Tunisia

Highlights

- **Growth is recovering but the outlook is modest amid extremely challenging conditions.** Real gross domestic product (GDP) growth picked up slightly in the first half of 2024, following a slowdown in 2023. The country's fiscal and external performances showed some improvement, despite a lack of progress on approving a new programme with the International Monetary Fund (IMF).
- **Tunisia has entered a strategic and comprehensive partnership with the European Union (EU).** The agreement should help the authorities promote macroeconomic stability, improve the business environment, boost growth, investment and trade, and support the green transition.
- **Key reforms are advancing.** Recent reform measures include an enhancement of the energy-sector regulatory framework, improvements in road quality, the partial liberalisation of foreign-exchange transactions and the restructuring of public banks. The state's footprint is large, however, and a recent law allowing exceptional fiscal monetisation in 2024 could undermine central bank independence.

Key priorities for 2025

- **Continued fiscal consolidation is a top priority to improve Tunisia's public finances.** This entails committing to the country's medium-term fiscal framework to contain the deficit and public debt. Efforts should be made to improve revenue mobilisation, as well as reduce the public wage bill, interest payments and subsidies.
- **Accelerating the green transition and improving the resilience of the agricultural sector are necessary.** These are important to reduce Tunisia's dependence on energy and food imports. Priorities should include enhancing the energy sector's regulatory framework and facilitating private-sector investment to scale up renewables. Moreover, continued efforts to strengthen food security and boost the resilience of the agricultural sector to climate shocks are crucial.
- **Reducing the state's role in the economy and improving the business environment are essential.** This will mean restructuring public enterprises, eliminating restrictions, improving operational efficiency and levelling the playing field.

Main macroeconomic indicators (per cent)

	2020	2021	2022	2023	2024 proj.
GDP growth	-8.6	4.6	2.7	0.0	1.2
Inflation (average)	5.6	5.7	8.3	9.3	7.4
Government balance/GDP	-9.4	-7.7	-7.6	-7.1	-6.6
Current account balance/GDP	-5.9	-6.0	-8.6	-2.5	-3.5
Net FDI/GDP [neg. sign = inflows]	-1.4	-1.1	-1.4	-1.3	-1.3
External debt/GDP	98.7	87.7	87.1	83.0	na
Gross reserves/GDP	21.4	18.5	17.0	17.8	na
Credit to private sector/GDP	71.0	76.0	75.0	69.4	na

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Macroeconomic developments and policy response

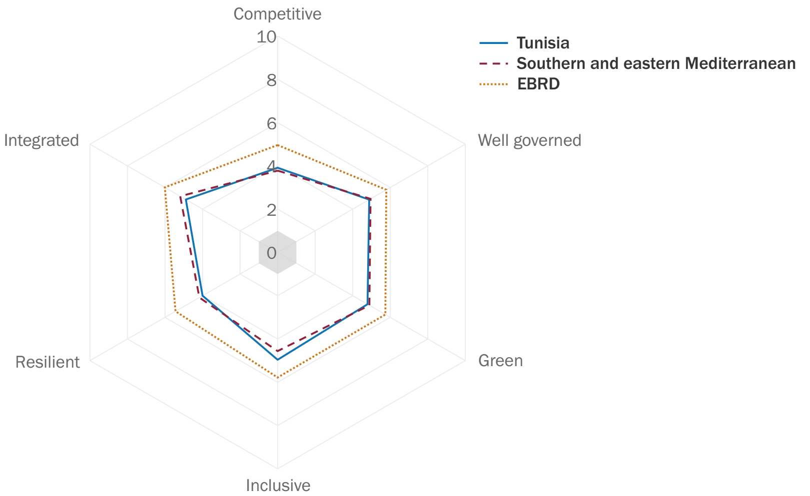
Growth recovered slightly in 2024, but economic activity remains largely subdued. Real GDP growth was close to zero in 2023, before increasing slightly to 0.6 per cent year on year in the first half of 2024. Although tourism, financial services and some industrial sectors recovered, a severe drought and a contraction in agriculture, along with declines in the mining and construction sectors, dragged on growth. Inflation dropped to a 30-month low of 7 per cent in July 2024, supported by a cumulative 175 basis-point tightening of the central bank's policy rate. Unemployment increased slightly to 16 per cent in the second quarter of 2024, remaining higher among women (21 per cent) and youth (41 per cent).

Public finances remain constrained, although the country's fiscal performance has improved. Tunisia's fiscal deficit narrowed to 7.1 per cent of GDP in 2023, driven by a rationalisation of wage and subsidy spending, despite a decline in tax revenues. Meanwhile, public debt increased to around 80 per cent of GDP. In the first half of 2024, the state budget recorded a surplus, driven by higher revenues. The government is targeting a decline in the deficit to 6.6 per cent of GDP in 2024, largely thanks to enhanced revenue mobilisation and lower basic goods subsidies (as weather conditions improved and food prices continued to gradually ease in the first half of 2024). Nevertheless, interest spending and public wages are projected to increase. Because of these fiscal pressures, the government has embarked on a medium-term fiscal consolidation plan to further contain the public deficit by undertaking tax reforms, rationalising fuel consumption, incentivising renewable energy investments and usage (including by raising the fuel/carbon tax), and consolidating the public-sector wage bill.

The current account and foreign reserves have proved resilient, but external vulnerabilities remain. The current account deficit stood at 1.4 per cent of GDP in the first half of 2024 and is expected to reach 3.5 per cent of GDP for the full year, despite increased tourism and remittances. Imports contracted (due to lower commodity prices), while mechanical, electric and olive oil exports improved. International reserves continued to increase (covering nearly four months of imports in August 2024), despite several major debt repayments. After credit-rating downgrades in 2023, Moody's raised Tunisia's outlook to stable from negative in March 2024 on the back of its better current account performance and continued access to bilateral and multilateral external funding (including from Afreximbank, the African Development Bank, Algeria, the European Union, Saudi Arabia and the World Bank). In September 2024, Fitch upgraded Tunisia's Long-Term Foreign-Currency Issuer Default Rating to CCC+ from CCC.

The outlook for 2024 is modest, with several external and domestic vulnerabilities. Growth is expected to gather pace to 1.2 per cent in 2024 and 1.8 per cent in 2025. The restrictive business environment, tighter monetary conditions, and fiscal and external pressures continue to weigh on economic activity, however. Moreover, the law allowing the monetisation of the fiscal deficit up to TND 7 billion (€2 billion) in 2024 poses a risk to central bank independence and could fuel inflation. Tailwinds include easing inflationary pressures, the stronger current account and continued fiscal consolidation. Despite the large financing gap and slow progress on agreeing an IMF-supported programme, Tunisia is expected to be able to service all of its external debt, thanks to solid reserves and key economic drivers, notably tourism and exports.

Assessment of transition qualities (1-10)



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Structural reform developments

Tunisia has embarked on a strategic partnership with the EU to promote macroeconomic stability and structural reform. In June 2024, the country launched the "Investments in Tunisia" initiative, in cooperation with the EU, to support its National Reform Programme. The initiative will mobilise over €3 billion through more than 120 projects to improve: (i) the investment climate, (ii) sustainable and digital infrastructure, and (iii) access to finance and support for micro, small and medium-sized enterprises (MSMEs). This followed the agreement of a comprehensive partnership package in July 2023 to promote macroeconomic stability, boost economic growth, investment and trade, improve the business climate, support the green transition and combat illegal migration.

Efforts are under way to enhance the regulatory framework in the energy sector and promote renewable energy investments. Recent measures include: (i) the submission for approval in April 2024 of a draft bill to establish an independent electricity regulator, (ii) plans to revise the tariff structure to authorise projects with various production capacities (including SMEs) to sell electricity to the Tunisian Electricity and Gas Company, and (iii) plans to enhance the legal framework to facilitate the production, export and transport of electricity and green hydrogen. If implemented, these reforms should facilitate private investment in the renewable energy sector. Moreover, several agreements have been signed with international investors to launch five solar energy projects with a total generation capacity of 500 megawatts in 2025.

Tunisia has launched several infrastructure projects to enhance regional integration and reduce economic disparities. In March 2024, the country launched the Economic Development Corridor project, aimed at enhancing the quality of road infrastructure linking the Kasserine, Sidi Bouzid and Sfax governorates and facilitating SME access to finance in the region by capitalising the Deposit and Consignment Fund for impact investment. The project is expected to enhance social inclusion and regional integration, as well as open new trade routes with Libya and Algeria. The strategic corridor will be supported by more than €400 million of funding from the World Bank and the European Investment Bank. Moreover, the government will develop a new bridge in the port city of Bizerte, supported by a €245 million financing package from the European Investment Bank and the African Development Bank, to boost the region's economic activity and trade by enabling access to the Mediterranean port of Bizerte.

Several initiatives are under way to enhance food security and improve the cereal sector's resilience to external and climate shocks. The Inclusive and Sustainable Development of the Cereal Sector project, launched in July 2023, aims to improve food security and self-sufficiency through upstream and downstream interventions in the cereals supply chain. Efforts are expected to benefit farmers by: (i) increasing productivity, (ii) modernising storage capacity, (iii) reducing transport costs and (iv) securing emergency supplies. The project will be supported by around €80 million from the African Development Bank and guaranteed by the United Kingdom under the Room to Run Sovereign risk-sharing arrangement. In addition, the World Bank will support the cereals sector with close to €300 million in financing to the Emergency Food Security Response project, which will streamline wheat imports and support small dairy and wheat producers by providing barley and climate-resilient seeds.

Foreign-exchange transactions are gradually being liberalised. In March 2024, the government approved a new foreign-exchange bill, which is currently subject to parliamentary review. If passed, it would partially liberalise foreign-exchange transactions, simplify regulations and allow for greater digitalisation of financial transactions. The new law is expected to allow certain residents to hold foreign-currency accounts, enabling them to invest, purchase assets and pay expenses abroad. It will also redefine the concept of residency, enabling foreign investors to avoid restrictions by maintaining permanent non-resident status. Some details of the eligibility criteria are still unclear, however.

The government will embark on a process to reform state-owned banks. A ministerial committee will be formed in coordination with the central bank to oversee an in-depth audit of financially distressed state-owned banks and to enhance their capital adequacy and expenditure management. Once a reform plan is proposed, banks will be allowed an implementation period of three months.