TUNISIA

WALKING A TIGHTROPE

Hard hit by the Covid crisis and the consequences of the war in Ukraine, the Tunisian economy is now facing significant financing constraints. External accounts held up fairly well in 2023, but the macroeconomic situation remains very fragile. Debt repayments for this year are significant, and the country is not immune from another shock. In particular, the prospect of rapprochement with the IMF seems less and less likely, fuelling fears about the government's ability to cover all its financing needs. A debt crisis cannot be ruled out.

IMF AGREEMENT IN 2024 SEEMS UNLIKELY

Tunisia is walking a tightrope without a real safety net. This is expected to be the case once again in 2024. The presidential elections held in the autumn have reduced the prospect of an agreement with the IMF; reaching this agreement would however help unblock most bilateral and multilateral assistance programmes. The IMF's assistance remains conditional on implementation of reforms that President Saïed has largely rejected, due to a social cost considered too high (restructuring of public companies, overhaul of the subsidy system). Officially, discussions have not broken off and new terms, taking into account the concerns of the Tunisian authorities, could contribute to reconciling positions. But this scenario seems unlikely. Any agreement with the IMF will require budgetary efforts, which are all the more difficult to implement since the very low participation rate in the local elections in December is evidence of latent grass-roots dissatisfaction. The stability of the foreign exchange reserves of the central bank (BCT) in 2023 probably also reinforced the authorities' idea that the economy could do without financial support from the IMF. Considering this year's significant financing needs, this strategy is nevertheless risky.

PUBLIC FINANCE: VERY HIGH FINANCING RISK

Despite the dissipation of the terms-of-trade shock linked to the conflict in Ukraine, and the moderation of civil servants' wage bill growth, the budget deficit barely stabilised in 2023, at 7.7% of GDP. This is 2.5 points higher than in the initial Finance Bill. For 2024, the adjustment should remain modest, with a budget deficit of 6.6% of GDP expected by the government.

Subsidies on energy and base products will remain a heavy burden on the budget. After doubling in 2022 to reach a record level of 8.3% of GDP, subsidies only fell very slightly in 2023 to 7.2% of GDP, compared to 5.5% budgeted. According to government forecasts, they are still expected to reach 6.5% of GDP this year, i.e. almost 20% of spending. By way of comparison, this item represented 12% of spending on average between 2015 and 2021. Further slippages should not be precluded, bearing in mind the volatility of global commodity prices. Added to this is the increase in interest costs, which have exceeded 10% of budget expenditure for the first time since early 2010. The debt burden is the result of an accumulation of high budget deficits and increased recourse to domestic financing on terms less favourable than those granted by official external creditors. However, this trend is not set to reverse.

Unless the budget deficit narrows more than expected, the Tunisian government's financing needs will exceed 17% of GDP this year (see Chart 1). Debt amortization will count for two-thirds of this amount. This is huge and incommensurate with the pre-pandemic situation, when financing needs were around 8-9% of GDP. The authorities' ability to cope with this remains very uncertain. In fact, 57% of the financing plan included in the budget is based on external resources, of which only one-third have been identified.

FORECASTS

	2021	2022	2023e	2024e	2025e
Real GDP growth (%)	4.6	2.6	0.6	2.2	2.0
Inflation (CPI, year average, %)	5.7	8.3	9.3	8.0	7.0
Central gov. balance / GDP (%)	-7.9	-7.7	-7.7	-6.6	-6.1
Central gov. debt / GDP (%)	79.9	79.8	79.7	80.7	81.6
Current account balance / GDP (%)	-6.0	-8.6	-3.8	-4.4	-4.7
External debt / GDP (%)	91.6	90.8	86.4	86.3	86.5
Forex reserves (USD bn)	8.4	7.7	8.3	8.0	7.9
Forex reserves, in months of imports	4.2	3.2	3.5	3.2	3.1

TABLE 1

e: ESTIMATES & FORECASTS
SOURCE: BNP PARIBAS ECONOMIC RESEARCH

TUNISIA: GOVERNMENT FINANCING NEEDS

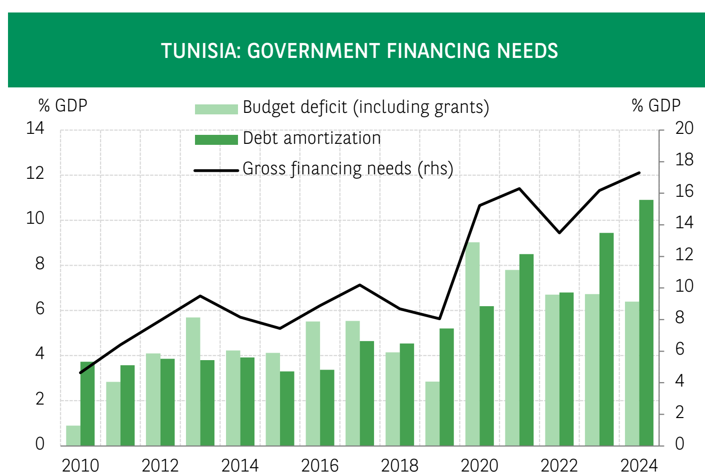

CHART 1

SOURCE: MINISTRY OF FINANCE, BNP PARIBAS

The government is counting on official external financial support, but the repeated budgetary underperformances of recent years call for caution. At the end of September 2023, the government had succeeded in mobilising only 28% of the external resources planned in the initial budget. Without an agreement with the IMF, such a scenario is therefore likely to recur, leaving a gap of 12-13% of GDP to be covered in a shallow domestic bond market. Standing at 15% at the end of 2019, banks' exposure to the public sector, in the broad sense (corporates and government), rose at the end of 2019 to 20% of the assets of the entire system.

Moreover, the overall volume of bank refinancing with the Central Bank increased by 43% in 2023, of which more than one-third in the form of open market operations compared to less than 20% in 2022. However, a minority of these open market operations are used for monetary policy purposes. In other words, the monetary authorities are indirectly refinancing the government by buying back treasury bills on the interbank market. Measures to allow the Central Bank to directly finance the government are even being developed, which could potentially have a significant impact on inflation or exchange rates.

Liquidity risk is not the only source of concern. With debt now reaching 80% of GDP and an inexorably increasing interest burden (14% of income in 2024 compared to 10% in 2020), the government's solvency is also deteriorating dangerously. The country is now considered as just one step away from payment default by Fitch and Moody's rating agencies.

FRAGILE IMPROVEMENT IN EXTERNAL ACCOUNTS

After a difficult 2022, pressure on foreign exchange reserves has eased considerably thanks to very good tourism activity, high remittances from the Tunisian diaspora, and the fall in prices of the main commodities imported. From USD 3.1 billion over the first nine months of 2022, the current account deficit narrowed to USD 1.1 billion in 2023. According to our estimates, it is not expected to exceed 4% of GDP over the whole year, compared to 8.6% in 2022. The BCT has been able to build up some of its foreign exchange reserves (+USD 600 million). At USD 8.3 billion, they now cover 3.5 months of imports of goods and services (G&S).

External accounts remain fragile. The outlook is for a moderate deterioration of the current account deficit to 4.4% of GDP in 2024. But the significant weight of the energy imbalance in the trade balance (more than half of the deficit in 2023), or the dependence on Europe for exports, exposes the economy to a number of economic uncertainties. In addition, the country will also have to cover significant external debt amortization (USD 3.6 billion compared to USD 2.8 billion in 2023). However, funding sources outside official assistance are largely insufficient. Net FDI flows are low, around USD 500-600 million for the last four years, i.e. less than 1.5% of GDP, and they will probably stay low in the coming months due to the country's macroeconomic difficulties. With five-year sovereign risk premiums still exceeding 1,000 bps, Tunisia will not be able to turn to the international financial markets either to issue debt. Should downside risks (increase in the current deficit, insufficient financing) materialise, foreign exchange reserves could, as a result, fall below the three-month alert threshold for G&S imports with, as a corollary, strong pressure on the dinar.

Another factor illustrates the current vulnerabilities: the emergence of shortages of subsidised base products since 2022, the import and marketing of which are handled by increasingly indebted public companies. The result is a compression of imports, which may ease pressure on foreign exchange reserves for some time, but this situation cannot last in the long term.

TUNISIA: SECTOR CONTRIBUTION TO GDP GROWTH

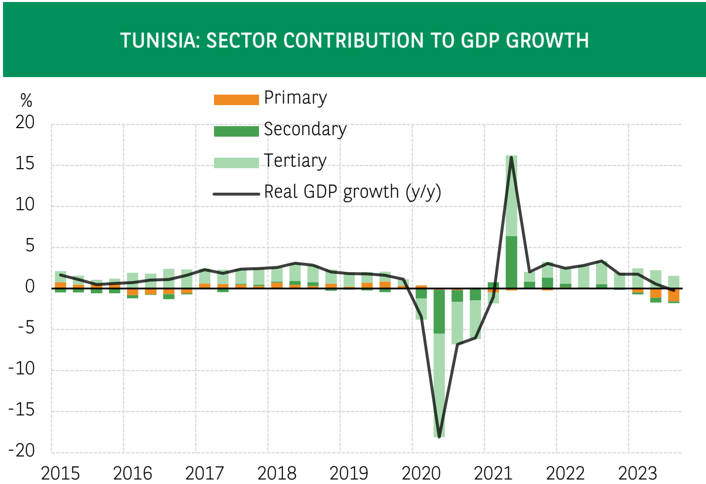

CHART 2

SOURCE: INS, BNP PARIBAS

ECONOMIC GROWTH: NO RECOVERY IN SIGHT

Against this backdrop, it is difficult to imagine how economic activity could really recover. Over the first nine months of 2023, economic growth only reached 0.7% on average (see Chart 2), its lowest level since 2011, excluding the Covid crisis. The contraction of more than 10% in agricultural value added due to severe drought, explains a large part of this underperformance. But outside the agricultural sector, growth has also stagnated. Despite the good performance of exports of manufactured products and tourism, growth stood at 1.9% on average compared to 3.1% the previous year. However, without a relaxation of financing constraints, most of the factors that weighed on the economy in 2023 are expected to persist or even worsen: crowding-out effect of bank credit in the economy due to the government's extensive use of the local market, high inflation (8.1% at the end of 2023, 12.3% on food), almost no budgetary leeway (current expenditure now above revenue). Even with an upturn in agricultural production, growth is expected to barely exceed 2% in 2024, which is too low to push down an unemployment rate of nearly 16%. Unlike almost all countries in the region, Tunisia will therefore not return to its pre-pandemic GDP until next year. This reflects the depth of a crisis in which the fall in investment by more than 10 GDP points since 2010 is one of the most striking elements. Beyond the necessary macroeconomic stabilisation, the Tunisian economy therefore needs extensive work on reforms to restore its growth potential. This will be a lengthy and risky process, especially if a debt crisis were to add to current difficulties.

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