International Monetary Fund

Tunisia: Letter of Intent

April 2020

The following item is a Letter of Intent of the government of Tunisia, which describes the policies that Tunisia intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Tunisia, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

Letter of Intent

Tunis, April 2, 2020

Madame Kristalina Georgieva
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International Monetary Fund
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Madame Managing Director,

1. Tunisia was hit hard by the Covid-19 pandemic. The first case of Covid-19 was reported on March 2. Initially an imported disease, new cases have been surging among people with no travel history. The total number of confirmed cases to date amounts to about 300. Like other countries, this apparently low number conceals however a more complex reality. The Tunisian population is particularly exposed to the pandemic given the country's geographical proximity to the current disease clusters in South Europe, and the intensive human and economic relations between Tunisia and its European neighbors. Tunisia has around 217,000 nationals in Italy, 824,000 in France, and 103,000 in Germany. Since the beginning of the year, Tunisia has received 1.1 million visitors (nationals and foreigners) including from its most hit European neighbors, multiplying the risks of contamination for the local population. The extent of the pandemic is not fully known: the health system is under-resourced and does not allow yet extensive testing of the population. The virus must have inexorably reached all regions of the country including the disadvantaged ones, in connection with the visits of Tunisians working overseas to their families.

2. The economic consequences of the pandemic for Tunisia are expected to be severe and to jeopardize some of the macroeconomic achievements of 2019. As in other countries hit by the shock, Tunisia will likely experience a steep recession in 2020 with growth falling by up to 4.3 percent although exceptionally high uncertainty today does not allow for any precise projections. The initial impact of the pandemic may be exacerbated through several channels: (1) the containment measures taken by the government will directly and immediately affect small businesses and will slow down an already weak domestic activity; (2) unforeseen health care costs will weigh on a tight budget with weak buffers to meet these expenses; (3) the consequences of the declining global demand, border closures, and the disruption of the supply chain will affect the Tunisian exporting sector and weigh on remittances from diaspora; and importantly (4) the anticipated strains on the tourism sector, a pillar of the Tunisian economy (7 percent of GDP), could lead to a shortfall of 4 billion dinars of FX revenues this year, and threaten an estimated 150,000 direct jobs and 250,000 indirect jobs.

3. In this difficult context, Tunisia will benefit from our recent efforts to improve macroeconomic stability, and notably our success in (i) containing inflation at 6.7 percent in 2019 compared with 7.3 percent in 2018, (ii) reducing external vulnerabilities through a reduction in the current account deficit to 8.8 percent of GDP in 2019 from 11.2 percent in 2018, (iii) building up

reserve buffers to US$7.4 billion by the end of 2019 from US$5.2 billion at the end of 2018, (iv) narrowing the fiscal deficit to 3.9 percent in 2019 from 4.6 percent in 2018, and (v) curbing the trajectory in the public debt/GDP ratio to 72 percent by the end of 2019 from 78 percent at the end of 2018.

4. Since the virus outbreak, the Government's priority was to contain the spread of the disease and address the public health threat. Day after day, measures were tightened, going from closure of schools and universities, to the announcement, on March 13, of quasi level-3 epidemic prevention measures, including the closure of all maritime borders to travel, the suspension or restriction on flights to-and-from affected countries, followed by the closure of airspace and compulsory self-isolation measures for 14 days for all those entering the Tunisian territory, bans of public gatherings, cancellation of fairs and exhibitions, closure of places of worship, a night curfew, completed by general confinement starting March 22.

5. Beyond these immediate responses, the government has adopted a set of measures to address the Covid-19 outbreak in a broader perspective (see LOI Table 1). These measures, whose cost to the central government budget is estimated at about TD 2 billion, include support for the health sector, including through the purchase of emergency medical equipment and medicine, support for low-income households and other vulnerable segments of society, and support for firms suffering from financial stress due to the spreading virus. We are committed to ensuring maximum effectiveness of these measures by targeted assistance programs (especially toward AMG1 and AMG2) and strong governance and transparency in their implementation. To contain pressures on the budget, we commit to reviewing these time-bound measures on a monthly basis with the objective of phasing them out as soon as they are no longer needed. The measures will not become permanent.

6. To create space for the Covid-19 response measures while maintaining fiscal stability, the government has already taken steps to limit budgetary pressures and reduce urgent balance of payments needs. First, we introduced an automatic price adjustment mechanism for the three main car fuels (gasoil, gasoil 50, essence) to ensure convergence of pump prices with import prices and hence full cost recovery. This will be important to eliminate a big structural risk to our budget. The mechanism, which is based on by-law (arrêté) 028 published in the official gazette on April 3, 2020, will apply monthly adjustments to the pump prices of the three fuels to bring them in line with import prices plus a fixed mark-up for distribution and other costs. The maximum monthly change will be limited to +/- 1.5 percent from the existing pump prices in a first time of its application to avoid large price changes for consumers and firms in the short run; the maximum change will be increased to +/- 2 percent -at the latest by January 2021. In case the international price for Brent oil increases to at least US$45 per barrel, the change to the +/- 2 percent band will be applied from the first month after crossing the US$45 threshold. Price changes will be automatically applied as signaled by the pricing formula, with the process being overseen by a technical commission headed by the Ministry of Energy. The mechanism will be applied for the first time by April 8, resulting in a reduction of pump prices by 1.5 percent across all covered fuel categories. Second, we introduced emergency measures on the civil service wage bill to prevent any hiring, non-statutory promotions,

or new wage increases for 2020 beyond those already agreed with the UGTT labor union. Third, we increased tobacco prices in March for an expected yield of TD 200 million. Finally, we are implementing a temporary and targeted rescheduling of TD 3.4 billion in public investment to open space for Covid-19-related capital expenditures. The savings will be achieved through the delay of lower-priority projects to minimize the negative impact on growth and will be implemented through directives issued to the relevant line ministries.

7. Despite these difficult but necessary measures, we expect a larger than projected fiscal deficit for which about US$1 billion (or 2.6 percent of GDP) in additional external financing would still need to be mobilized. The BOP need will be even larger, given the expected fallout of the Covid-19 outbreak also on the private sector and its access to external financing. To help cover these urgent budget and BOP needs, Tunisia requests emergency financing from the IMF in the equivalent of SDR 545.2 million (about US$753.2 million), corresponding to a purchase of 100 percent of quota under the Rapid Financing Instrument (RFI). The government also requests cancellation of the current Extended Fund Facility arrangement with the Fund.

8. The RFI will contain short-term risks and provide a bridge towards a more durable solution to Tunisia's macroeconomic imbalances. It will be critical to help us cover the urgent scaling up of our medical response to the virus outbreak and address priority needs of low-income households and firms under stress. It will also help us in maintaining a reserve buffer above 3 months of imports to insure our economy against shocks or in the event of a protracted recovery from the Covid-19 outbreak.

9. To further reduce short-term risks, we will ensure realistic costing and maximum effectiveness of our fiscal crisis-response measures and will introduce safeguards to prevent the measures from becoming permanent. Moreover, we commit to addressing two structural challenges that weigh heavily on Tunisia's budgets once the current crisis abates. First, we plan to durably reduce the subsidies for electricity and natural gas while preserving social tariffs. This work stream will start with us adopting a reform strategy with the assistance of the World Bank. We will also implement a natural gas price increase after the Covid-19 crisis subsides to reduce the pressure of this subsidy on the budget. Achieving additional savings on the civil service wage bill will be another priority. We will start negotiations with the UGTT labor union to this effect in April 2020, including on wage policies for 2021 and the medium term; and have already started with an audit of the civil service to detect and reduce absenteeism and ghost workers. We consider all these measures critical for containing the increase in the fiscal deficit, limiting cuts in public investment to make room for crisis-related spending, and maintaining debt sustainability.

10. The CBT commits to pursuing a regular policy dialogue with IMF staff based on high-frequency data. Consistent with its price stability mandate, CBT stands ready to tighten monetary policy in case of a buildup of depreciation expectations that could lead to exacerbating pressure on inflation prospects. To preserve its international reserves, the CBT will also refrain from other FX interventions than those necessary to ensure price discovery; it will consult with IMF staff in the event of pressures on the FX market. We will monitor very closely the evolutions of the banking sector, in particular with respect to credit and deposit growth and asset quality. Loan classification and

provisioning rules will not be eased, and any loan guarantees and subsidies will be provided by the government rather than the CBT.

11. To further reduce budget and BOP pressures, we will intensify our efforts to mobilize additional financing, especially from our external official partners. We are already receiving pledges from several multilateral and bilateral partners to help with our Covid-19 response. We are also working with partner governments on a potential guarantee for future sovereign bond issuances in the currently difficult international context; and will further step-up our efforts to maximize financing from multilateral and bilateral sources. In this regard, we support the call of the WBG/IMF on all official bilateral development partners to mobilize further financing. We also established a National Solidarity Fund for grants from the Tunisian population, which already collected TD 140 million out of the TD 170 million expected for this year.

12. The RFI will pave the way for an EFF request to support our efforts to resume macroeconomic adjustment and support sustainable and inclusive growth. The new government is committed to request an EFF successor arrangement as soon as possible, in support of its economic policy reform agenda that is currently under development. Our fiscal priorities to reduce our large debt burden and make our budget more supportive of growth and fairness will include the reduction of the large civil service wage bill as a percentage of GDP, the phasing out of energy subsidies, a reform of state-owned enterprises and the implementation of an effective social safety net especially for low-income households. To further foster inclusive growth in the economy, we will introduce measures to revive the economy and support SMEs, enforce the rule of law and advance in the fight against corruption, and improve public services especially in the areas of education, health, and digitization.

13. We intend to continue the dialogue with the IMF on Tunisia's balance-of-payments difficulties and will avoid measures or policies that would compound these difficulties. In this spirit, we will not impose new or intensify existing restrictions on the making of payments and transfers for international transactions, trade restrictions for balance-of payments purposes, or multiple currency practices, or to enter into bilateral payments agreements which are inconsistent with Article VIII of the IMF's Articles of Agreement.

14. In line with IMF safeguards policy, we commit to undergoing an update of the safeguards assessment that will be completed before the approval of a new EFF arrangement. As in previous instances, we will provide IMF staff with the Central Bank's most recently completed external audit reports and authorize our external auditors to hold discussions with IMF staff. Since the funds obtained under this RFI will be used for budget financing, we have updated the existing memorandum of understanding between the Ministry of Finance and the Central Bank of Tunisia on their respective responsibilities for servicing the related financial obligations to the IMF.

15. We authorize the IMF to publish this Letter of Intent and the staff report for the request for disbursement under the RFI.

Please accept, Madame Managing Director, the expression of our highest consideration.

Sincerely yours,

/s/	/s/
Marouane El Abassi	Nizar Yaiche
Governor, Central Bank of Tunisia	Minister of Finance, Tunisia

LOI Table 1. Tunisia: Measures Implemented by the Tunisian Authorities to Deal with the Impact of Covid-19 (Millions of Tunisian Dinars)

Total measures	**2,050**
Revenue	**260**
• Postponement of CIT filing to end-May, except for companies subject to the rate of 35%.	
• Encouragement of VAT e-filing.	
• Suspension, until the end of May, of all tax controls and adjustments, as well as time limits for contesting.	
• Acceleration of VAT reimbursements (through weekly rather than biweekly decision meetings and assurance of reimbursement within a month).	100
• Activation of the National Committee and regional reconciliation committees.	
• Rescheduling of tax arrears for up to 7 years.	100
• Suspension of penalties for delayed tax return for three months (starting on April 1).	10
• Immediate accreditation of tax certificated to businesses affected by the pandemic (without need to provide required documents).	
• Waiver of VAT for companies selling medicines (wholesalers and retailers).	30
• Extension of car road tax payment (to April 30).	
• Amnesty on customs offenses against industrial establishments convicted before March 20, 2020 (with the latter required to pay the amounts due to customs with a 10% fine).	20
• For all institutions, allow them to revalue their real estate and non-real estate assets included in their budgets according to their real value, while exempting the goodwill resulting from the revaluation provided that they do not sell them; this to consolidate the balance sheet of companies, among others in front of banks.	
Spending	**1,790**
Social spending	**1,450**
• Health care.	300
◦ Current spending.	300
◦ Creation, at the initiative of the CDC, of an investment mechanism of TD 100 million for the acquisition of equipment for hospitals and public health establishments.	
• Strategic stock of basic food items.	200
• Support for low-income families.	450
◦ One-off cash transfer of TD 200 to 623,000 PNAFN beneficiary households.	
◦ Discounted health care cards for AMG-2 beneficiaries.	
◦ One-off cash transfer of TD 50 to 260,000 AMG-1 beneficaries.	
◦ One-off cash transfer of TD 200 for families taking care of elderly people without support.	
◦ One-off cash transfer of TD 200 for families taking care of disabled family members.	
◦ Restoration and no cut of electricity, gas and water for 2 months for delinquent customers.	
◦ Support for homeless people.	
• Other.	500
◦ Support for unemployed (detail not yet provided).	300
◦ Support for the self-employed (fragile jobs).	200
◦ Report de paiement des crédits bancaires pour 6 mois pour les travailleurs ayant un revenu inférieur à 1000 dinars.	
◦ Maintenance of health coverage; and family and single salary premia.	
◦ Deferral of CNSS contributions until June.	
Financial	**340**
• Reduction of the policy rate by 100 bps.	
• Establishment of a financing line for SMEs of TD 300 million.	300
• Activation of the mechanism for the State to take charge of the interest rate differential between the TMM and the effective interest rate, on investment loans for SMEs (max 3%).	40
• Creation of an investment fund of TD 500 million (with a first closing of TD 100 million) on the initiative of the Caisse des Dépôts et des Consignations in order to finance strategic private companies with mechanisms similar to quasi-equity and allow the preservation of jobs.	
• Creation of a "bridging fund" of TD 100 million on the initiative of the CDC, for the repurchase of shares in investment funds for companies in strategic sectors which are going through difficulties.	
• For the benefit of the sectors most affected by the pandemic, setup of a mechanism allowing the State to guarantee new credits for management, operation and maintenance provided by the banking system until December 31, 2020 reimbursable over seven years, including two years of grace. The total amount of these credits is fixed at 500 MTD. The sectors concerned are those of tourism, transport, culture, etc.	
• Postponement (not credit restructuring) of payment of the installments of credits between March and September for companies and craftsmen classified 0 and 1 and possibility for classes 2 and 3 case by case.	
• Deferral of bank credit payments between March and september for workers with a net income of less than TD 1,000 classified 0 and 1 and possibility to extend the postponent for clients classified 2 and 3, case by case.	
• Imposition on banks with a LTD ratio of more than 120% at the end of a quarter to lower the ratio level by 1% each quarter.	
• Free cash withdrawal from ATMs.	
• Suspension of any commission applied to the electronic payment of billers and merchants for any transaction less than or equal to TD 100.	
• Provision of a free bank card (and/or pre-paid card) to interested customers.	
Other	**0**
• Permission for fully exporting companies in the food and health sectors to increase their marketing ratio on the local market from 30% to 100% in 2020.	
• Permission for fully exporting companies in other sectors to increase their local market marketing ratio from 30% to 50% in 2020.	
• Exemption from late tax payment penalties for a period of up to 6 months of companies with public contracts whose implementation has been disrupted by the coronavirus.	
• Creation of a cell within the Presidency of the government to support the companies most affected by the pandemic. The aim is to avoid loss of jobs. The cell will be made up of representatives from MoF, the Ministry of Social Affairs, Utica, UGTT, UTAP and APTBEF. The definition of "business affected by the pandemic" will be clarified later by a government decree after consultation with the monitoring unit at the level of the presidency of the government. The ministry said the cell will be responsible for monitoring the implementation of these measures, as well as ensuring respect for workers' rights and guaranteeing jobs.	

Source: Tunisian authorities.