COVID-19, Challenges and Opportunities
The case of Tunisia
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Summary

Given the growing impact of COVID-19, the initial measures taken by the Tunisian authorities failed to address the second wave effectively. After providing an overview of the Tunisian public debt situation prior to the pandemic and of the subsequent challenges posed by the Covid-19 crisis, the brief suggests additional measures to counter the effects on the national economy. Short-term measures include extending support to SMEs that are the real lever of the Tunisian economy. Medium-term measures include increased support to modernize the health sector and actions in the financial sector such as reducing the key interest rate to stimulate domestic private investment. Overall, policy coordination between the fiscal and monetary authorities will be needed and the «welfare state» should regain its place and play its role in the field of social security and in the realization of a public-private duality in all sectors (health, education, transport etc), ensuring social and economic equity.

Introduction

Faced with the threat of the «COVID-19» pandemic, Tunisian public institutions succeeded in adopting effective emergency measures that helped contain the first wave of this pandemic. This was largely the result of well-coordinated efforts between the various components of the Tunisian economy (citizens, medical sector, public and monetary authorities, etc.). Their cooperation was essential to contain the immediate damage of the pandemic. However with the second wave which started at the end of July 2020, the authorities have been less successful in coping with the renewed outbreak, especially as they have been facing a very difficult budgetary situation.

Indeed, given the current socio-economic situation in the country, coping with the economic and social after-effects of Covid-19 is by no means an easy task. It requires the mobilization of very substantial financial resources estimated at several billion dinars, to support, in particular, the most vulnerable social classes, the sectors of activity most affected by this pandemic as well as post-COVID-19 national recovery.

The aim of this policy brief is to identify measures that, on the one hand, would contribute to the mobilization of the required resources and on the other stimu-
late the recovery of the national economy in the wake of the Covid-19 crisis thereby laying the foundations for a new socio-economic model of development.

The brief is divided into three sections: (1) the Tunisian public debt situation prior to the Covid-19 crisis (2) the economic and social challenges posed by the Covid-19 crisis and (3) proposed institutional, economic and social reforms to cope with this crisis at the same time, help steady the country's democratic path.

I. Tunisian public debt prior to the COVID-19 crises: a brief overview

With continuous fiscal deficits, varying over the years but showing an increasing trend after 2011, the Tunisian authorities have constantly resorted to public borrowing to accommodate mounting budgetary obligations. As shown in Figure 1, the budget deficit that had decreased to 1 percent of GDP by 2010 showed a trend reversal after the uprising. It climbed to 3.3 percent for 2011, 5.5 percent for 2012, and 6.9 percent for 2013. In the subsequent six years it tended to decline, reaching 3.5 percent of GDP for 2019; but it is estimated to rise again to about 6 for 2020.

Similarly, whereas prior to the uprising the level of public debt had been declining, standing at 49 percent of GDP at end 2010, since then the trend has turned around. By the end of 2019 it stood at 75 percent of GDP climbing to 80 percent at the end of the first semester of 2020. More than two thirds (69.7 percent) is denominated in foreign currency. This total debt is higher than the average public debt held by non-residents for the EMDE (emerging markets and developing economies) estimated at about 67 percent of GDP for that year [1].

The severity of the debt issue since 2010 is related to the depreciation of the dinar, increasing fiscal and current account deficits, a generally declining rate of growth and a rising level of unemployment (around 15 percent for 2019 and 18 percent at the end of June 2020). In turn it resulted in a slowdown in public investment, especially in infrastructure. The share of investment spending in total public spending declined from 30 percent for 2010 to 17.4 percent for 2019 and 13.4 percent for the first semester 2020 [2].

Indeed, the current account deficit remains a growing source of vulnerability. It stood at around 7.8 percent of GDP in 2019 compared with 4.8 percent in 2010. While the depreciation of the Dinar was expected to strengthen the current account, in fact, it did not stimulate the rate of exports as expected whereas, in view
of the inelasticity of the demand for imports, they kept constantly increasing. Thus, the depreciation of the dinar did not lead to the desired adjustment of the current account.

Against a background of slower economic growth since 2012, the country’s ability to honor its external commitments without resorting to new debt has given rise to a vicious circle of financing that will disadvantage future generations and increase concerns over the sustainability of Tunisia’s debt, especially that it has been mainly used to finance wages and other compensatory payments, rather than investments that widen the country’s production capacity [3]. Indeed, Tunisia may not be able to avoid a forced renegotiation or restructuring of its debt in the near future.

Not surprisingly, the evolving Tunisian debt situation has given rise to grave national concerns. Even before the recent pandemic crisis there were fears that continued dependence on external borrowing would continue to put pressure on the exchange rate and promote economic instability and consequently discourage potential private investors from investing in the national economy[4]. With the pandemic outbreak there are increasing fears that high indebtedness shall further weigh heavily on long-term growth by increasing the risk of recession, by limiting the possibilities for countercyclical fiscal stimulus and by curbing private investment (see Rogoff 2020)[5].

II. Impact of the COVID-19 crisis: a brief overview

One immediate impact of the COVID-19 outbreak is the significant additional internal and external financial burden it has imposed on an already strained governmental budget. Meeting unanticipated additional obligations on account of this crisis, especially foreign obligations, has greatly added to the budgetary challenges faced by the government amidst a declining national economic growth.

The engendered health crisis apart, a major challenge facing the Tunisian public authorities is that the distancing measures they have implemented[6] to control the spread of COVID-19, have further slowed down or even halted activity in most sectors of the economy putting a brake on reversing the declining trend of economic growth: for the first quarter of 2020, the rate of growth was a negative -2.2 percent and for the second quarter it is estimated to have declined by a dramatic 20.4 percent (National Institute of Statistics, 2020)[7]. The industrial sector fell by 47.8 percent, followed by the services sector (-30.4 percent) and agriculture (-3.6 percent). Indeed, what compounds the negative impact of this decline is that it comes on top of downward growth trend Tunisia has been experiencing since 2007 (see Figure 2), mainly due to the lack of necessary economic reforms, inefficient policies but also to the slowdown in global growth.

![Figure 2. Evolution of external debt and GDP](Source: By author based on National Institute of Statistics Data.)
The decline in economic activity resulting from the COVID-19 crisis, in turn, has had a negative impact on employment. The overall unemployment rate increased from 15.1 percent for 2019 to 18 percent for second quarter of 2020[8] (figure 3).

But at the sectoral level, the services (Hotel and restaurant, transportation and commerce) and manufacturing sectors were the hardest hit followed by the non manufacturing industries and agricultural sectors (Fig 4); by contrast banking and insurance services remained relatively unaffected. The total number of unemployed increased in the second quarter of 2020 to 746.4 thousand of the total labor force, compared to 634.8 thousand unemployed in the first quarter for the same year.

According to a survey conducted by the National Institute of Statistics on «indicators of informal employment 2019», published in September 18, 2020, a total of 1.598 million people worked there, against 1,976 million working in the formal sector. This represents 44.8 percent of jobs in Tunisia. It should be noted that workers in the informal sector live in total precariousness particularly without any social security coverage and in this pandemic context and social distancing it is difficult to identifying them in order to provide them with assistance. It is estimated that the informal sector provides employment for over 86 percent of the workers in the agriculture and fisheries sector compared to 69 for the construction and public works sector and 65 percent for the trade sector.

Given the complexity of the employment situation and this second wave of the pandemic, the Tunisian authorities are called upon to take immediate reform measures to stabilize the economic situation and prevent the country from sinking into an endless turmoil. This means Tunisia must meet several challenges in different time frames but above all in a global macroeconomic framework where the authorities must orient their short and medium strategies towards an optimal allocation of available resources (detailed in section III) in order to generate a turning point and reverse the curve of declining economic growth.
Of course, the magnitude of the financial impact of the pandemic on the most vulnerable classes and businesses depends on their sizes, sectors activities and their integration into the international markets. Whatever economic and fiscal measures the current government has initiated, or should initiate to meet the crisis (discussed in section III below), it should aim at countering the increase in unemployment and the loss of markets. It should also endeavor to preserve the purchasing power of the poorest class and the middle class, the latter being the engine of economic dynamism that would guarantee the resumption of economic activity in the post crisis phase. Hence, the government should not necessarily rely on raising income taxes or cutting public service salaries, as suggested by some economists and politicians. However, new taxes on properties and patrimonies may be introduced.

The support measures taken by the government (equivalent to 1.9% of GDP) to limit the impact of COVID-19 on the various economic agents, particularly the social categories most affected by social distancing have certainly been relevant, but have been introduced at the cost of equipment and capital expenditures which have been reduced by almost one half (equivalent to 3.2 percent of GDP). But, as the authorities face financial constraints, an immediate assessment of already existing resources in the economy (human and financial) is called for to help identify needed external aid in support of internal efforts to overcome the economic and fiscal impact of the crisis in addition to what Tunisia has already received since the eruption of the Covid-19 pandemic[9]: altogether foreign aid has so far amounted to US $ 1.738 billion (equivalent to 76 percent of public debt service for 2020) providing needed balance of payment support.

Clearly Tunisia faces key growth, fiscal and balance of payment challenges in overcoming the economic and financial impact of the Covid-19 crisis and for setting the stage for future sustainable development. Section III outlines the needed policy initiatives.

III. Policy Reform Measures

In attempting to cope with the renewed outbreak of the second wave of the pandemic (see Appendix Figure1) the authorities need to undertake a number of both short-term measures as well as longer term ones. The following measures are suggested.

III.1. Short term measures include:

1) **Strict compliance with social distancing by enforcing distancing measures.** The adoption of smartphone applications that allow the detection of new COVID-19 cases in real time helps monitor compliance
with the measures in place. In May, Tunisia already launched a tracing application (E7mi) to fight the spread of the coronavirus.

(2) Protecting large companies specifically operating in the industrial sector such as the mechanical and electrical and agro-food sectors. Equally, support should be extended to SMEs that are the real lever of the Tunisian economy. Specifically, their cash flow should be maintained to ensure they continue to support their workers and avoid a further increase in unemployment, which rose to 18 percent in the first half of 2020. It should be noted that, despite the aid announced by the government in April 2020, the results of the «MIQYES» survey[10], of September 23, 2020, indicates that in August 2020 only 18.4 percent of the SMEs requesting assistance had effectively benefited from government support measures in response to crisis. Among the surveyed SMEs, 17.6 percent reported they were still not operating while 50.4 percent considered the recovery to be very slow and damaging.

(3) The government, till now was able to negotiate with its financial partners medium-term credit and grants[11] to strengthen the capacity of the health sector, protect vulnerable businesses and households from the effects of the COVID-19 crisis, and accomplish essential economic reforms to enable Tunisia to improve its recovery potential after the crisis. But unfortunately, most of these funds were used to finance the primary budget deficit to the detriment of the health sector, which has proved powerless in the face of the current second wave of coronavirus. To ensure that funds will be used optimally, an option where they could be placed in an account audited by a specialized committee made up of representatives of donors and the government could be explored.

(4) It is necessary to efficiently address the overcrowded public transportation sector to control the spread of the virus particularly in large cities, through the development of phone applications that organize and control carpooling.

III.2. Longer term reform measures
They may be divided into two categories: those related to two sectors (heath and finance) where specific measures can be applied to counter the impact of the pandemic and those of a more general nature intended to reinvigorate the national economy in the wake of COVID-19 and its generally negative economic effects.

III.2.1. Measures in the Health and Finance sectors
(1) Concerning the health sector, in addition to measures already taken by the public authorities in terms of revision of the 2020 finance law for the benefit of the health sector and assistance to vulnerable classes, it is imperative that the government continues investing in the public health sector by creating niches of hospitals thereby increasing their capacity to serve the entire population in both urban and rural areas. It is also necessary to invest in the acquisition and installation of modern equipment which will allow access to an efficient and digital health system. This would help alleviate disadvantaged regions’ deprivation from poor health infrastructure and additionally encourage well trained and competent health staff to remain in Tunisia instead of seeking to emigrate, a growing phenomenon since 2012.

(2) Regarding the financial sector, the Central Bank, in response to this pandemic crisis situation, has:
   a) provided banks with the necessary liquidity[12] by suspending the rules on the eligibility criteria for guarantors’ assets so that they can continue to finance the government deficit and grant individuals and companies, affected by the current crisis, the possibility to defer payment of the shares of maturing credits (capital and interest) during the period from March 1 to the end of September 2021.
   b) rescheduled the repayment of bank credits according to the capacity of each beneficiary while having the possibility of obtaining new financing;
   c) relaxed the calculation and requirements of the credit/deposit ratio;
d) **Lowered the BCT’s key interest rate** by 50 basis points to 6.25 percent in October 2020, which will ease the financial burden on individuals and companies that have taken out variable-rate loans.

These measures are necessary but not sufficient to support the government in achieving its emergency objectives, preserving financial stability and reviving economic activity. Thus, the BCT could also:

- e) ask banks and financial institutions to **suspend the distribution of dividends** for the fiscal year 2020;
- f) adopt **unconventional measures** such as:
  - The purchase of treasury bills held by banks,
  - Reduce the BCT’s key interest rate significantly in order to restore confidence in monetary policy and stimulate domestic private investment in a country that is struggling to attract foreign direct investment;
  - alleviate the financial burden on individuals and businesses that have taken out variable-rate loans;
  - Exercise a policy of targeting credit to strategic sectors.

- g) Adopt new **social finance instruments to help improve public social services**. Indeed, the issue of regional development will come to the fore at the end of this crisis whose brunt the disadvantaged classes will bear; hence the urgency of identifying and implementing innovative and effective projects so as to avoid a widening of the social gap and establish a first nucleus of trust between the authorities and this marginalized class. **Sustainable finance instruments**, such as participatory finance (crowdfunding), SIB (Social Impact Bonds) and microfinance have proven to be effective in encouraging private investment in social projects[13]. Meanwhile, the development and catching-up of regions cannot be done without public investment in large innovative projects that create jobs.

### III.2.2. Measures to stimulate the National Economy

1. It appears essential to promote the **mobility of workers** in the public sector towards activities and regions experiencing a labor shortage in order to ensure better allocation of resources along with the implementation of other measures that enhance productivity in this sector.

2. Similarly, it is urgent to **reform educational, scientific research and vocational training** with the objective of rendering them more transparent in terms of prioritizing and allocating the use of funds. This would lead to a more efficient employment policy of graduating classes in the job market and enhance Tunisian human capital, the most important ingredient in the country’s development. However, this reframing needs to be backed by national consensus as it involves decisions on the nature of the knowledge to be acquired, both general and specialized, to form a qualified and creative workforce that masters new technologies and digital knowledge in different fields to better meet the needs of the domestic economy. Without an infrastructure of quality with regards universities and training centers, it is difficult to provide a skilled and employable workforce and therefore absorption rates in the labor market will remain low.

3. For the transport sector in the medium term, **the government should maintain and adapt hundreds of kilometers of railway lines to current standards**. This calls for a national investment strategy to develop and modernize the railway network and make it a means for reducing inequalities.

4. It is important to **control inflation** in order to avoid potential shocks in prices and the exchange rate, following the resumption of active foreign trade, after the abolition of measures adopted by Tunisia and its main trading partners as a consequence of the pandemic. These measures included the temporary closure of borders resulting in price increases of imported products, particularly cereals.

5. The momentum of **digitalization** adopted in Tunisia during the confinement period, particularly at the level of administration, distance education and the banking sector should be generalized to all sectors and economic activities in order to “ensure the traceability of operations and fight against corruption”.
(6) Since 2011 the authorities have been struggling with the issue of rising unemployment as well as with the slowing down of the country’s competitiveness vis-à-vis the European market. What is called for is an active policy for diversifying Tunisia’s trading partners and deploying its efforts to orient its development policies quickly in the direction of creating conditions conducive to the achievement of the objectives of the COMESA treaty.

(7) Finally, authorities should invest in the modernization of the agricultural sector which, despite its vulnerability, remains strategic and of undeniable «economic and socio-political» importance in terms of food security, poverty reduction and the creation of employment and its role in exports. Indispensable strategies and measures must be adopted to make it solid and competitive before moving on to the realization of a Deep and Comprehensive Free Trade Agreement (DCFTA).

Conclusion

Given the growing impact of COVID-19, the initial measures taken by the Tunisian authorities failed to address the second wave effectively. Additional measures, such as those proposed above, are essential in countering COVID-19 effects on the national economy and minimizing its multiple costs. This would require properly implemented policy coordination between the fiscal and monetary authorities and the «welfare state» should regain its place and play its role in the field of social security and in the realization of a public-private duality in all sectors (health, education, transport etc), ensuring social and economic equity.

Given the vulnerable national macroeconomic context prior to COVID-19 and the magnitude of the impact of the pandemic, more effective international cooperation is needed in combatting this pandemic, while economic collaboration should also be promoted. This would allow for national efforts to be more successful in ensuring the recovery and to prepare Tunisia for the geopolitical and economic changes that will take place after this crisis.

Appendix

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<th>Table 1. Public deficit and External debt estimation</th>
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<td>Public Deficit</td>
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<tr>
<td>----------------</td>
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<tr>
<td>2017 -5,4percent</td>
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<tr>
<td>2018 -4,8percent</td>
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<td>2019 -4,1percent</td>
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<td>2020a -5,0percent</td>
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<tr>
<td>2021a -3,8percent</td>
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<td>2022a -2,9percent</td>
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Source: World Bank data
Figure 1. Evolution of the number of COVID-19 contaminations

Source: By author data base of Coronavirus Statistics in Tunisia (https://www.coronavirus-statistiques.com/stats-pays/coronavirus-nombre-de-cas-tunisie/)

Figure 2. Evolution of FDI by sector for the First trimester (MDTN)

Source: National Institute of Statistics Data

Notes


[4] Dufrénot and Paret determine the main characteristics of economies carrying a large debt risk as follows: (i) the exchange risk is strongly determined by the fraction of public debt denominated in foreign currency, (ii) a low level of credibility of economic policies due to the lack of commitment from the public and monetary authorities; and (iii), instability in terms of growth, interest and inflation for example (Dufrénot and Paret (2016), Power-Law Distribution in the Debt-to-Fiscal Revenue Ratio: Empirical Evidence and a Theoretical Model, Working paper HAL, https://halshs.archives-ouvertes.fr/halshs-01357797/document).
Since the announcement of the first case on 2 March 2020, the Tunisian government put in place a series of measures to mitigate the health, economic, and social effects on the Tunisian economy and the most vulnerable members of Tunisian society. These measures had a positive impact on COVID-19 containment. The government on 22 March shut down the national borders, stopped non-essential activities, closed restaurants and cafés, and, for companies wishing to continue working, allowed them to only use 15 percent of their workforce.


Tunisia received two European Union loans concessional terms. The first is a 600 million euro loan in the form of «macro-financial assistance from the European Union (EU). The second amounts to SDR 545.2 million (equivalent to $745 million, or 10 percent of the quota) under the Rapid Financial Instrument (RFI). These resources were used to meet the urgent budget and balance of payments financing needs caused by the COVID-19 pandemic in order to mitigate its humanitarian, social and economic impact. In addition, IMF financing has helped to ensure an adequate level of international reserves to mobilize additional donor financing. Tunisia has also benefited from two other European donations. The first is 250 million euro donation extended in the form of budget support to fight against this pandemic, and the other is a 60 million euro donation extended to support the «Health / Essaha Aziza» program. (“Situation sanitaire, impact socio-économique et mesures (22/4) », World Bank Publication).

At the end of April 2020, the World Bank approved a $20 million project to support Tunisia in the face of the COVID-19 pandemic by strengthening the capacity of the health sector. June 12, 2020 a budget support of $175 million allocated under the Emergency Operation in Support of Development Policies for Resilience and Recovery. The financial envelope of the joint operation will amount to between $600 million and $700 million in 2020 granted by the German bank KfW, the French Development Agency (AFD), the Japan International Cooperation Agency (JICA) and the African Development Bank.

The overall volume of refinancing increased by 17 percent at the end of July compared to June 2020, after declines in the previous three months.


The recent coronavirus crisis threatens the health, economies and societies of all countries, regardless of level of development. In the South Mediterranean countries the fight against the pandemic is even more complicated. It must be done with limited health and economic resources compared to other regions. In addition, it takes place in a unique social and geopolitical context.

Cooperation and EU-Med strategies in key sectors are needed. Therefore, CMI and FEMISE have decided to join forces and launch this series of Policy Briefs to pave the way for thematic analyses and prescriptions, which will be explored throughout this series.