PROGRAM INFORMATION DOCUMENT (PID)
CONCEPT STAGE

September 1, 2015
Report No.: 99425

Operation Name	Tunisia: Third Governance, Opportunities, and Jobs DPL
Region	MIDDLE EAST AND NORTH AFRICA
Country	Tunisia
Sector	Central government administration (30%); General public administration sector (20%); Other social services (20%); Banking (20%); Telecommunications (10%)
Operation ID	P150950
Lending Instrument	Development Policy Lending
Borrower(s)	GOVERNMENT OF TUNISIA
Implementing Agency	Ministry of Economy and Finance
Date PID Prepared	October 26, 2014
Estimated Date of Appraisal	November 5, 2014
Estimated Date of Board Approval	December 18, 2014
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Country and Sector Background

Following the resolution of the political crisis at end 2013, the subsequent adoption of a new Constitution and the appointment of a non-partisan government, the democratic transition has followed its course according to plan, with the organization of orderly and peaceful legislative elections at end October. Consistent with the course of action charted in the GOJ-2 DPL, and with a view to establish the most adequate policy environment for orderly elections cycle to be held until end 2014, the Government has pursued several key reforms that had been initiated since the revolution, taken some short-term actions where immediate remedy was needed, while attempting to stabilize an challenging macroeconomic situation. After the promulgation of the Constitution, the Government also completed major steps for the completion of the democratic process, namely the establishment of the electoral commission, the adoption of election code and lastly the successful organizations of the legislative elections in October, while the preparation for the Presidential elections are ongoing. Following the latter, a new Government should take office by the end of the first quarter of 2015. In the meantime, the current transition government will stay in place, while the new Assembly should be inaugurated before the end of 2014.

The challenges identified throughout the DPL series will remain central policy drivers even after the election cycle is completed: Tunisia has to maintain economic and social stability, while preparing the ground for the implementation of reforms that will stimulate structural transformation, sustained growth and sustainable employment generation. After recovering in 2012, growth is hovering just above 2 percent, a pace insufficient to make a dent in unemployment and poverty, and the outlook remains uncertain. Consequently, external financing needs are expected to remain large over the next two or three years. Accelerating the pace of recovery will depend on the Government's ability to complete some of the key reforms before the elections, and thereby pave the way for a medium-term economic transformation plan.

II. Operation Objectives

The reforms supported by the proposed GOJ-3 DPL operation aim at assisting Tunisia tackle the short-term challenges to consolidate the transition, while paving the way to stronger and more inclusive growth, leading to job creation over the medium-term.[1] The reforms are instrumental to achieve the objectives that have motivated the revolution: opening up the economy so that it can deploy more and better economic opportunities for the Tunisian people, in particular the youth, while entrenching participation and voice as key ingredients of policy making. Building upon achievements realized under the GOJ-1 DPL and GOJ-2 DPLs, the reform program underpinning the proposed operation, focuses on the four key policy areas of the series: (i) promoting private investment and establishing a more competitive environment; (ii) restructuring the financial sector; (iii) improving the quality and accountability of social sector services; and (iv) increasing transparency and accountability of public policies and finance.

Building upon achievements realized under the first and second DPL in the series, the supported reform program underpinning the proposed GOJ-3 DPL, focuses on three of the series' four key policy areas: (i) promoting private investment and establishing a more competitive environment; (ii) restructuring the financial sector and (iii) increasing transparency and accountability of public policies and finances. Measures in the area of improving the quality and accountability of social sector services have been supported in the first two operations of the series.

- **Private sector investment**: Key reforms focus on the telecommunications sector to (i) simplify the regulatory environment for businesses; (ii) expand regulatory reforms in the telecommunication sector to increase access to and affordability of broadband and internet services; (iii) modernize the competition framework by establishing a level playing field and independent enforcement mechanisms against anti-competitive practices.
- **Financial sector strengthening**: the reforms focus on (i) restructuring state-owned banks so as to improve their operations and solidify their capital base, with a view to improve the overall banking environment; (ii) improve the insolvency framework through the modernization of the law governing collective procedures; and (iii) take rapid action to reduce the stock of non-performing laws in the tourism sector, also with a view to provide new dynamism to this crucial sector.
- **Governance**: fundamental reform of the access to information framework in line with the provision of the new constitution, as well as improved transparency in public finances, notably in relation of operations by state-owned enterprises.

III. Rationale for Bank Involvement

Following a period of uncertainty characterizing most of 2013, the new Government which was appointed along with the approval of the new Constitution at end January 2014, has embraced the transition period with the ambition to stabilize the security situation, create the proper conditions for transparent and fair elections and take necessary action to strengthen the macroeconomic situation, while accelerating the reform agenda that had been initiated in 2011 with the support of the Bank other partners. Initial post-revolutionary reforms had primarily focused on strengthening governance through greater transparency and participation.[2] Since 2012, governance reforms are supplemented by economic reforms seeking growth acceleration and job creation. This program has been focusing on reforms aiming at: (i) creating the conditions to facilitate competition and private sector initiative (administrative simplification,

[1] See World Bank (May 2014), *The Unfinished Revolution. Bringing Opportunity, Good Jobs And Greater Wealth To All Tunisians*, Report No. 86179-TN.

[2] See World Bank (2011). *Program Document: Governance and Opportunity DPL*. June 2011. Report N.61627-TN.

competition increase in ICT sector, Public Private Partnerships); (ii) reinforcing financial sector development and stability (launch of a full audit of public banks; tighter prudential regulation; development of microfinance and private equity sectors); (iii) increasing inclusion and to improve quality and strengthen accountability in social sectors (reforming the National Employment Fund by consolidating and rationalizing work insertion programs, facilitating NGOs participation in the selection of public works programs, and introducing an M&E system; establishing a certification and accreditation agency for higher education and for health sector institutions; improving social policy targeting systems); and (iv) improving transparency, accountability, and public participation in policy making (clarify the implementation procedures related to the public access to information held by public bodies, including statistics; increasing transparency of the budget, by disseminating key information during the preparation; simplifying administrative controls; creating an anti-corruption judicial Authority to ultimately replace the anti-corruption investigation commission).

Progress on this ambitious program has been at times hampered by political and security developments, but is altogether satisfactory. The program further paves the way for a medium-term reform effort that can be undertaken at the end of the transition. The specific policies underpinning the program received broad support across the political spectrum, as well as amongst an array of civil society and private sector stakeholders.

The program is being implemented in the dual context of positive political developments, notably with the successful organization of parliamentary elections in October 2014, and of a challenging macroeconomic situation. While the Tunisian economy has continued to recover from the 2011 recession, growth weakened in 2013, and remained weak for most of 2014. The recovery in FDI inflows and tourism receipts has not accelerated despite the positive political developments as investors continue to wait for the end of the political cycle and isolated security incidents have deterred a rebound in tourism. Following a period of expansionary fiscal and monetary policy between 2011 and 2013, the authorities have gradually tightened their policy stance, thereby creating a satisfactory macroeconomic framework for the proposed operation. To support its macroeconomic policies, Tunisia signed a stand-by agreement (SBA) with the IMF in June 2013, for a total amount of US$1.7 billion over a 24 months period. The IMF has successfully concluded the first four reviews of the program between January 2014 and September 2014. The successful completion of the fifth review is imminent.

The proposed Third Governance, Opportunities and Jobs DPL is part of a package of support being prepared in close consultation with the African Development Bank (AfDB) and the European Union (EU). Preparatory missions have been held jointly. Also, the program has been closely coordinated with the International Monetary Fund.

IV. Tentative Financing

Source:		(US$m.)
Borrower/Recipient		0
International Bank for Reconstruction and Development		500 (two tranches)
Others (specify)		0
	Total	500

V. Institutional and Implementation Arrangements

The responsibility for coordinating the implementation of the program in Government rests with the Ministry of Economy and Finance. The Government takes the lead in monitoring progress in implementation of this operation. Given the importance and the visibility of the program, the Prime

Minister's office and the Central Bank are also closely involved in the monitoring of the program design and implementation.

Regular supervision is undertaken by the Bank to continue providing policy advice and technical assistance to the institutions involved in the implementation of the program of reform, notably thanks to its staff based in the field. The Bank will continue to maintain continuous dialogue with relevant government ministries and will conduct regular reviews in close collaboration with other partners. Supervision by the Bank (and associated donors) is organized with a broad and inclusive approach, including the implementation follow up and assessment of measures and results of the forms supported as part of previous operations.

The monitoring and evaluation of the program and its expected results will be based on the government regular monitoring and evaluation (M&E) activities. The Bank and other development partners will continue to provide support to the government to strengthen M&E, improve data quality and management and enhance capacity for using development outcomes to inform policy making.

VI. Risks and Risk Mitigation

The risks to this operation relate to:

(i) *Risks related to potential uncertainty arising from political or security tensions*: as described above, the political tensions experienced in 2013, notably following the assassination of two political leaders had an impact on the pace of implementation of the reforms program supported by the series. While the political situation has improved markedly in 2014, and the recent legislative elections have been a full success with respect to their orderly organization, transparency and fairness of all parties, the political tensions may again rise in the run-up to, and aftermath of the elections. A benevolent international framework, including financial and political support from the international community and outreach in the media, will help mitigate these political risks. Also, consultations on the reform program have been held with the main political parties and the program is enjoying the support of a majority of political stakeholders.

(ii) *Risks related to the uncertainty of the macroeconomic outlook*: In addition to domestic social tensions, uncertainty about the economic outlook related to the impact of the Eurozone crisis and the stabilization process in Libya, as well as the pressures on the fiscal and external accounts, all pose significant risk to economic and political developments in Tunisia. Lower growth and additional pressure in the labor market could lead to renewed social tensions and reinforce a sense of lack of economic opportunity. The negative shock on the tourism sector and the sensitivity of the exporting sectors to growth variations in Europe both translate into higher credit and liquidity risks in the banking sector. These risks will further aggravate the already relatively tight liquidity and weak asset quality of the banking sector. To mitigate these risks, the authorities have launched various initiatives to improve public investment execution, notably in lagging regions and have scaled-up some social interventions (cash transfers to the most vulnerable households). The Government has also started to devise mechanisms to improve the targeting of food and fuel subsidies. The measures supported by this operation further aim to help reinforce the banking sector and reduce the risks of financial instability. A continuation of the satisfactory implementation of the SBA with the IMF will contribute to restore confidence among international investors about the soundness of the macroeconomic framework, and the continuity in the implementation of reforms during the remainder of the transition, notably with respect to financial sector strengthening.

(iii) *Risks related to the institutional capacity for reform deliver:* The actual implementation of the reforms supported in 2011 and 2012 has proven difficult and longer than expected, partly as a result of implementation capacity shortages, but mainly on account of the negative impact of the political uncertainty on the administration's resolve to carry out some of the reforms in a timely fashion. The Bank's technical assistance will help bridge the implementation capacity gaps, notably with respect to the financial sector reforms (bank restructuring, application of the bankruptcy law, and operation of the asset management company) and sector reforms (telecommunications). Technical support from other partners will contribute to mitigate the risk (notably the IMF in the area of financial sector reforms or the EU with respect to competition policy). The new government will enjoy a more predictable policy horizon and thereby be able to establish a clear reform implementation roadmap that will steer the priorities of the administration.

(iv) *Risks related to stakeholder resistance*. Some key stakeholders will oppose the reforms, notably if they hold a dominant position on the markets or if they extract undue rents that are challenged by the reforms. The Bank's analytical work, chief among which the *Development Policy Review*, highlights risks of capture and subsequent disconnect between reforms on paper and real change on the ground for citizens and firms. Many of the reforms supported by the GOJ DPL series aim at empowering citizens to obviate this risk, and the Bank is itself investing considerable effort in awareness-raising and consensus-building. To this end, it has engaged in a broad-based consultation and dissemination effort of the DPR's findings and recommendations. The Bank is also supporting a public awareness project, using local media, so as to spur and feed the national debate on key social and economic issues faced by Tunisia.

VII. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

The poverty reduction impact of the policies supported by the DPL, namely enhancing growth and jobs creation in the medium term, putting in place systems to improve the quality of service delivery, and strengthening governance and access to information are expected to have positive social and poverty impacts. The specific policies supported by this DPL are not expected to have negative distributional and social impacts.

Environment Aspects

The reforms supported in this DPL operation are not expected to have significant positive or negative effects on the environment, forest and other natural resources. The DPL supports policy actions that create the enabling environment to support job creation, employment and poverty reduction, and which by themselves do not have an environmental impact. It is expected, however, that regular private and public investment activities which may result from such policy actions could have impacts on the environment. Nevertheless it is not expected that there will be a need to introduce special measures since all activities to be carried out are subject to the Tunisian legal framework for the protection of the environment. Thus, neither specific environmental studies nor environmental impact management measures are anticipated.

VIII. Contact points

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