TUNISIA ECONOMIC MONITOR

Renewed energy to the economy

Spring 2024
Tunisia
Economic Monitor

Renewed Energy to the Economy

Spring 2024

Middle East and North Africa Region
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ACKNOWLEDGEMENTS

The Tunisia Economic Monitor (TEM) is a report that provides information on recent economic developments and policies in Tunisia, as well as the country’s economic outlook and challenges to its development. The report is aimed at a diverse audience, including policy makers, business leaders, financial market actors, and analysts and professionals working on or in Tunisia. It is produced by the North Africa and Middle East department of the World Bank Group’s Macroeconomics, Trade and Investment (MTI) global practice.

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The report is authored by a team led by Massimiliano Cali (Senior Economist, MTI) and Mohamed Habib Zitouna (Consultant, MTI). The team also includes Riadh Ammari (Communications Specialist, External Affairs), Asma Bouraoui Khouja (Senior Operations Officer, Tunisia) and Fatma Marrakchi Charfi (Consultant, MTI), and — for part B — Amira Klibi (Senior Energy Specialist, Energy) and Moez Cherif (Lead Energy Economist, Infrastructure).

The report was prepared under the direction of Jesko Hentschel (Country Director, Maghreb), Eric Le Borgne (Practice Manager, MTI), Alexandre Arrobbio (Resident Representative, Tunisia), and Abdoulaye Sy (Lead Economist, MTI), with administrative support from Jawhar Abidi (Consultant, MTI).

The opinions and conclusions expressed in this report are those of the World Bank staff and do not necessarily represent the views of members of the World Bank Board of Directors or the countries they represent.

For information on the World Bank and its activities in Tunisia, please visit: https://www.worldbank.org/en/country/tunisia or https://www.albankaldawli.org/ar/country/tunisia (Arabic). For questions or comments on the content of this publication, please contact Massimiliano Cali (mcali@worldbank.org) or Eric Le Borgne (eleborgne@worldbank.org).

The deadline for input and forecast preparation is April 5th, 2024.
# LIST OF ACRONYMS

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<th>Acronym</th>
<th>Definition</th>
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<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>CAD</td>
<td>Current Account Deficit</td>
</tr>
<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
</tr>
<tr>
<td>SOEs</td>
<td>State-Owned Enterprises</td>
</tr>
<tr>
<td>CCDR</td>
<td>Climate Change Development Report</td>
</tr>
<tr>
<td>US</td>
<td>United States</td>
</tr>
<tr>
<td>OdC</td>
<td>Office des Céréales</td>
</tr>
<tr>
<td>TD</td>
<td>Tunisian Dinar</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>CBT</td>
<td>Central Bank of Tunisia</td>
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<tr>
<td>STEG</td>
<td>Société Tunisienne de L’électricité et du Gaz</td>
</tr>
<tr>
<td>STIR</td>
<td>Société tunisienne des industries de raffinage</td>
</tr>
<tr>
<td>CPI</td>
<td>Consumer Price Index</td>
</tr>
<tr>
<td>VAT</td>
<td>Value-Added Tax</td>
</tr>
<tr>
<td>UGTT</td>
<td>Union Générale Tunisienne du Travail</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>INS</td>
<td>National Institute of Statistics</td>
</tr>
<tr>
<td>Mtoe</td>
<td>Million Tonnes of Oil Equivalent</td>
</tr>
<tr>
<td>MW</td>
<td>Megawatt</td>
</tr>
<tr>
<td>GW</td>
<td>Gigawatt</td>
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<tr>
<td>TD/TOE</td>
<td>Tunisian Dinar/Tonnes of Oil Equivalent</td>
</tr>
<tr>
<td>SDDP</td>
<td>Stochastic Dual Dynamic Programming</td>
</tr>
<tr>
<td>UNDP</td>
<td>United Nations Development Programme</td>
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<td>BAU</td>
<td>Business As Usual</td>
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EXECUTIVE SUMMARY

Tunisia’s already modest economic recovery came to an abrupt halt in 2023 amidst a severe drought, tight financing conditions, and a modest pace of reform. With this slowdown, the Tunisian economy in 2023 was still below its pre-Covid level, marking one of the slowest recoveries in the Middle East and North African region. Agriculture was the main driver of the 2023 economic slowdown, declining by 11 percent as the drought forced the government to introduce irrigation restrictions. This highlights the urgency for Tunisia to adapt to climate change.

The growth slowdown amplifies the challenges Tunisia faces in covering its significant external financing needs despite an improving external balance. Boosted by favorable changes in international prices, Tunisia’s merchandise trade deficit improved in 2023, declining to 10.8 percent of GDP from 17.5 percent in 2022. At the same time, the energy deficit widened despite more favorable prices, continuing to account for the bulk of the merchandise trade deficit. The narrowing trade deficit along with the rebounding of tourism exports lowered the current account deficit (CAD) in 2023. While the lower CAD eases the pressure on external financing needs, these remain significant, especially due to the burdensome debt service.

Tunisia continues to depend on sovereign lending to finance its external needs, as it cannot access international capital markets, and Foreign Direct Investment (FDI) and portfolio flows remain limited. These limited capital inflows are consistent with a high degree of controls on capital outflows, which the government is currently planning to revise.
Tunisia’s increasing reliance on domestic sources to fill the external financing gap may put pressure on the Dinar, on prices, and on the domestic banking system

With declining external financing, the government has turned increasingly to monetary financing to cover external needs, notably through the use of foreign reserves from the Central Bank. While both the Dinar and foreign reserves have proven resilient so far, the continued use of monetary financing of the external needs could have adverse impacts on currency and price stability.

The reimbursement of the latest Eurobonds consolidated the recent hike in Tunisia’s bond prices, which reflects the perceived reduced risk of default on public external debt to private markets in the short term. The drying up of external financing sources along with the rising public debt have resulted in the growing role of the domestic banking system (along with monetary policy) for debt financing. At the same time the sustained use of local funding to finance the public debt continues to crowd out credit to the economy.

Shortages of basic products persist amidst import compression and declining agricultural production

As external financing conditions remain tight, imports continue to be compressed particularly for those products imported by increasingly indebted state-owned enterprises (SOEs). This import compression along with the drop in domestic agriculture production translated into protracted shortages of some basic products, such as flour, dairy products, sugar, rice, and coffee.

Inflation moderated from the record levels of early 2023 but it remains elevated, particularly for food

Inflation started to moderate since the peaks of February 2023 on the back of lower global prices and weak domestic demand. Inflation is now lower than the nominal interest rate for the first time since July 2021. However, inflation is still high, particularly for food, as the drought and import compression reduced the supply in domestic food markets. The recent government measures to contain food prices focused on hoarding behavior and enhancing price controls but food inflation remains elevated. New analysis shows that most of the recent inflation episode is driven by rising profits and import prices, pointing to the important role of competition and trade policy to fight inflation.

The budget continues to be under pressure as the low growth affects tax revenues

The budget deficit was stable in 2023 (6.7 percent of GDP) following a more modest increase in tax revenues than expected, dragged by the slowdown in economic growth, and the moderate increase of public expenditures. The latter was the product of rising transfers and interest payment, moderated by relatively contained wage bill growth and stalled capital expenditures. Reversing the decline in public capital expenditures by re-orienting less productive recurrent expenditures continues to be key to revive economic growth.

We expect a moderate growth rebound in 2024-25 assuming drought conditions ease, but economic prospects remain uncertain

After the significant slowdown in 2023, we expect a moderate rebound of the economy with a 2.4 percent growth rate in 2024, and a 2.3 percent growth in 2025–26. These growth forecasts are subject to significant downside risks related to the external financing conditions, the evolution of the drought and the pace of fiscal and pro-competition reforms. Tunisia’s public finance and external account will remain precarious in the absence of sufficient external financing. The financing of the deficits will require a significant
scale-up of the external financing in the face of the heavy debt reimbursement schedule. If the pace of reforms and the level of financing remain sufficient, we project growth to be maintained over the medium run along with some stabilization of the macro and fiscal imbalances.

Accelerating the transition of the power sector to renewable energy could help address Tunisia’s macro-fiscal challenges and boost the economy

As Tunisia’s macro-fiscal challenges deepen, the government’s target of generating 35 percent of energy from renewable sources by 2030 becomes even more important. The country has grown more dependent on fossil fuel imports, which undermine the sustainability of the current account. Eventually, if this dependence were to continue, Tunisia’s current account deficit and financing conditions may limit its ability to import the energy it needs to meet its growing demand, thus stifling economic activity. This dependence on fossil fuels weighs heavily also on the fiscal balance given the high costs of fossil energy generation. By increasing the demand for energy, global warming is exacerbating the challenges of energy dependence and undermining the security of energy supply.

In fact, Tunisia’s energy sector does not have to depend on fossil fuels as the country has a rich untapped renewable energy potential. Renewable energy could significantly reduce the cost of electricity production especially in the context of high and volatile international energy prices. Exploiting Tunisia’s renewable energy potential is even more important in light of the ongoing development of the electric connection between Tunisia and Italy. The recent World Bank’s Tunisia Climate Change and Development Report (CCDR) shows that renewable energy generation is projected to play a dominant role in power generation in Tunisia as it is the least cost energy source. The benefits of expanding renewable energy production would extend to the whole of economy, with significant gains in terms of economic growth already by 2030.

The CCDR estimates large investment needs to enable this green energy transition (around US$ 27–35 billion by 2050). The bulk of these investments are expected to be covered by the private sector given the significant cost advantage of renewables over fossil fuel in Tunisia. However, an adequate regulatory framework should be in place to favor such investments. Strengthening the regulatory framework would also accelerate Tunisia’s ambitious renewable energy development program, which would move the country closer to its 2030 renewable target.
La reprise économique — déjà limitée — de la Tunisie s’est fortement ralentie en 2023 dans un contexte de sécheresse sévère, de conditions de financement strictes et d’un rythme de réformes peu soutenu.

La reprise économique — déjà limitée — de la Tunisie s’est fortement ralentie en 2023, dans un contexte de grave sécheresse, de conditions de financement strictes et de un avancement peu soutenu de la mise en œuvre des réformes. Avec ce ralentissement, l’économie tunisienne en 2023 était encore en dessous du son niveau d’avant Covid, marquant l’une des reprises les plus lentes de la région du Moyen-Orient et de l’Afrique du Nord. L’agriculture a été le principal frein à la croissance économique en 2023, avec un déclin de 11 pour cent alors que la sécheresse a contraint le gouvernement à introduire des restrictions à l’irrigation. Ce contexte met en évidence l’urgence pour la Tunisie de s’adapter au changement climatique.

Par ailleurs, la faiblesse de la demande intérieure et l’assainissement budgétaire, semblent avoir contribué à aggraver les pertes liées à la sécheresse. En effet, le déclin des secteurs de la construction et du commerce semble avoir annulé une partie des gains réalisés sur les marchés d’exportation, en particulier dans le tourisme. Le ralentissement de la croissance — en particulier dans les secteurs à forte intensité de main-d’œuvre — s’est traduit par une hausse du chômage et une baisse du taux de participation au marché du travail.

Le ralentissement de la croissance amplifie les défis auxquels la Tunisie est confrontée pour couvrir ses besoins de financement extérieur, qui demeurent importants malgré une amélioration du solde de la balance courante.

Stimulé par l’évolution favorable des prix internationaux, le déficit commercial de la Tunisie s’est amélioré en 2023, passant à 10,8 pour cent du PIB contre 17,5 pour cent en 2022. Alors que sur la même période, le déficit énergétique s’est creusé malgré des prix plus favorables, continuant de représenter l’essentiel du déficit commercial. L’amélioration du déficit commercial ainsi que le rebond des exportations touristiques ont réduit le déficit du compte courant (DCC) en 2023. Même si la baisse du DCC atténue la pression sur les besoins de financement extérieur, ceux-ci restent importants, notamment en raison de l’importance du service de la dette. La Tunisie continue de dépendre des prêts souverains pour financer ses besoins extérieurs, car elle ne peut accéder aux marchés de capitaux internationaux sachant que les investissements directs étrangers (IDE) et les flux de
Les entrées limitées de capitaux sont en cohérence avec le degré élevé de contrôle des sorties de capitaux, que le gouvernement prévoit actuellement de réviser.

La dépendance croissante de la Tunisie à l’égard des sources de financement intérieures pour combler le déficit de financement extérieur pourrait exercer une pression sur la valeur du dinar, sur les prix et sur le système bancaire national.

Face à la diminution des financements extérieurs, le gouvernement s’est tourné principalement vers le financement monétaire pour couvrir les besoins extérieurs, en utilisant les réserves de change de la Banque Centrale. Même si le dinar et les réserves de change ont jusqu’à présent fait preuve de résilience, le recours continu au financement monétaire pour répondre aux besoins extérieurs pourrait avoir des effets négatifs sur la stabilité de la monnaie et des prix.

Le remboursement des dernières euro-obligations a consolidé la récente hausse des prix des obligations tunisiennes, qui reflète la perception d’un risque réduit de défaillance sur la dette extérieure publique envers les marchés privés. Le tarissement des sources de financement externes ainsi que l’augmentation de la dette publique ont amené les autorités à plus solliciter le système bancaire national (en conjonction avec la politique monétaire) dans le financement de la dette. Alors que, le recours soutenu aux financements locaux pour financer la dette publique continue d’éviter les crédits à l’économie.

Les pénuries de certains produits de base persistent dans un contexte de compression des importations et de baisse de la production agricole

Alors que les conditions de financement extérieur restent serrées, les importations continuent d’être compressées, en particulier pour les produits importés par des entreprises publiques (EP) de plus en plus endettées. Cette compression des importations, conjuguée à la baisse de la production agricole nationale, s’est traduite par des pénuries prolongées de certains produits de base, tels que la farine, les produits laitiers, le sucre, le riz et le café.

L’inflation s’est atténuée par rapport aux niveaux records du début 2023, mais elle demeure élevée, en particulier dans le secteur alimentaire.

L’inflation a commencé à ralentir depuis les sommets atteints en février 2023, en raison de la baisse des prix mondiaux et de la faiblesse de la demande intérieure. L’inflation est désormais inférieure au taux d’intérêt nominal pour la première fois depuis juillet 2021. Cependant, l’inflation reste élevée, en particulier dans le secteur alimentaire, car la sécheresse et la compression des importations ont réduit l’offre sur les marchés alimentaires intérieurs. Les récentes mesures gouvernementales visant à contenir les prix des produits alimentaires se sont concentrées sur la lutte contre la monopolisation et le renforcement du contrôle des prix, mais l’inflation des produits alimentaires reste élevée. Une nouvelle analyse par la Banque Mondiale montre que l’essentiel du récent épisode d’inflation est dû à la hausse des bénéfices et des prix des importations, soulignant le rôle important de la concurrence et de la politique commerciale dans la lutte contre l’inflation.

Le budget reste sous pression car la faible croissance affecte les recettes fiscales

Le déficit budgétaire est resté stable en 2023 (6,7 pour cent du PIB) suite à une augmentation des recettes fiscales plus modeste que prévu, entraînée par le ralentissement de la croissance économique et l’évolution modérée des dépenses publiques. Cette dernière est la résultante de la hausse des transferts et des paiements d’intérêts, mais qui est atténuée par une croissance relativement contenue de la masse salariale et par une stagnation des dépenses d’inves-
tissement. Inverser la baisse des dépenses publiques d'investissement en réorientant les dépenses récurrentes moins productives reste essentiel pour relancer la croissance économique.

Nous prévoyons un rebond modéré de la croissance en 2024-26, en supposant que les conditions de sécheresse s’atténuent, mais les perspectives économiques restent incertaines.

Après le ralentissement significatif de 2023, nous prévoyons un rebond modéré de l’économie avec un taux de croissance de 2,4 pour cent en 2024 et de 2,3 pour cent en 2025-26. Ces prévisions de croissance sont soumises à des risques baissiers importants liés aux conditions de financement extérieur, à l’évolution de la sécheresse et au rythme des réformes budgétaires et pro-concurrentielles. Les finances publiques et l’équilibre extérieur de la Tunisie resteront précaires en l’absence de financement extérieur suffisant. Le financement des déficits nécessitera une augmentation significative du financement extérieur face au lourd calendrier de remboursement de la dette. Si le rythme de mise en œuvre des réformes et le niveau de financement sont suffisants, nous prévoyons un maintien de la croissance à moyen terme ainsi qu’une certaine stabilisation des déséquilibres macroéconomiques et budgétaires.

Accélérer la transition du secteur électrique vers les énergies renouvelables pourrait aider à relever les défis macro-budgétaires de la Tunisie et à stimuler l’économie.

Au fur et à mesure que les défis macro-budgétaires de la Tunisie s’accentuent, l’objectif du gouvernement de produire 35 pour cent d’énergie à partir de sources d’énergie renouvelable d’ici 2030 devient encore plus important. Le pays est devenu plus dépendant des importations de combustibles fossiles, ce qui compromet la viabilité du compte courant. À terme, si la dépendance aux combustibles fossiles se poursuit, le déficit du compte courant de la Tunisie et les conditions de financement pourraient limiter sa capacité à importer l’énergie dont elle a besoin pour répondre à la demande croissante, étouffant ainsi l’activité économique. Cette dépendance aux combustibles fossiles pèse également lourdement sur l’équilibre budgétaire étant donné les coûts élevés de la production d’énergie fossile. En augmentant la demande d’énergie, le réchauffement climatique exacerbe les défis de la dépendance énergétique et compromet la sécurité de l’approvisionnement énergétique.

En fait, le secteur énergétique tunisien pourrait ne plus dépendre des combustibles fossiles car le pays dispose d’un riche potentiel d’énergies renouvelables inexploité. Les énergies renouvelables pourraient réduire considérablement le coût de la production d’électricité, en particulier dans le contexte de prix internationaux de l’énergie élevés et volatils. L’exploitation du potentiel d’énergies renouvelables de la Tunisie est encore plus importante à la lumière du développement en cours de la connexion électrique entre la Tunisie et l’Italie. Le récent Rapport sur le Climat et le Développement en Tunisie (CCDR) de la Banque mondiale montre que la production d’énergie renouvelable devrait jouer un rôle dominant dans la production d’électricité en Tunisie, car il s’agit de la source d’énergie la moins coûteuse. Les avantages de l’expansion de la production d’énergies renouvelables s’étendraient à l’ensemble de l’économie, avec des gains significatifs en termes de croissance économique dès 2030.

Le CCDR estime que d’importants investissements seront nécessaires pour permettre cette transition énergétique verte (environ 27 à 35 milliards de dollars américains d’ici 2050). La majeure partie de ces investissements pourrait être couverte par le secteur privé étant donné l’avantage significatif en termes de coûts par rapport aux combustibles fossiles en Tunisie. Cependant, un cadre réglementaire adéquat devrait être mis en place pour favoriser de tels investissements. Le renforcement du cadre réglementaire accélérerait également l’ambitieux programme de développement des énergies renouvelables de la Tunisie, ce qui rapprocherait le pays de son objectif de 2030 en matière d’énergies renouvelables.
تعترف الاقتصاد الاقتصادي المتواضع في تونس بشكل مفاجئ في عام 2023 وسط جفاف شديد، ظروف مالية ضيقة وtworzyć منخفضة من الإصلاحات.

كاد الاقتصاد الاقتصادي المتواضع في تونس أن يتوقف في عام 2023، وظروف مالية ضيقة، وつつيرة منخفضة. أدّى هذا التباطؤ إلى جعل الاقتصاد التونسي أقل من مستوى قبل جائحة كوفيد، مسجلًا واحدًا من أبطأ حالات الانتعاش في منطقة الشرق الأوسط وشمال أفريقيا.

وانخفض نمو القطاع الفلاحي، وهو السبب الرئيسي لهذا التباطؤ في المائة، بأمر حكومي في عام 2023، بنسبة الإقتصادي في عام 2023؛ فرض قيود على الري، وهو ما يؤكد الحاجة الملحّة لتونس للاستثمار في القطاع الفلاحي. كما أن ضعف الطلب المحلي وضغط الوضع المالي العام قد أدى إلى زيادة الخسائر المتصلة بالجفاف.

إن اعتماد تونس المتزايد على المصادر المحلية لسد فجوة التمويل الخارجي قد يضع ضغوطاً على الدينار والأسعار والقطاع المالي المحلي.

تعدّد التحديات التي تواجهها تونس في تغطية احتياجات كبيرة من التمويل الخارجي على الرغم من تحسن التوزانات الإقتصادية في عام 2023، وذلك بفضل التغيرات المناسبة في السياسة النقدية، حيث ارتفعت إلى 10.8 في المائة من الناتج المحلي الإجمالي في 2022، مقابل 7.5 في المائة في عام 2021. في الوقت نفسه، ارتفع الدين العام، وظلت الأسعار باباً في الفوائد على الرغم من التطور المالي للأداء، وظلّت المؤشرات الاقتصادية المهمّة متداولة في تونس.
بمجرد التضخم في الأفلاس منذ فبراير 2023 على خلفية ازدياد الأسعار العالمية وضعف الطلب المحلي التضخم الآن أقل من معدل الفائدة في عام 2021. ومع ذلك، لا يزال التضخم مرتفعًا، ولا سيما بالنسبة للأغذية، حيث أن التضخم الغذائي قفز بشكل كبير أيضًا على التوالي في alanı سوق التضخم لأدوات الأسعار المستقلة في البنوك الدولية. وركزت التدابير الحكومية الأخيرة لحظر أسعار المواد الغذائية على سبل الإستراح، وتوفير رقاق الألغاز، لكن التضخم الغذائي لا يزال مرتفعًا، يظهر تحليلاً جديًا، أن معظم حلقات التضخم الأخرى مدفوعة بارتفاع الرأس وأسعار الورادات، مما يرزق الطلب المحلي. يرجح تدابير التضخم في الماضي بارتفاع الأجور والنمو في المائة من الناتج في برنامج التضخم الذي تشير إليه وتوقعات النمو هذه. ومع ذلك، لا يزال النقص في المنتجات الأساسية قائما في ظل تقلص الورادات وانخفاض الإنتاج الفلاحي.

يتم وجود استمرار ضيق شروط التمويل الخارجي، لا تزال الورادات مضغوطة، لا سيما بالنسبة للمنتجات المستوردة من قبل الشركات المعمولية التي تزداد مدروبتها. هذا الضغط على الورادات جنبًا إلى جنب مع التضخم الإنتاجي الداخلي الذي يوة نحو تقلص طول الطلب. في بعض المنتجات الأساسية، مثل الدقيق ومنتجات الألبان والسكر والأرز، لا يزال التضخم غير محدود.

ولا تزال الميزانية تعرض لضغوط لأن النمو المضارع يؤثر في المديح الجبائي.

كان حجم الواردات المستقر في عام 2023 (6.7% من المائة من الناتج المحلي الإجمالي)، بعد زيادة مفتوحة في الدفعة الاقتصادية تأثر بالواردات الفلاحية، بسبب خلق الورادات العالمية لزيادة معدل الورادات العالمية في النجوم العامة. يدأ هذا التضخم تأثير زيادة معدلات التضخم ونشاط الورادات، التي تأثر بها ضخامة الأغذية وتوقف النفقات. لذا يزال التضخم مالوري، تحتوي طبيعيًا على أدنى مستوى وذوب في الماء. صناعة النشاط الاقتصادي، وتمكنت من النمو في المائة في عام 2023، والنمو بجودة 2.4% في الورادات، وهو نسبة 2.3 في المائة في الفترة 2025-2026. وتتضمن توقعات النمو هذه مخاطر كبيرة تصل
RECENT ECONOMIC DEVELOPMENTS

1. Tunisia’s already modest economic recovery came to an abrupt halt in 2023 amidst a severe drought, tight financing conditions, and the modest pace of reform

Tunisia’s already modest economic recovery almost halted in 2023, amidst a severe drought, tight financing conditions, and the modest pace of implementing reforms. The economy grew by 0.4 percent in real terms during 2023, with a significant deterioration since the second quarter linked to the effects of the drought (figure 1). The 4th consecutive year of below average rainfall led the government to ration water usage since March. This negative shock has compounded a difficult recovery, marred by tight external financing and continued regulatory barriers to growth, such as authorizations to access many sectors, strict and discretionary controls on foreign exchange and regulatory capture of incumbents, which have not yet been addressed by reforms (see the 2022 and 2023 issues of the Tunisia Economic Monitor). This performance has widened the gap in post-Covid economic growth vis-à-vis Tunisia’s peers in the region (figure 2). In 2023 Tunisia was the only country among its regional peers with real GDP still below pre-pandemic level.

Agriculture was the main driver of the 2023 economic slowdown, as the drought exposed the deficiencies of a sector that needs to adapt to climate change. The lack of rainfall throughout 2023 aggravated the dry conditions prevailing in Tunisia over the previous 4 years, forcing the government to introduce irrigation restrictions since March. This resulted in reduced harvest and a significant loss of production. That is the case for instance for wheat, which is one of the key staples in Tunisians’ diet. The dry conditions precipitated the production losses, as the bulk of cereal production is rainfed. Hence, domestic cereal production in 2023 dropped by 61 percent compared to 2022, reaching just over 22 percent of the level in 2019.1 As a result, in 2023 agricultural value added fell by 11 percent in real terms, aggravating the declining trend since 2019 (figure 3). Had agriculture and agro-industry grown at the (modest) rate of 2022 (1.7 percent), the economy would have expanded by 1.8 percent in 2023, slightly below the 2022 rate (2.6 percent). As rainfall conditions are expected to deteriorate further in the future because

1 That is based on sales data from OdC.
of climate change, Tunisia needs to act swiftly to ensure its food security, building the resilience of agriculture as well as the water sector as a whole. To that end, some of the priority measures include: managing water demand, promoting the use of nature-based solutions, expanding non-conventional water sources, improving irrigation efficiency, increasing uptake of climate-smart practices, developing disaster risk financing and insurance.2

The weak domestic demand and the fiscal consolidation appear to have added to the drought-related losses, offsetting some of the gains from export markets. The compression of public wages—with the public administration sector growing only by 0.7 percent in real terms—and of public investment compounded the agriculture-related losses. These trends likely depressed domestic demand, penalizing sectors such as construction services and materials (−4.0 percent) and commerce (−0.4 percent). The former may have also been affected by some labor shortages as many sub-Saharan African workers, who had comprised a large share of construction workers, departed Tunisia in 2023 (see the Fall 2023 edition of the Tunisia Economic Monitor). The difficult international financing conditions also likely contributed to the slowdown by affecting the economy’s ability to import, particularly for manufacturing sectors, which shrank by 1.1 percent in the second semester (figure 4). These factors offset the gains from export markets, including for hotels and restaurants (+12.8 percent), which benefited from the continued tourism recovery driving the overall positive contribution of services, and for mechanic and electric sectors (+ 5.8 percent).

The growth slowdown—especially in labor-intensive sectors—translated into worsening labor market outcomes. As labor-intensive sectors (i.e., agriculture and construction) were particularly hit by the slowdown, unemployment grew to 16.4 percent in Q4 2023 up from 15.8 percent in the previous quarter and 15.2 percent a year earlier. This was the third consecutive quarter of year-on-year increases in the unemployment rate, reversing the declining post-Covid trend (figure 5). Additionally, the labor force participation rate continued the decline that had started during the Covid period, suggesting persistent growth in the number of discouraged workers. The average participation rate in 2023 (45.8 percent) was 1.3 percentage point below the average pre-Covid. As a result, the net job creation relative to the previous year was negative in the second half of 2023, with over 83,000 net jobs lost in Q4 alone (figure 6). Most of the losses were for female workers, adding to the already large penalty that women experience in the Tunisian labor market, with a higher unemployment (22.2 percent versus 13.8 percent in Q4) and a lower participation rate than men (27.1 versus 65.1 percent).

2 See World Bank (2023) Tunisia: Climate Change and Development Report.
2. The growth slowdown amplifies the challenges Tunisia faces in covering its significant external financing needs despite the improvement in the external balance.

Tunisia’s merchandise trade deficit improved in 2023, boosted by favorable changes in international prices. After the adverse terms of trade shock induced by the war on Ukraine in 2022, more benign global prices helped reduce the trade deficit to TD 17.1 billion in 2023 (10.8 percent of 2023 GDP) from TD 25.2 billion (17.5 percent of GDP) in 2022 (Figure 7). This reduction was driven by the shrinking trade deficit of mechanic industries and the expanding surplus of textile and garments, both of which benefited from significant increases in prices. For instance, unit values of exported electric equipment, which accounted for half of the merchandise export growth, increased year-on-year by 3.5 percent and hosiery (6.5 percent of export
growth) by 15 percent (Figure 8). The price hike was even larger for oil and fats (+65 percent accounting for 27 percent of goods’ export growth), which benefited from the tightening of the global olive oil supply. Despite a 15 percent reduction in quantities, Tunisia’s oil and fats exports increased by 40 percent, contributing to a significant shrinking of the agricultural and agro-industrial trade deficit (−43 percent).

The energy deficit widened despite more favorable prices, continuing to account for the bulk of the merchandise trade deficit. As a net energy importer, Tunisia benefited from a reduction in global energy prices in early 2023 as the global impact of the Russian invasion of Ukraine dissipated. The average price of hydrocarbons imported by Tunisia declined by 14.4 percent in 2023 compared to 2022. Yet, imported quantities increased by 4 percent as Tunisia’s production of oil and gas declined.3 Thus, energy imports declined only by 10.8 percent in value. On the other hand, energy exports declined by 16.6 percent along with production. As a result, the energy trade balance deteriorated further, accounting for 56.6 percent of the merchandise trade deficit in 2023. That share has more than doubled since 2017, reflecting the delay in developing alternative sources of energy, particularly renewables (see part B).

The narrowing trade deficit along with the rebounding of tourism exports lowered the current account deficit (CAD) in 2023. The significant reduction in the merchandise deficit was accompanied by the continued recovery of tourism, which benefited from a robust summer season. Receipts grew by 28.1 percent in 2023, reaching TD 6.9 billion, or 4.4 percent of GDP up from 3.8 percent of GDP in 2022. In early 2024, there are signs of stabilization. By March 20th, tourism receipts were up 8.8 percent compared to the same period last year. In 2023, the contribution to tourism in GDP returned almost to its pre-Covid level (4.6 percent), while the total number of foreign visitors (8.1 million) was slightly higher than in 2019 (7.9 million). Tourism receipts were almost on par with remittance inflows (TD 7.3 billion or 4.6 percent of GDP), which recorded a more modest increase (+1.4 percent) but which remain a key source of foreign exchange for Tunisia. As a result, the CAD fell by two-thirds, from TD 12.4 billion in 2022 (8.6 percent of GDP) to TD 4.1 billion (2.6 percent of GDP) in 2023 (figure 9).

While the lower CAD eases the pressure on external financing needs, the latter remain significant especially due to the burdensome debt

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3 In the first six months the production of oil declined by 8 percent while that of natural gas by 11 percent (source: Ministry of Industry, Mining and Energy (2023) Conjoncture Énergétique, June).
service. Despite the reduced CAD, external financing needs remained significant in 2023 (TD 13.4 billion, or 8.4 percent of GDP) with amortization accounting for 70 percent of them. These needs are expected to rise further to TD 16.4 billion in 2024 (9.4 percent of GDP), most of which (59 percent) again due to debt reimbursement. Securing these large needs continues to present a pressing challenge for Tunisia, further amplifying the pressure on the economy.

3. Tunisia’s increasing reliance on domestic sources to fill the external financing gap raises concerns about the stability of the Dinar and of prices

In the absence of private sources of capital, Tunisia continues to depend on sovereign lending to finance its external needs amidst tight financing conditions. Tunisia depends mainly on sovereign financing to cover its external financing needs as other sources of funding are either inaccessible (international private financing) or cover only a small share of the external financing needs, as is the case for foreign direct investments and portfolio flows (figure 10). Foreign sovereign financing however has been declining over the past couple of years and there are no expectations that it could cover a larger share of external financing needs in 2024 than it did in 2023, particularly in the absence of an IMF loan agreement. The draft new foreign exchange code recently submitted by the government to Parliament could address some of the restrictive capital controls which limit FDI and portfolio flows. According to the most common indicators, Tunisia is a relatively closed economy in terms of capital controls. According to the Chinn-Ito de-jure financial openness indicator, Tunisia was ranked 116 out of a sample of 176 countries in 2021 in terms of the openness of its capital account. This is consistent with a study by Fernandez et al. (2016), which classifies Tunisia as one of the 5 closed economies in terms of capital controls out of the 26 comparable economies

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4. External financing needs are defined as current account deficit + debt (public + private) reimbursement.
5. The Tunisian government has not been able to issue foreign-denominated bonds since 2019, as its sovereign credit rating has been consistently assessed as noninvestment grade (including by Moody’s, Fitch Ratings and Rating and Investment Information).
6. In fact, the 2024 budget indicates that 71 percent of the external budget support needed to cover the external financing was not identified (versus only 37 percent in the 2023 budget).
analyzed. The bulk of Tunisia’s regulatory restrictions on capital are applied to outflows and dates back to the original foreign exchange code of 1976. The generally cumbersome application of these measures exacerbates the uncertainty around access to foreign exchange created by the code, thus contributing to stifle capital inflows. The government recently approved a draft new foreign exchange code, which should eventually be discussed by the Parliament. However at this stage it is unclear to what extent it will be able to strike the right balance between financial openness and capital and financial accounts stability.

With shrinking sovereign financing, the government has turned to monetary financing to cover its external needs, notably through the use of foreign exchange reserves. The government borrowed from the domestic banking system to reimburse a Euro 500 million Eurobond last October. In February 2024 the Parliament approved a bill authorizing the BCT to finance the budget up to TD 7 billion in 2024, including also for the reimbursement of foreign denominated debt. The loan would bear zero interest and would be reimbursable over 10 years with a 3-year grace period. The amount is equivalent to 4 percent of GDP, a quarter of total financing needs and 42 percent of the budget external financing needs forecast by the government for 2024.

In the context of limited alternative financing sources, this facility could fund much of the external financing gap in 2024, i.e., TD 10.3 billion according to the 2024 Budget Law. That could pose some risks to the stability of the Dinar. The brief periods of reserve losses since 2020 have been associated with some depreciation of the Dinar, e.g., May-Nov 2022 (Figure 11). If the entire facility were used to fund external debt service (and reserves were not accumulated through additional external financing), reserves would decline by 27 percent, double the maximum peak-to-trough reserve loss since 2020 (Figure 12). Should the entire external financing gap be covered by reserves, the loss would be 40 percent, bringing the import coverage to only 70 days. The Dinar depreciation would also put pressure on inflation, which remains high (7.5 percent in February).

This is the second time Parliament is approving a bill for direct financing by the BCT, following the one in December 2020, when it authorized a TD 2.8 billion financing facility to cover exceptional budgetary needs due to the Covid pandemic. Using monetary financing under non-exceptional circumstances could reduce fiscal discipline. This would establish a regime of fiscal dominance over monetary policy, reducing the BCT’s effectiveness at controlling inflation and at maintaining financial stability.

4. The rising role of domestic financing of the public debt heightens the pressure on the domestic banking system

The reimbursement of the latest Eurobonds consolidated the recent hike in Tunisia’s bond prices,

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9 Potentially important measures included in the revised code comprise a review of the notion of residency for investors, the freedom to open foreign currency accounts for exporters, and the possibility of opening accounts that enable sales on online platforms.
reflecting the perceived reduced risk of default on public external debt to private markets. By early March 2024, two weeks after the repayment of the February Eurobond, Tunisia’s US$ denominated bonds maturing in 2025 were trading at 93 percent of their issuance price. That is their highest level since July 2021, marking a rebound of 80 percent from their lowest price in May 2023. This jump reflects the increased trust in Tunisia’s ability to repay its external public debt to capital markets given its shrinking level. As Tunisia has been unable to borrow from international capital markets since 2019, the share of private creditors in both total public debt and public external debt is the lowest in decades (Figure 13). And the level of foreign reserves (US$ 7.4 bn) would be sufficient to cover the external debt to capital markets, which was around US$ 3.0 billion as of February 2024.

The drying up of external financing sources along with the rising public debt have resulted in the growing role of the domestic banking system for debt financing. The challenging external financing environment has translated into the slow growth of the nominal external debt stock over the past few years (Figure 14). In parallel, public debt grew rapidly (from 66.9 percent to 80.2 percent of GDP between 2017 and 2023), reflecting rising public expenditures and the deceleration of the economy.10 As a result, Tunisia has increasingly tapped into local markets as a financing source so that the share of external debt in total debt decreased from 73 (2018) to 57 percent (2023) (figure 14). This domestic financing necessitated a high level of refinancing to local banks by the Central Bank.11

The sustained use of local funding to finance public debt continues to crowd out credit to the economy. The injection of liquidity through refinancing operations is directing bank liquidity towards government lending, which is likely to crowd out credit to the rest of the economy. The banking sector’s exposure to the State continues to grow at an annual rate of more than 17 percent, while the share of loans to

10 The debt figure covers only the central government’s but not SOEs’ debt, much of which is guaranteed by the State as well as payment arrears to public and private companies.
11 Refinancing consists of the Central Bank lending money to banks with liquidity needs, generally short-term. They are carried out on the initiative of central banks (through tenders) or banks (lending facilities). While refinancing is associated with money creation, the relation is not one-to-one as it depends on the terms of the reimbursement and the loan maturities.
the economy is decreasing with a growth rate of 3 percent. As a result, the share of central government in total claims of the banking sector increased from an average of 14.4 percent in 2015 to 32 percent in 2023 (Figure 15). In a context of limited credit growth, this pattern has displaced credit to the rest of the economy. And this pattern does not account for the crowding out of the rising credit to SOEs vis-à-vis private credit (see Tunisian Economic Monitor, Fall 2023 edition).

5. Shortages of basic products persist amidst import compression and declining agricultural production

As external financing conditions remain tight, imports continue to be compressed particularly for the increasingly indebted state-owned enterprises (SOEs). Compressing imports has remained an important strategy to achieve the external balance, given the challenging external financing environment. That is particularly the case for SOEs, as their increasing debt stifle their access to credit, particularly in foreign currency. Several of these SOEs hold the monopoly over the import and distribution of specific products, such as the Office des Céréales (OdC) for wheat, the Pharmacie Centrale for medicines, the Office du Commerce for coffee and sugar, the Tunisian Company of Electricity and Gas (STEG) for gas and the Tunisian Company of Refining Industry (STIR) for petrol (see part B). As discussed in the Fall 2023 edition of the Tunisia Economic Monitor, the system of price control that regulates the markets of these basic

Office du Commerce for coffee and sugar, the Tunisian Company of Electricity and Gas (STEG) for gas and the Tunisian Company of Refining Industry (STIR) for petrol (see part B). As discussed in the Fall 2023 edition of the Tunisia Economic Monitor, the system of price control that regulates the markets of these basic

12 SOEs’ net debt to the state for instance grew from TD 1.4 to TD 3.6 billion in 2020–2022.
products is the main cause of the increasing indebtedness of SOEs and hence of the current shortages.

This import compression has translated into shortages of basic products, exacerbated by the drop in domestic agricultural production. The increasing constraints to imports faced by SOEs has affected several basic products, including coffee, tea, vegetable oils, wheat (soft and hard), medicines, causing repeated shortages in key markets since 2022. For cereals, as the drought decimated Tunisia’s hard wheat harvest in 2023, the OdC was unable to step up its imports sufficiently to compensate for the shortfall, in spite of the lower international prices (Figure 16). In the absence of sufficient wheat stocks, the quantity of hard wheat supplied to the market dropped by 8 percent in 2023 compared to 2022. This contributed to the shortages of hard wheat products, notably semolina. Given the substitutability between hard and soft wheat, the shortfall seems to have also affected products usually made with soft wheat, particularly flour and its derivatives, including bread.

6. Inflation moderated from the record levels of early 2023 but it remains elevated, particularly for food

Inflation started to moderate since the peak of February 2023 on the back of lower global prices and weak domestic demand. Year-on-year price inflation continued its gradual decline from the record level of February 2023 (10.4 percent), reaching 7.5 percent in February 2024 (Figure 17). This followed the reduction in core inflation to 6.9 percent (February 2024) from 7.9 percent (February 2023) driven in part by the weak domestic demand given the slowdown in economic growth. The decline in international prices compounded this effect, helping reduce the pressure on domestic prices. Driven by the drop in international prices of energy, cereals and iron and steel, Tunisia’s merchandise import prices declined on average by 4.4 percent in 2023. That allowed Tunisia to implement a price freeze of energy products with electricity and gas inflation declining from 14.9 percent in February 2023 to 0.2 percent in February 2024.

Inflation is lower than the nominal interest rate for the first time since July 2021. With declining inflation, the Central Bank (CBT) maintained its key policy rate unaltered at 8 percent since the beginning of 2023. As a result, real interest rates became positive as of January 2024 after more than 2 years of having been negative. The challenge for the authorities continues

Core inflation is computed by excluding energy and food products from the CPI.

That is an average obtained by weighing each 2-digit sector level price change by the corresponding share in total Tunisian merchandise import in the first 7 months.
to be to avoid inflationary pressures fueled by a price-wage spiral. The effectiveness of this policy depends on accompanying measures to pursue macroeconomic stabilization and adopt the structural reforms needed to resume a sustainable growth trajectory. Maintaining a strong and independent Central Bank will continue to be a central pillar in the pursuit of price stability.

However, inflation is still high, particularly for food, as the drought and import compression reduced the supply in domestic food markets. Despite the decline, inflation remains well above the 2021–2022 average (7 percent) and food inflation is particularly high (10.2 percent). While the rate of price increases for food have been historically higher than average inflation, the gap has been growing in the past year as the drought and import compression reduced the domestic supply of agricultural products. This presents a significant challenge particularly for lower income households, for which food accounts for a relatively greater share of expenditures.15

The recent government measures to contain food prices focused on combating hoarding behavior and enhancing price controls but food inflation remains elevated. The government has taken several measures since 2022 to reduce food inflation, including through a new law punishing hoarding and new regulations controlling food prices and distribution channels. However, these measures do not appear to have yielded the desired effect, as other factors, including the shortfall in supply and imports linked to the drought and the monopoly of highly indebted SOEs, seem more important drivers of inflation to date.

New analysis shows that most of the recent inflation episode is driven by rising profits and import prices, pointing to the important role of competition and trade policy against inflation. The analysis is based on a novel decomposition of Tunisia’s consumer price inflation into factors of production (labor and capital), net taxes and

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15 According to the 2021 Household Budget survey, the share of food in total expenditures is 35.5 percent for the bottom quintile of the income distribution and 27.2 percent for the top quintile.

16 This decomposition is proposed by a recent paper by Hansen, N.-J., Toscani, F. and J. Zhou (2023). “Euro Area Inflation after the Pandemic and Energy Shock: Import Prices, Profits and Wages”, IMF Working Paper 23/131. The decomposition needs four sets of data: (i) sectoral nominal and real GDP; (ii) sectoral nominal wages and profits; (iii) the share of gross value added in sectoral consumption; (iv) the sectoral taxes net of subsidies. For Tunisia, data for (i) and (ii) comes from the INS national account data; data for (iii) comes from the OECD Trade in Value Added dataset; and data for (iv) is taken from various rounds of the social accounting matrix from the INS.
import prices. The decomposition shows that after the Covid pandemic in 2020, profits (driven by capital rent) accounted for the lion’s share of annual inflation—61 percent on average (Figure 18). Import prices were responsible for around 40.9 percent and wages only accounted for 21.9 percent. Increased profits were responsible for a hike in prices of 4.9 and 4.2 percentage points in 2022 and 2023 respectively. That is double the effect of profits in the Euro area in 2022 estimated by Hansen et al. (2023). This major role of profits along with imports is not new in the last two decades (Figure 18) and it suggests that policies to promote open competition and trade, such as through reducing barriers to entry and trade across sectors, would be key to keep inflation in check.

7. The budget continues to be under pressure as the low growth affects tax revenues

The budget deficit was stable in 2023 (6.7 percent of GDP) following a more modest that expected increase in tax revenues pulled down by the slowdown in growth. The provisional 2023 budget—rectifying the 2023 budget law—shows that tax revenues are expected to have grown by 11.4 percent in 2023 compared to 2022. That is significantly below both the initial projections in the 2023 Budget Law (15.3 percent) and the 2022 growth rate (16.6 percent), but higher than nominal GDP (Figure 19). The comparatively modest performance of indirect taxes, particularly VAT (6.8 percent growth) and customs (4.8 percent), weighted down overall tax revenues. That is consistent with the effect of the economic growth slowdown, with lower demand for consumption and investments, including for imports. On the other hand, direct taxes showed greater resilience (+12.4 percent) as their largest component—labor income taxes—is less responsive to short-term variations in growth.

The growth in public expenditures was due mainly to rising transfers and interest payments but moderated by relatively contained wage bill growth and stalled capital expenditures. The public wage bill—the largest expenditure item—grew by 8 percent in 2023, slightly below the inflation rate and nominal GDP. While Tunisia still has one of the highest public wage bills in the world relative to the size of its economy, it declined from 16.1 percent of GDP in 2020 to 14.4 percent in 2023 and from 47.0 percent to 40.6 percent of total public expenditures. The slow decline of the wage bill follows the agreement between the government and the trade union (UGTT) in October 2022 and the continued freeze of public sector recruitment. The relatively moderate growth of the wage bill helped keep overall expenditure growth in check (+11 percent) despite the significant expansion of transfers (+30 percent, growing from 4.1 percent to 4.8 percent of GDP) and interest payments (+25 percent, from 3.2 to 3.7 percent of GDP). Capital expenditures continued to grow below the rate of overall expenditure (+2 percent) and its share in GDP declined further to 3 percent (from 3.2 percent in 2022).

Reversing the decline in public capital expenditures by re-orienting less productive recurrent expenditures continues to be key to revive economic growth. With slowing economic growth and employment creation, successive governments over the past decade have increased recurrent public expenditures to provide public employment and to keep market prices for basic goods and services below cost recovery. Expenditures on subsidies (for energy and food products) grew from 2 percent to 7.2 percent of GDP between 2016 and 2023 (figure 20). These measures crowded out public investments, which declined from 6 percent to 3 percent of GDP over the same period. Reversing this decline in capital expenditures is crucial to revive Tunisia’s growth trajectory.

8. Assuming drought conditions ease, we expect a moderate growth rebound in 2024-25 assuming but economic prospects remain uncertain

After the significant slowdown in 2023, we expect a moderate rebound of the economy in 2024–26.

At the same time productivity (both of labor and capital) increased marginally and hence resulted in only a small inflation reducing effect. This inflation reducing effect explains why the sum of the positive contributors to inflation, i.e. profit, wage costs and import prices, is greater than 100 percent.
Assuming a moderation of the ongoing drought and slightly more benign financing conditions, growth is forecast to reach 2.4 percent in 2024 and 2.3 percent in 2025–26. With this growth rate, real GDP in 2024 would eventually reach its pre-Covid 19 level, a full four years after the pandemic started. This modest growth is due to challenging conditions linked to water scarcity, the uncertainty around debt financing and the weak momentum of reforms to address structural impediments to growth.

The 2024–26 growth forecast is subject to significant downside risks. Growth projections could be even lower should Tunisia not implement fiscal and pro-competition reforms and/or should available financing not be sufficient to cover Tunisia’s external needs. If these conditions were to materialize, it may be challenging to secure sufficient foreign currency in the economy, which could lead to pressures on exchange rate and prices, exerting a negative impact on economic activity and employment. In addition, should the drought conditions persist, the projections could be revised downwards given the negative impact on agriculture and the trade balance.

Tunisia’s public finance and external account will remain precarious in the absence of sufficient external financing. The budget deficit is expected to decline somewhat to 6.1 per cent of GDP in 2024. That is mainly driven by a decline of subsidies and wage bill in real terms and a moderate increase in tax revenues. The CAD is projected to remain stable at 2.4 percent of GDP in 2024 with continued growth in travel exports and stable terms of trade. With FDI projected to be relatively stable and minimal portfolio investments, foreign lending would still have to shoulder the financing of the CAD.

The financing of the deficits will require a significant scale-up of the external financing in the face of the heavy debt reimbursement schedule. Despite the lower deficits, gross financing needs are expected to rise further at 16.1 percent of GDP in 2024 (from 13.8 percent in 2023) due to significant external debt service. In fact, almost two-thirds of the financing is expected to be amortization. It also increases Tunisia’s reliance on external funding sources, which should account for around 57 percent of total financing. With FDI projected to be stable and minimal portfolio investments, sovereign lending would still have to cover the external financing needs as Tunisia continues to be cut off from international capital markets.

If the pace of reforms and the level of financing remain sufficient, we project growth to be sustained at the 2024 level over the medium run along with some stabilization of the macro and fiscal imbalances. We expect the economy to maintain its pace of growth to 2.3 percent in 2025–26. That would entail the alignment with the long-run growth path, from which the economy deviated during
the Covid-19 crisis. We expect inflation to decrease somewhat due to the relatively large post-Covid output gap and the mild increases in public wages following the government-UGTT agreement at the end of 2022. These conditions along with economic reforms should help Tunisia reduce its current account and budget deficits, easing financing conditions. Furthermore, the slight increase in real economic growth should lead to a decrease in the poverty rate below pre-Covid levels by 2025. However, these medium-term prospects are conditional on an ambitious pace of reforms, sufficient financing, and the stability of international energy prices, oil in particular.

18 The finding applied whether using lower-middle or upper-middle income country poverty line (equivalent respectively to US$3.65/person/day and US$6.85/person/day in 2017 purchasing power parity terms).
Summary

As Tunisia’s macro-fiscal challenges deepen, the government’s target of generating 35 percent of energy from renewable sources by 2030 becomes even more important. In the last two decades, the country has grown more dependent on fossil fuel imports, which undermine the sustainability of the current account. This dependence weighs heavily also on the fiscal balance given the high costs of energy subsidies when international oil and gas prices are high. By increasing the demand for energy, global warming is exacerbating the challenges of energy dependence and undermining the security of energy supply.

Tunisia’s energy sector does not have to depend on fossil fuels as the country has a rich untapped renewable energy potential. Renewable energy could significantly reduce the cost of electricity production, especially in the context of high and volatile international energy prices. New analysis shows that renewable energy generation could play a dominant role in power generation in Tunisia as it is the least cost energy source. To fulfill this potential the Government would need to address various impediments including the weak energy sector financial performance and the integration of the grid. The benefits of expanding renewable energy production would extend to the whole of economy, with significant gains in terms of economic growth materializing already by 2030.

The World Bank’s Tunisia Climate Change and Development Report (CCDR) estimates large investments needed to enable this green energy transition, to the amount of US$ 27–35 billion by 2050. The bulk of these investments are expected to be covered by the private sector given the significant cost advantage of green energy investments over thermal energy and fossil fuels in Tunisia. However, adequate conditions should be in place to favor such investments and accelerate the implementation of Tunisia’s ambitious renewable energy program towards its 2030 renewable energy target.
gas, more than half of which is imported due to rising demand and declining local resources since the early 2000s. The significant role of energy subsidies in Tunisia’s fiscal deficit (22 percent of budget expenditures in 2022–23) compounds this dependence. The development of renewable energy, which is a local, abundant, and lower cost resource, could reduce the dependence on imported fossil fuels, the fiscal deficit, and the cost of electricity production. As such, the government’s target of 35 percent of energy from renewable sources is crucial not only for emission reduction but also for economic development goals.

The country has grown more dependent on fossil fuel imports, which undermine the sustainability of the current account. This increasing dependence has translated into an increase in energy imports as well as of the share of energy in the trade deficit (figure 21). The latter has grown from an average of 15–20 percent in 2017 to 86 percent in the last six months of data (Sep. 2022–Feb. 2023). The increased dependence on imports of fossil fuels is illustrated by the increase in the primary energy balance deficit which reached 4.7 Mtoe in 2023 and by the deterioration of the energy independence rate, the ratio of primary energy resources to primary consumption, which stood at 48 percent in 2023 compared to 80 percent in 2012 and 59 percent in 2015.19

Eventually, Tunisia’s current account deficit and financing conditions may limit its ability to import the energy it needs to meet growing demand, thus stalling economic activity. With a large structural current account deficit and limited capital inflows (see Part A), Tunisia is expected to maintain large external financing needs over the next years. Recent evidence has shown that financing these needs without accessing international capital markets will become increasingly challenging, limiting Tunisia’s ability to import energy and other inputs for its industrial activities. The recent World Bank’s Tunisia Climate Change and Development Report (CCDR) projects that Tunisia’s energy imports would have to be reduced by 3.5 percent to preserve a level of foreign exchange reserves covering at least two months of imports. This energy supply constraint would significantly affect production across all sectors. An analysis in the CCDR based on World Bank Enterprise Survey data suggests that doubling the number of power outages would reduce the value added by Tunisian manufacturing and service companies by 8.7 percent. For households, it would mean reduced mobility and comfort, since energy is a critical input for transport, cooking, heating, and lighting. An energy shortage would also generate large losses and inflation at the macro level.

The dependence on imported fossil fuels also weighs heavily on the fiscal balance given the high energy products’ subsidy rate when international oil and gas prices are high. Despite some tariff increases in recent years (lastly in 2022), the price of electricity and gas for consumers are still well below production costs. The average tariff for electricity covers around 62 percent of the costs, while that of natural gas only 46 percent.20 This gap continues to generate large losses for STEG, which complicates its financial position and hence its ability to meet the growing demand.

By increasing the demand for energy, global warming is exacerbating the challenges of energy dependence and undermining the security of

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energy supply. Warming temperatures are causing a rapid increase in demand for energy, particularly during the summer season. Peak electricity demand reached 4,825 MW in the summer of 2023, a 3 percent increase over the same period in 2022, mainly as a result of the rising usage of air conditioning. This peak demand forced STEG to resort to load shedding in certain areas of the country as the system was unable to fully cover the peak. The load shedding strategy may also disrupt water supply in certain regions as the water transfer stations require electricity to operate. The heightened demand also resulted in the direct purchase of electricity and additional gas import from Algeria as well as in the use of marginal gas power plants, all of which further increased the cost of electricity.

In fact, Tunisia’s energy sector does not have to depend on fossil fuels as the country has a rich untapped renewable energy potential. With its high solar irradiation and wind resources, Tunisia has a potential of up to 280 GW of solar and 90 GW of wind power, far exceeding the current electricity peak demand of 5GW. This potential would even allow for the development of energy exports, especially given Tunisia’s strategic location near the large European market.

Based on this huge potential, the government has set the ambitious target of generating 30 percent of electricity from renewables by 2030. This is an increase compared to the original 30 percent target, which was set as part of the Tunisian solar plan approved in 2014. The achievement of the 2030 target would require the development of a capacity of 4.8 GW renewable energy and an investment to the tune of US$ 4.5 billion.\textsuperscript{21} The National Low-Carbon Strategy is even more ambitious with a target of 50 percent of electricity from renewables (6 GW) by 2035 and 80 percent by 2050. While ambitious, such targets are achievable. A capacity expansion model developed by the World Bank indicates that renewable energy is part of the least-cost solution to serve fast-increasing demand in Tunisia, resulting in a capacity level of 12.6 GW by 2040 (with wind accounting for 70 percent of the renewable capacity).

To achieve the renewable energy target, Tunisia has set up an ambitious renewable energy development program based on public-private partnerships. The implementation of the first 500 MW in the program is progressing after some delays due to rising prices and financing costs in the wake of the Covid and Ukrainian crises. In addition, in December 2022, the government announced projects for a further 1,700 MW to be implemented over the period 2022–2025, with bids for the first round of solar projects due by May 30, 2024. This overall 2,200 MW program would require a US$ 2 billion private investment. Once implemented, it will increase the share of renewable energy in the electricity mix from 3 to 17 percent, with estimated savings of 1 million ton of oil equivalent of imported gas and a significant reduction in production costs.

Renewable energy could significantly reduce the cost of electricity production especially in the context of high and volatile international energy prices. The cost of natural gas accounts for over 70 percent of the cost of electricity produced. With the rise in oil prices in 2022, the electricity produced from natural gas (whose price is indexed to that of crude oil) became increasingly expensive, and its cost far exceeded that of electricity produced from renewable energy (Figure 22). In 2022, the average cost per MWh produced by STEG\textsuperscript{21}

\textbf{FIGURE 22} • The Cost Advantage of Renewables for Electricity Production  
\textit{(Costs and tariffs: TD per MWh of electricity in 2022)}

A\textsuperscript{v}g electricity tariff (STEG)

\begin{tabular}{|c|c|c|c|c|c|}
\hline
Gas & Algeria import & Solar & Wind & Min solar & Max solar & Wind (30 MW) \\
\hline
0 & 50 & 100 & 150 & 200 & 300 & 400 & 450 \\
\hline
\end{tabular}

\textit{Note:} Algeria import refers to the direct import of electricity from Algeria; Concession tariffs are the current maximum tariffs according to the source of energy production.

\textsuperscript{21} Source: Ministère de l’Industrie, des Mines et de l’Energie and UNDP (2023), Stratégie énergétique de la Tunisie à l’horizon 2035, Tunis: April.
New analysis shows that renewable energy generation is projected to play a dominant role in power generation in Tunisia as it is the least cost energy source. Analysis carried out in the CCDR uses a capacity expansion model (OPTGEN) and a dispatch model (SDDP) to prepare projections of power generating capacity and electricity production by type of technology until 2050 for three scenarios (described in Box 2). In all scenarios, there is a massive switch from natural gas to renewable energy because solar and wind are part of the least-cost solution for producing electricity. By 2050 renewables would account between 77 and 84 percent of total installed capacity (Figure 23). Some natural gas capacity is added for the latter part of the forecast period, at which point some gas plants would have been retired and additional gas-fired generation will likely be needed to enhance the flexibility of the power system. Given the higher electricity demand for hydrogen production in Scenario 3, the installed capacity is double that of Scenario 2. It also favors solar PV energy due to lower investment costs and the possibility of shifting hydrogen production to hours with avail-

was TD 441 (with an import price for natural gas of 1335 TD/TOE). This is two third higher than the average electricity tariff and three and four times as high as the average cost of electricity generated through solar and wind power respectively. It also far exceeds the maximum tariffs for the electricity produced with solar power in Tunisia’s concession regime (large scale Independent Power Producers).

Exploiting Tunisia’s renewable energy potential is even more important in light of the ongoing development of the electric connection between Tunisia and Italy. This project—named Elmed interconnector—aims to create by 2028 a 600 MW sub-marine link between Tunisia and Italy (Sicily), allowing the bi-directional exchange of electricity between the two countries. Connecting the Tunisian power system to the larger European power system could reduce the dependence on natural gas and enable large-scale development of the renewable energy potential by increasing the power system flexibility. This in turn could reduce the overall generation cost in Tunisia, hence enhancing the sector’s financial viability, and lowering the need for natural gas imports. In the long term, as the country develops its renewable energy potential on a large scale, Tunisia could become a net electricity exporter to Europe and thereby structurally improve its balance of payments.


That is in line with the government’s target of 80 percent.
able sunlight. In all scenarios, natural gas accounts for an increasingly smaller share of generation, down to less than 2 percent in the most ambitious scenario 3 (figure 24). The Elmed interconnection could initially be used to import electricity until the renewable energy potential is sufficiently developed. Towards the end of the forecast horizon, Tunisia would become a net exporter of electricity under all scenarios.

The benefits of expanding renewable energy production would extend to the whole of economy, with significant gains in terms of economic growth already by 2030. Macro-economic modelling developed for the CCDR shows the impacts of the 3 scenarios of renewable energy transition described above. The modelling shows that all scenarios lead to sizable economic gains relative to business as usual, with the economy expected to be larger by between 1.1 percent (scenario 1: least-cost scenario) and 1.75 percent (scenario 3: deep decarbonization) by 2030 (figure 25). Scenario 3 is particularly beneficial for the economy in the short term because end-user sectors are likely to benefit from enhanced decarbonization policies, resulting in lower energy costs. While all sectors benefit, industry and agriculture perform particularly well given their greater energy dependence compared with services. Public debt increases in all scenarios, but not signifi-
large investments across all green energy transition scenarios, ranging between US$ 11 and 12 billion by 2030 and going up to US$ 27–35 billion by 2050. Around 60–65 percent of the investment needs are expected to be covered by the private sector. That is because the investments in renewable energy production are commercially viable given the significant cost advantage over fossil fuel in Tunisia. Such massive development of renewable energies, driven by the private sector, will require a favorable regulatory and financial environment and a highly flexible power system.

**Tunisia needs to accelerate the green transition to achieve its ambitious renewable energy target.** The Tunisian government has started to undertake regulatory reforms to improve the performance of the Tunisian electricity sector and the attractiveness of the renewable energy program to private investors. Accelerating these efforts would be crucial to achieve the ambitious renewable energy objectives and reap the related economic benefits. This would require various measures including (i) strengthening the coordination between the various parties involved in the projects, and the monitoring of program implementation, (ii) accelerating the implementation of ongoing programs, which is important for the country’s credibility; (iii) strengthening the governance of the renewable energy sector; (iv) clarifying the approval process and limiting the number of permits required; (v) simplifying the procedures for land access; (vi) speeding up the establishment of an independent regulator to reassure investors and ensure a transparent and fair access to the grid; and (vii) modernizing STEG and restoring its financial viability.