU	0	1 025	0	300
including, FMA	359	120	105	35
including, KFW	342	683	100	200
including AFD	0	342	0	100
including Saudi Arabia	0	1 500	0	439
including, MFI	1 709	0	500	0
Syndicated loan	0	810	0	237

Source: MoF, 2018

VI. OPERATION IMPLEMENTATION

6.1. Programme Beneficiaries

6.1.1. **The programme's end-beneficiary is the Tunisian population.** It will benefit from improved living conditions due to inclusive and sustainable economic growth made possible by the creation of economic opportunities and jobs. The private sector will also benefit from PAMSFI. Its access to financing will be facilitated by the improved supply of financial services, including in the country's hinterland. Access to savings services will enable people with low and often irregular incomes to maintain a more stable level of consumption over time. In addition, access to financing for very small, small and medium-sized enterprises (VSMEs) should help to create more jobs. Finally, financial inclusion reduces the cost of implementing social policies, such as the payment of benefits.

6.2. Expected Impact on Gender, the Poor and Vulnerable Groups

6.2.1. One of the main objectives of PAMSFI II is to strengthen financial inclusion in access to micro-credit and digital finance in order to enhance access to financial services for women, employment opportunities and the reduction of inequalities. About half of micro-credit beneficiaries in Tunisia are women and 26% are young people, who borrow to finance small productive projects in the agricultural and handicraft sectors, usually in rural areas. The inclusion strategy supported by PAMSFI will also foster the economic and financial inclusion of the poor through other channels. PAMSFI includes a measure for financing women entrepreneurs. In addition, several segments of the population, including needy families and students, are expected to benefit from the development of mobile financial services to receive their allowances.

6.3. Impact on the Environment and Climate change

6.3.1. **In terms of climate change, PAMSFI II has no potential environmental and social impact.** The project has been classified in category 3 in accordance with the Bank's environmental and social procedures. It is expected to strengthen the resilience of small farmers to climate hazards due to insurance and compensation mechanisms.

6.4. Impact in Other Areas

6.4.1. **By focusing on improved access to finance for businesses, PAMSFI will help to create an enabling environment for private sector activities.** Facilitation of access to financing for businesses is especially important since this factor is one of the main obstacles to doing business in Tunisia.

6.5. Implementation, Monitoring and Evaluation

6.5.1. **The programme's implementation will be carried out by the Ministry of Finance (MoF), in close coordination with the Ministry of Development, Investment and International Cooperation (MDICI).** The General Directorate of Financing (DGF) of the MoF will be responsible for supervising the programme. With the necessary staff and reform expertise, it effectively monitored

the implementation of Phase 1 of the programme. The MoF has satisfactorily implemented several policy-based programmes from different donors thanks to its ability to mobilize the various stakeholders involved in the Programmes. The agreed action matrix will form the basis for PAMSFI II monitoring and evaluation. Supervision missions are planned during implementation of the programme to assess the progress made.

6.6. Financial Management Disbursement and Procurement

6.6.1. Fiduciary risk assessment: The assessment of Tunisia's fiduciary risk conducted under CSP 2017-2021 concluded that the risk level was moderate, based on the most recent public finance management diagnostic review (2015 PEFA, OECD Integrity Scan). An update of some aspects of fiduciary risk was carried out during PAMSFI II's appraisal, including an assessment of financial sector-specific risks. This revealed that the Tunisian public finance management system allows for an acceptable preparation and execution of the annual budget and has an adequate mechanism for internal control and expenditure verification. However, a significant delay has been noted in the implementation of priority intervention thrusts. Indeed, the far-reaching public finance management reforms, including the ambitious programme of Performance Budgeting (PB) has just been strengthened by the adoption, in January 2019, of the new Organic Budget Law (OBL). This Organic Law provide for: (i) the effective implementation of the new budgetary nomenclature; (ii) the simplification of ex-ante control and the strengthening of ex-post control; and (iii) the expansion of the Court of Auditors' role, which will be responsible for certifying the State's accounts. In addition, attention should be paid to the streamlining of internal control bodies characterized by a high degree of fragmentation and a systemic approach not based on a risk-based approach. Implementation of the reform programme is expected to help mitigate the identified fiduciary risks. PAMSFI II will be implemented using the full public expenditure chain in Tunisia.

6.6.2. Financial Management Mechanisms and Disbursement: Due to the type of operation (budget support), the use of financial resources will be subject to national public finance regulations. The public expenditure circuit will be used in its entirety and the relevant internal control rules will be applied. Through its single tranche disbursement in 2019, the EUR120 million loan will help to cover the budget deficit for 2019. At the Borrower's request, the Bank will disburse the funds of this loan in foreign currency to a special account opened at the Central Bank of Tunisia. The Borrower will ensure that once the deposit is made to the said account, the equivalent of the funds in local currency will be transferred to the Treasury's Current Account. The Ministry of Finance will provide the Bank, within thirty (30) days after the disbursement, with a letter of confirmation of this transfer indicating that the total amount of the loan has been received, converted and repaid into the Treasury's Current Account, together with the transaction notices issued by the Central Bank of Tunisia. Given the moderate level of overall fiduciary risk, this programme will be subject to annual supervision. The half-yearly budget implementation reports available on the Ministry of Finance's website will also be consulted. In addition, the following documents, which must be drawn up in accordance with the new Organic Budget Law: the Final Settlement Law on the implementation of the Finance Law and the related Court of Auditors' report for 2019 and 2020 will be consulted by the Bank.

6.6.3. External Audit: The audit will be based on the national ex-post verification mechanism employed by the *Contrôle Général des Finances* (General Financial Control) (CGF), which will conduct a specific audit on financial flows and an audit on the implementation performance of the measures. The deadline for submission of the specific audit report on flows and performance by the CGF to the Bank will be six months following the closure of the Programme.

6.6.4. Procurement: The Tunisian public procurement system has made major progress in recent years since the start, in 2014, of implementation of the action plan of the public procurement reform (undertaken with Bank assistance in 2012) and the adoption of a new public procurement code, as well as the continued implementation of the various actions provided for in the plan. The country fiduciary

risk level for the procurement component was reassessed during the appraisal and was deemed moderate.

6.6.5 Financial sector procurement practices have been reviewed by the Bank to ensure that the programme includes appropriate fiduciary measures. In particular, it should be noted that public banks are no longer subject to public procurement regulations¹⁰. They have specific public procurement regulations and are now subject to control bodies. Public banks¹¹ exempted from using the public procurement code have developed procurement manuals based on the new national regulations while taking into account the efficiency and flexibility aspects they need. Information collected¹² from sector stakeholders shows some weaknesses in terms of procurement practices within public banks: (i) the contracts awarded by these institutions are sometimes split, resulting in a lower risk of competition and challenges in supervising a large number of contracts; (ii) although TUNEPS¹³ has been in force since 1 September 2018, Public Banks have still not had access to it; and (iii) the Public Bank Procurement Control Boards (PCBs), which reviews the procurement/purchase documents and rules on contract awards, is also responsible for reviewing complaints and claims from bidders participating in these same contracts: there is no independence and fairness in the handling of complaints. The financial sector's fiduciary risk is deemed substantial. However, to reduce this risk to a moderate level, it was recommended that public banks set up an independent commission to examine complaints and claims from bidders.

VII. LEGAL INSTRUMENT AND AUTHORITY

7.1. Legal Instrument

7.1.1. **The Bank (AfDB) will sign a loan agreement with the Republic of Tunisia** for the purpose of implementing PAMSFI II in the amount of EUR 120 million (UA 98 million).

7.1.2. **Conditions precedent to loan effectiveness:** Loan effectiveness will be subject to fulfilment of the conditions stipulated in Section 12.1 of the General Conditions Applicable to Loan Agreements.

7.2. Conditions Associated with the Bank's Intervention

7.2.1. **Conditions precedent to Board presentation of the PAMSFI II:** It was mutually agreed with the Government during the Programme's appraisal that the measures precedent indicated in Section 5.4.1 (Table 5) of this report should be implemented before the programme's presentation to the Bank's Board of Directors.

7.2.2. **Conditions precedent to disbursement.** Disbursement of the EUR 120 million single loan tranche will be subject to fulfilment of the following condition: Submission to the Bank of evidence of the existence of a special account opened at the Central Bank of Tunisia, into which the loan resources will be paid.

7.3. Compliance with Bank Group Policies

7.3.1. **PAMSFI II was prepared in compliance with applicable Bank Group policies**, in particular, the policy on programme-based operations. No waiver has been requested for these Guidelines in this proposal.

¹⁰ The new public procurement system is governed by Decree No. 2014-1039 of 13 March 2014

¹¹ As the Board of Directors and its specialized committees composed of qualified profiles recruited through a call for applications.

¹² Auditors of Public Banks, Committee of State Auditors

¹³ Electronic procurement system for Tunisia's procurement procedures

VIII. RISK MANAGEMENT

8.1. **Two major risks could affect the quality of this operation's outcomes:** (i) a worsening of the budget deficit, notably due to the risk of a higher than expected level of energy subsidies, which would be spread over time also the increase in the wage bill; and (ii) a decline in the pace of reforms as elections approach (detailed analysis in Technical Annex 3).

8.2. **The Tunisian authorities have already taken the necessary measures to anticipate and address these risks.** As regards the risk of deepening the fiscal deficit and the need to contain the increase in the wage bill and energy subsidies, a framework has been agreed with the IMF and various donors to control the evolution of these additional expenses. To reduce the cost of energy subsidies, the Government has undertaken an ambitious program to produce electricity from renewable energy sources. This sector is likely to contribute to economic recovery.

IX. RECOMMENDATION

9.1. In the light of the foregoing, it is recommended that the Board of Directors approves in favour of the Republic of Tunisia a loan not exceeding EUR 120 million to implement the Financial Sector Modernization Support Programme II, for the purpose and conditions set out in this report.

Republic of Tunisia
Ministry of Development, Investment and International Cooperation

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Letter of Development Policy
Financial Sector Modernisation Support Programme (PAMSFI II)
(2018-2019)

Mr. President,

I Country Context

With a **democracy** crowned by the holding of municipal elections, Tunisia is firmly committed to strengthening **its constitutional achievements** and successfully holding the presidential and legislative elections scheduled for the end of 2019. The **gradual introduction of decentralisation** as a new mode of local governance was enshrined in the **local government code** based on the principles of free governance of local authorities, financial independence of municipalities, free administration of local affairs and **participatory local democracy**.

In addition, the Government is striving to further entrench good governance and the fight against corruption through the establishment of the **Independent Constitutional Good Governance and Anti-Corruption Commission**. The government is also committed to creating a legal framework attuned to international standards relating to the fight against money laundering and the protection of personal data.

On the security front, the continued commitment to the implementation of a **proactive, purposeful and forward-looking security strategy** has recorded remarkable progress.

It is also important to stress that the Government is committed to laying the foundations for a sound and enabling social climate for human capital development and recognition of the value of work. The adoption of the **social contract** and the establishment of the **National Council for Social Dialogue** have fostered a **participatory approach to dialogue and consultation among social partners**. The recent adoption of the "Social Amen" platform is expected to promote the right to a fixed minimum wage and the benefit of urgent social interventions for disadvantaged groups.

Regarding economic development, and in order to achieve a successful economic transition, the Government has committed itself to a finely measured adjustment effort to ensure the modernisation and strengthening of the economy's competitiveness and to restore the solidity of major balances.

In the context of major economic challenges, particular attention has been paid to speeding up the implementation of structural reforms in order to improve economic and financial performance, make the business and investment environment more attractive and raise the level of potential growth over the medium term.

In this context, **an action plan** has been developed to **improve Tunisia's ranking in the Doing Business report**. For the first time since 2010, Tunisia has improved its score in the "Doing Business 2019" ranking. Tunisia has moved from the 88th position in the "Doing Business 2018" ranking to 80th position, gaining 8 spots. This action plan includes 50 regulatory measures and reforms that cover a wide range of areas and require the active participation of several organisations. The objective is to join the world's top 50 and be among the top 3 in Africa by 2020.

In addition, the Government has ensured the effective operationalization of the new investment law through the establishment of governance bodies; the **Tunisian Investment Authority** operates as a single interlocutor and functions as a "one-stop shop" to support domestic and foreign investors and facilitate administrative formalities and procedures. This adds to the launch of the **Strategic Investment Council**, which brings together both private and public actors whose main role is to promote private investment efforts and improve the business climate through the approval of comprehensive and sectoral strategies.

In the same vein, it should be noted that the desire to **substantially reduce the number of investment-related authorisations** was reflected in the publication of Government Decree No. 417 of 11 May 2018 on the publication of the exclusive list of economic activities subject to authorisation and the list of administrative authorisations required for the implementation of projects, the relevant provisions and their simplification. The objective is to unlock economic potential and boost private investment.

A high-level international conference on the prospects for public-private partnership was organised on 18 September 2018 as part of promotion of the PPP approach and the launch of transformative projects; a pipeline of thirty-three (33) major projects with a budget of around TND 13 billion was presented. The projects presented concern the sectors of transport and logistics, energy, water and the environment, infrastructure and urban development and science and technology poles. The objective is to strengthen infrastructure and open up new economic opportunities through innovative and job-creating projects in all regions of the country.

At the same time, the Government is committed to speeding up implementation of the **energy transition policy and developing secure energy supply**. An action plan to accelerate new renewable energy generation projects in Tunisia was initiated with the award of wind and solar energy concessions and authorizations.

In addition, as part of implementation of the Tunisia 2020 digital strategy, the Startup Act was adopted. This law reflects the Government's desire to significantly improve Tunisia's attractiveness as a hub for innovation and technological value added creation and to promote the initiative of young people and innovators.

In addition, the 2019 Finance Law aims to **strengthen growth, restore the purchasing power of citizens, improve the business climate and attractiveness of investments and control financial balances**. Similarly, no measures to increase taxes on individuals or companies are planned for next year.

Furthermore, and with the aim of further modernising public financial management, an **organic budget law** was recently adopted by the ARP; this new regulation enshrines **performance budgeting** while drawing up a new budgetary architecture based on three-year budgeting.

The **growth pattern for 2019** hinges mainly on consolidating the growth rate with a gradual control of global financial balances.

The GDP growth target is 3.1% in 2019 compared to 2.5% expected in 2018; this growth rate is contingent on an improved contribution from investment and exports. This objective hinges in particular on the impetus provided by the reforms initiated to promote entrepreneurship and the creation of new businesses, as well as export support and access to new markets.

In addition, the Government will endeavour to restore financial stability by reducing the budget deficit from 4.9% in 2018 to **3.9% in 2019**, containing the current account deficit in order to consolidate the country's external balances and reduce the inflation rate by pursuing a proactive monetary policy.

Financial sector reform is an essential prerequisite for achieving the objectives of inclusive and sustainable development while promoting the sustainability of financial balances.

In this regard, and in consolidation of the achievements of PAMFSI I, the Government undertook to implement the second phase of the Financial Sector Modernisation Support Programme through a second round of reforms aimed at improving financial inclusion and financial sector development. This second phase of financial sector modernisation will help to support the emergence of a new development model for Tunisia, in which the private sector can thrive and create jobs throughout Tunisia, and in which disadvantaged segments of the population can contribute to growth by having more access to financing.

II Financial Sector Modernisation Support Programme (PAMFSI II) Measures

PAMFSI II builds on two complementary components, namely the reduction of social, territorial, regional and gender disparities through improved financial inclusion and strengthening of financial sector resilience and development of capital markets for efficient financing of the economy. The first component will cover improvement of the financial inclusion of vulnerable populations with a gender perspective and improvement of access to financing for SMEs. The second component focuses on the strengthening of financial sector governance framework and deepening of capital markets.

Component I - Reduction of Social and Regional Disparities through Better Financial Inclusion

This component will include a first reform component that will enable the national financial inclusion strategy to achieve its objectives: improving financial inclusion from 36% in 2015 to over 38% in 2020 and increasing the penetration rate of mobile financial services from 4% in 2017 to 10% by 2020; doubling the amount of micro-credit stock granted by microfinance institutions; online registration (and payment of related fees) of 100% of public school pupils/students; and covering 400,000 ha of rain-fed cereals against natural disasters.

To meet these challenges, it was agreed under this programme to implement reform measures, some of which have already been executed, such as (i) publication of the Order of the Minister of Finance on doubling the ceiling of microcredit granted by micro-finance institutions; (ii) approval by the Microfinance Supervisory Authority (ACM) Board of Directors of the draft order of the Minister of Finance, setting out the administrative and financial penalties imposed by the ACM on Microfinance Institutions (MFIs); (iii) launch of the digital payment product for the enrolment of public education pupils/students; (iv) Approval by the Minister of Finance of the status of the MFI professional association; (v) publication of implementing decrees operationalising the compensation fund for agricultural damage caused by natural disasters; (vi) publication of the decree for implementation of the fund for the compensation of agricultural damage caused by natural disasters and (vi) publication of the Decree on the Real Estate Loan Guarantee Fund and signature of the agreement with the Tunisian Guarantee Company (SOTUGAR) for real estate loans guarantee product for the population with irregular income.

The second reform aspect covered by this component aims to improve access to financing for SMEs in the regions, develop support and guarantee mechanisms for SMEs, encourage private equity activity and finance innovation to raise the ratio of credit to private companies relative to GDP from 85.58 percent of GDP in 2018 to 88 percent in 2020.

In order to achieve these objectives, several reform measures taken by the Government, including (i) adoption by the Council of Ministers of the draft law establishing the Bank of the Regions; (ii) signature of the agreement between the Ministry of Finance and SOTUGAR, for implementation of the redesigned guarantee product, Dhamen Express, for SMEs; (iii) publication of the decree establishing the SME Restructuring Fund and signature of the agreement between the Ministry of Finance and SOTUGAR for the financial restructuring guarantee product; (iv) publication of the three implementing instruments of the law governing collective procedures; and (v) signing of the agreement between the Ministry of Finance, the Ministry of Communication Technologies and Digital Economy and SOTUGAR for the Startups Guarantee Fund.

Component II - Strengthening Financial Sector Resilience and Developing Capital Markets for Efficient Financing of the Economy

The measures under this component will focus on two reform areas. The first thrust will aim to strengthen financial sector governance through the adoption of international standards to combat illicit financing, modernize insurance sector governance and strengthen the banking sector's resilience. It is expected that implementation of the measures agreed under this sub-component will raise the insurance penetration rate from 2% in 2015 to 3% in 2020 and decrease the non-performing loans rate from 13.9% in 2017 to 11.5% in 2020.

In this regard, some measures have already been implemented, including: (i) publication of the organic law on the fight against terrorism and the suppression of money laundering (ii) publication of the regulatory instruments implementing this law by the Central Bank of Tunisia (BCT), the Financial Market Council (CMF), the General Insurance Committee (CGA) and the Microfinance Supervisory Authority (ACM), concerning risk-based supervision in the area of money laundering and the fight against terrorism financing; (iii) transmission by the Minister of Finance to the Council of Ministers of the draft law on the Insurance Code; (iv) issuance of the CGA regulations on the governance of insurance companies and the factsheet on life insurance contracts; (v) publication of the law on the policy for waiving public banks' outstanding receivables; and (vi) commencement of the necessary measures to ensure

separation between the procurement board and the bidders' claims commission at the level of public banks.

The second reform area covered by this component will contribute to the development of capital markets through consolidation of the efficiency of the public securities market, facilitation of access to financing for SMEs through the stock market and diversification of the product offer to mobilize private and institutional savings. It is expected that the implementation of this sub-component will increase the financial market's contribution to the financing of the economy from 9.2% in 2015 to 10.5% in 2020 and increase the market capitalisation and subscription rate of public securities.

In order to achieve these objectives, several actions have been adopted in this area, including: (i) publication by the Ministry of Finance, the Financial Market Council, Tunisia Clearing and the Central Bank of a yield curve serving as an efficient benchmark for issues and mark-to-market valuation of assets; (ii) operationalisation of the electronic auction platform for Treasury securities by Primary Dealers (PDs); (iii) publication of the decrees on Sukuks; (iv) adoption by the CMF college of the regulations on application of the decrees on Sukuks; and (v) publication of the decree on monetary open-ended investment companies (SICAV).

Furthermore, other reform measures supported under this second phase of PAMSFII are also under preparation in 2019 to further strengthen financial inclusion in order to reduce regional disparities and strengthen the resilience of the financial sector.

The consistency of the reform actions provided for in this programme attests to Tunisia's firm commitment to a new development and construction process that will entrench the spirit of democracy and ensure economic prosperity and social progress through inclusive growth.

Technical and financial support for this reform effort is necessary to meet current and future challenges. The Tunisian Government is thus determined to implement, with the support of its partners and in particular the AfDB, all the reforms planned under this programme in order to ensure the success of its new development model and is seeking appropriate financial support from the Bank.

ANNEX II
MATRIX OF REFORM MEASURES OF THE 2018 – 2019 PROGRAMME

(*)Measure prior to Board Presentation

Objectives	Measures carried out in PAMSFII	PAMSFII Measures 2018	PAMSFII Measures 2019	Targeted Outcome Indicators and Data Source	Data Sources and Responsible Institution
I. Reduction of social and regional disparities by improving financial inclusion					
I.1 Financial Inclusion					
<i>Boost the microfinance sector while developing responsible microfinance</i>	<i>Issuance of the Order of the Minister of Finance on equitable treatment of clients of microfinance institutions</i>	Publication of the Order of the Minister of Finance on the doubling of the microcredit ceiling granted by microfinance institutions	Validation of the feasibility study on the implementation of a refinancing vehicle for microfinance institutions by the steering committee	Financial inclusion rate up from 36% in 2017 to 38% in 2020	<u>DS₁</u> : Copy of the order of the Minister of Finance <u>DS₂</u> : Copy of the minutes of the steering committee meeting <u>RI</u> : MoF; ACM
	<i>Operationalization of the micro-credit risk registry</i>	Transmission by the Minister of Finance of the draft decree setting out the administrative and financial penalties imposed by the Microfinance Supervisory Authority on MFIs, including the opinion of the ACM Board of Directors, to the President of the Government(*)	Operationalization of phase 4 of the micro-credit risk centre integrating APR and basic scoring		<u>DS₁</u>: Copy of the letter of transmission of the draft decree setting out the administrative and financial sanctions decided by the ACM against MFIs <u>DS₂</u> : Letter of notification from the ACM of the operationalization of Phase 4 <u>RI</u> : MoF ; ACM

<i>Diversify the range of financial services and products (digital finance, micro-insurance, natural disaster compensation and social housing)</i>	<i>Launch of the national interbank and inter-telecom mobile payment product based on a platform managed by SMT</i>	Launch of the digital payment product for public education students' enrolment	Launch of at least one digital financial product for State payment to citizens as part of the implementation of the de-cashing strategy	Mobile financial services penetration rate from 3% in 2017 to 10% by 2020	<u>DS1</u> : notification letter for the launch of digital payment products <u>RI</u> : MoF; SMT
	<i>Validation of the pilot phase of index-linked agricultural insurance and the feasibility study of the overall agricultural insurance mechanism</i>	Approval by the Minister of Finance of the status of the professional association of MFIs pursuant to Decree-Law 117 relative to the organisation of microfinance institutions	Signing of the agreement between FTUSA and the professional association of MFIs for the marketing of micro-insurance products		<u>DS1</u> : Copy of the minutes of the constituent general meeting of the professional association of MFIs <u>DS2</u> : Copy of the signed agreement <u>RI</u> : MoF
			Publication of implementing decrees for the operationalization of the compensation fund for agricultural damage caused by natural disasters		<u>DS2</u> : Letter from the MoF transmitting a copy of the publication of the implementing decrees <u>RI</u> : MoF, MinAgri
	Publication of the Decree on the Real Estate Loan Guarantee Fund and signing of the agreement with SOTUGAR for the guarantee product for real estate loans for people with irregular income (*)				<u>DS1</u> : Copy of Government Decree No. 2018-749 of 7 September 2018, establishing the methods of management of the guarantee fund for housing loans for the benefit of social categories with irregular incomes, and the terms and conditions for the benefit of its interventions <u>DS2</u> : Copy of the Agreement on the management of the guarantee fund for real

					estate loans for the benefit of the population belonging to the social classes with irregular income RI: MoF and SOTUGAR
I.2 Financing of VSMEs					
<i>Strengthen SME financing in the regions by improving the efficiency of SME financing mechanisms</i>	<i>Adoption by the steering committee of the institutional model for the establishment of the Bank of the Regions (BDR)</i>	Adoption by the Council of Ministers of the draft law establishing the Bank of the Regions	Inclusion in the State Budget of an allocation of TND 100 million to enable it to subscribe to the capital of the Bank of Regions	Ratio of credit to private companies relative to GDP from 83.8% of GDP in 2018 to 86% in 2020	<u>DS1</u> : Copy of 2019 Finance Law RI: MoF
Develop guarantee products better adapted to the financing needs of SMEs		Signing of the agreement between the Ministry of Finance and SOTUGAR, for the implementation of the reconfigured Dhamen Express guarantee product for SMEs (*)	Launch of the study on improving the management of the national guarantee fund (as part of the setting up of the Bank of the Regions)		<u>DS 1</u>: Copy of the agreement signed by Dhamen Express RI: MoF and SOTUGAR
<i>Support SMEs in restructuring situations</i>	<i>Operationalization of the agreement between the BTS and the Ministry of Women for the launch of a financing product dedicated to women entrepreneurs</i>	The decree establishing the SME Restructuring Fund is published and the agreement between the MoF and SOTUGAR is signed for the financial restructuring guarantee product.	Operationalization of the SME Restructuring Fund through validation of the first batch of diagnostic reports and proposals for an SME safeguard plan		<u>DS1</u> : Copy of the decree creating the SME restructuring fund <u>DS2</u> : Copy of the minutes of SME funds steering committee meeting RI: MoF ; Min Ind
		Publication of the decree implementing regulations of the law governing collective proceedings.	Adoption by the Council of Ministers of the decree implementing the law on excessive interest rates for companies setting the new margin		<u>DS1</u> : Copy of implementing decrees of collective proceedings <u>DS2</u> : Copy of minutes of the CM meeting adopting the decree RI: Ministru of Industry and SMEs

<i>Establish instruments to strengthen SMEs' equity capital</i>	<i>Extension for a 3-year period of the provisions of Article 22 of the 2015 Finance Law allowing private equity funds to support the financial restructuring of companies</i>	Finalization and transmission of the draft Law on Crowdfunding to the Ministry of Industry and SMEs and to the Presidency of the Government	Adoption by the Council of Ministers of the draft law on Crowdfunding		<u>DS1</u> : Copy of the excerpt of the minutes of the Council of Ministers <u>RI</u> : API
<i>Finance innovation</i>		Signing of the agreement between the Ministry of Finance, the Ministry of ICT and SOTUGAR for the Start-up Guarantee Fund	Establishment of the Public-Private Fund (Anava) for the financing of start-up firms and its financing by the State via the CDC for up to 20% of its size.	5 direct beneficiaries of the Start-up Fund by 2020.	<u>DS1</u> : Copy of the agreement <u>DS2</u> : Copy of the BPI France contract Study on the structuring of the fund of funds <u>RI</u> : MoF ; CDC
II. Strengthening of financial sector resilience and development of capital markets for an efficient financing of the economy					
II.1 Financial sector governance					
<i>Adopt international standards in the fight against illicit financing</i>		Publication of an organic law on the fight against terrorism, the suppression of money laundering (and incorporating provisions against proliferation), repealing and replacing Law 2015-26 (*)	Submission to the FATF of the CTAF report on the status of the Action Plan drawn up with the FATF and confirming the implementation of all actions.	Tunisia is taken off the FATF grey list	<u>DS1</u> : Copy of Law 2019-09 <u>DS2</u> : Letter of transmission of the CTAF Report to the FATF <u>RI</u> : CTAF
		Publication of the regulatory texts of supervisory institutions: BCT, CMF, CGA and ACM, relating to risk-based supervision in the field of money laundering and the fight against the financing of terrorism			<u>DS1</u> : Copies of texts on the suppression of money laundering and the financing of terrorism. <u>RI</u> : BCT, CGA, CMF, ACM
<i>Modernize the legal and regulatory framework governing the insurance sector</i>	<i>Launch of the revision of the legal framework governing the insurance sector</i>	Submission of the draft law on the Insurance Code by the Minister of Finance to the Council of Ministers	Preparation and transmission to stakeholders for consultation of the first implementing instruments of the Insurance Code Law	Insurance penetration rate from 2% in 2015 to 2,5% in 2020	<u>DS1</u> : Copy of the letter from the CGA transmitting the bill <u>DS2</u> : Letter of transmission to stakeholders <u>RI</u> : MoF
			Operationalization of the insurance sector's risk register		<u>DS1</u> : Copies of the CGA regulations

		Issuance of the General Insurance Committee Regulations on the governance of insurance companies and the technical sheet on life insurance contracts			<u>DS2</u> : Copy of the CGA circular note on the operationalization of the registry <u>RI</u> : MoF; CGA
<i>Strengthen the Banking sector's resilience</i>	Adoption by the ARP of the law revising Banking Law No. 2001-65 of July 2001 on credit institutions	Publication of the law on the policy of waiving public banks' outstanding debts (*)	Establishment of the Control Committee for Administrative and Structural Reform and Recovery and Audit Policies in Public Banks	decrease in the rate of outstanding debt from 13.9% in 2017 to 11.5% in 2020	<u>DS1</u> : Copy of Law 2018-36 <u>DS2</u> : Copy of the decision to set up the committee <u>RI</u> : MoF
<i>Strengthen the integrity of public banks' procurement systems</i>			Implementation of the necessary provisions to ensure separation between the Procurement Board and the Bidders' Complaints Commission at the level of public banks (*)		<u>DS1</u> : Letter from MoF <u>RI</u> : MoF
II.2 Deepening of Capital Markets					
<i>Deepen and improve the efficiency of the public securities market, as well as the efficient management of public debt</i>	<i>Signing of the new specifications of the primary dealers</i>	Publication by MoF, CFM, Tunisie Clearing and BCT of a yield curve serving as an efficient benchmark for issues and mark-to-market valuation of assets	Operationalization of the electronic platform for the auction of treasury securities by primary dealers	100% of primary market auctions included in the platform before the end of June 2019	<u>DS1</u> : Copy of the letter of notification of the operationalization of the yield curve <u>DS2</u> : Copy of the notification letter to the <i>primary dealers</i> for auctions via the electronic platform <u>RI</u> : MoF
			Submission of a note and draft law by the DGGDCF to the Minister of Finance on the establishment of the "Agence Tunisie Trésor".		<u>DS2</u> : Copy of the letter of transmission of the bill <u>RI</u> : MoF
Mobilize private and institutional savings and boost the capital		Publication of the Sukuks Decree	Adoption by the CMF college of the regulation on the application of the provisions of the decrees on	Contribution of the financial market to the financing of the	<u>DS1</u> : Copy of the Sukuks Decree

market through new products			Sukuks on the issuance of sukuks to private sector institutions	economy from 8% in 2018 to 11% in 2020	<u>PDS2</u> : Copy of the letter of transmission to the MoF for VISA <u>RI</u> : MoF ; CMF
			Publication of amendments to the Stock Exchange General Regulations on the review of the Alternative Market Regulatory Framework		<u>DS1</u> : Copy of the order <u>RI</u> : MoF ; CMF
		Publication of the decree on money market funds (*)	Issuance by the BCT of the circular governing the issuance of Negotiable Debt Securities		<u>DS1</u>: Copy of the decree on money market funds <u>DS2</u> : Copy of the circular issued by the BCT on NDSs <u>RI</u> : MoF; BCT

NOTE ON RELATIONS WITH THE IMF

IMF Reaches Staff Level Agreement on the Fifth Review of Tunisia’s Reform Program Supported by the Extended Fund Facility Arrangement

April 17, 2019

End-of-Mission press releases include statements of IMF staff teams that convey preliminary findings after a visit to a country. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF’s Executive Board. Based on the preliminary findings of this mission, staff will prepare a report that, subject to management approval, will be presented to the IMF’s Executive Board for discussion and decision.

- A staff-level agreement was reached between IMF staff and the Tunisian authorities on the Fifth review of Tunisia’s economic reform program supported by the Extended Fund Facility arrangement.
- The authorities and IMF staff agreed on policy and reform steps to ensure that the budget deficit target of 3.9 percent of GDP (before grants) for 2019 can be met to contain the high debt and elevated financing needs.

An International Monetary Fund (IMF) staff team led by Björn Rother met with the Tunisian authorities in Washington, DC on the sidelines of the IMF Meetings on April 11-16 to discuss the authorities’ economic reform program and their policy plans for the Fifth Review of the Extended Fund Facility (EFF) arrangement. At the end of these discussions, Mr. Rother made the following statement:

“The IMF team and the Tunisian authorities have reached a staff-level agreement on the Fifth Review of the country’s economic reform program supported by the IMF’s EFF arrangement. Completion of the Review is subject to the approval by the IMF’s Executive Board. Tunisia will benefit from a sixth disbursement of SDR 177 million (around US\$247 million) following the Executive Board’s review that is expected to take place by early June 2019. This will bring total disbursements under the EFF to about US\$1.6 billion and will help unlock additional financing from Tunisia’s other external partners.

“We had fruitful discussions with the authorities on their economic policy agenda aimed at stabilizing and reforming the economy in the months ahead, taking into account the difficult socio-economic situation and the challenging regional environment. The authorities and staff agreed on policy and reform measures to ensure that the budget deficit target of 3.9 percent of GDP (before grants) for 2019 can be met to contain the high debt and elevated financing needs. In parallel, the authorities are working on strengthening the social safety net for lower-income families to help protect them from the potential impact of the reforms, supported by the new databank of vulnerable households . Monetary and exchange rate policies will remain geared towards reducing inflation that threatens the standards of living of all Tunisians and on

supporting an improvement in the large current account deficit through better price competitiveness.

“The IMF team thanks Minister of Finance Chalghoum, Minister of Development, Investment and International Cooperation Laâdhari, Minister of Major Reforms Rajhi, and Central Bank Governor El Abassi, as well as their staff for constructive discussions.”