

MCC Advisory Council

Tunisia Compact Development Update

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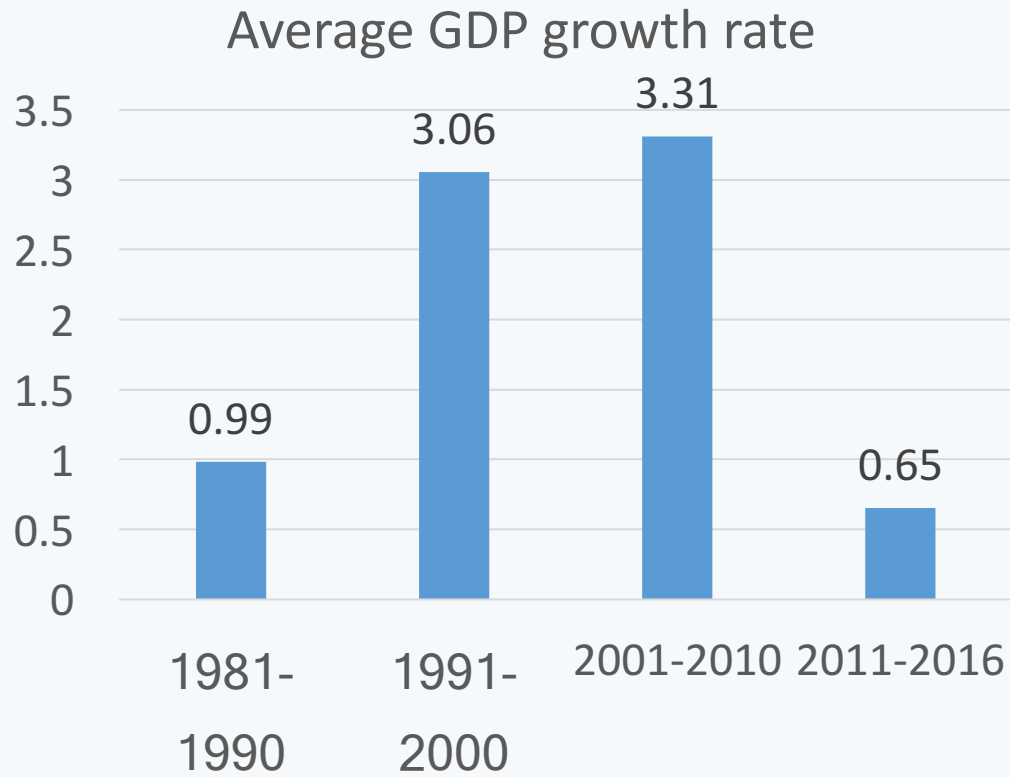
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Tunisia Country Context

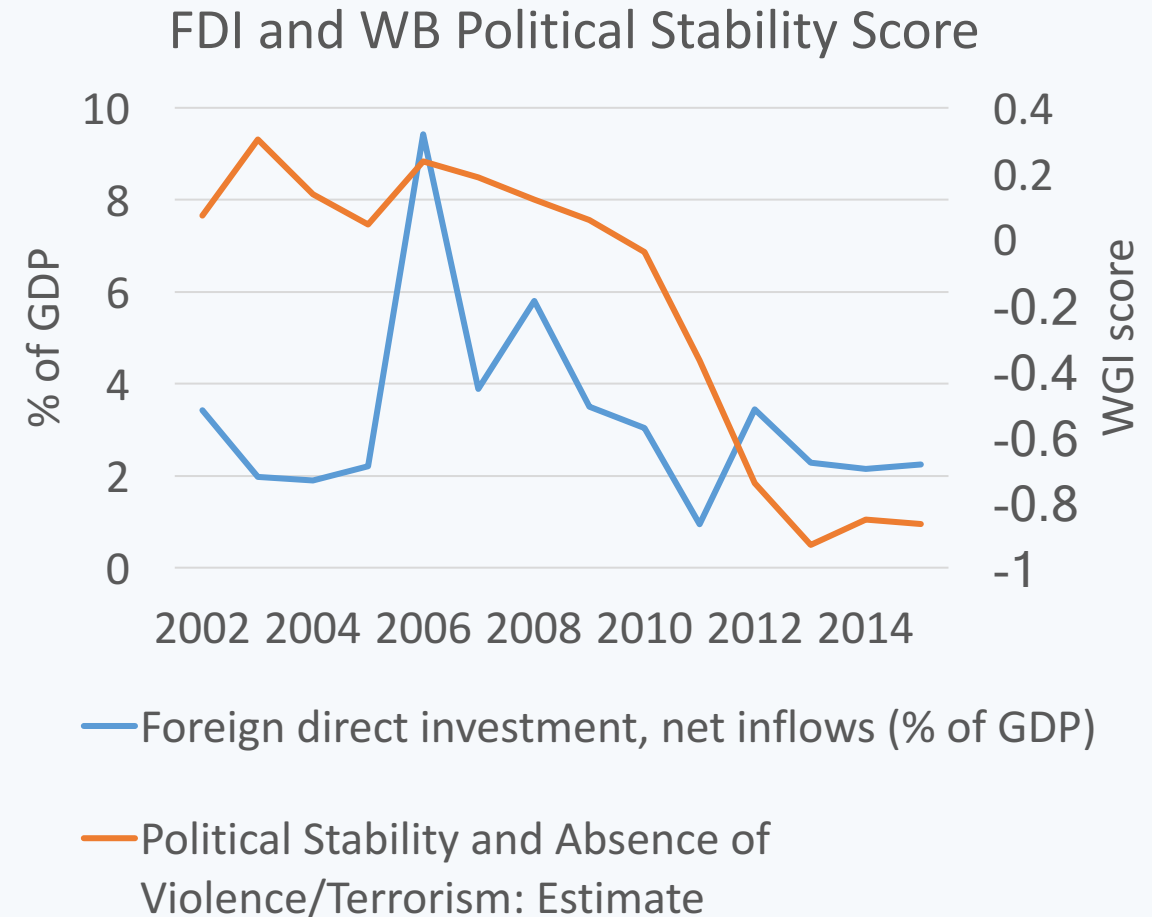
- Tunisia's democratic transition was relatively successful, economic transition from era of heavy state intervention is still work in progress
- Important and long-standing partner for USG in a volatile region
- Security situation is improving but terrorism remains a critical threat
- Political will is there today, will need to be sustained during compact
 - Address GoT Priorities of inclusive growth, decentralization & good governance
 - Assess and optimize alignment of MCC efforts with 2020 Development Plan



Tunisia's pre-2011 growth and poverty reduction were significant



Post-2011 growth and investment are low; likely due to instability, uncertainty and slow reform



Tunisia Constraints Analysis Results

- Tunisia Compact will consist of investments designed to address binding constraints to the country's long-term economic growth potential
- Binding constraints are those that, if relieved, would produce the largest gains in growth and entrepreneurship of any potential constraint areas
- Identified constraints include:
 - Excessive Market Controls
 - Rigid Labor Market Regulations
 - Water Scarcity in Interior Regions and Agriculture Sector
- Access to Finance and Human Capital not found to be binding
 - GoT requested MCC to consider finance as part of market controls

Preliminary Ideas for Compact Projects

Market Controls:

- E-government, with investment law support, administrative/regulatory guillotine, and IT infra
- Special economic activity zones in interior regions possibly focused on agriculture/agri-business
- PPP for management of port infrastructure, with customs modernization and reform

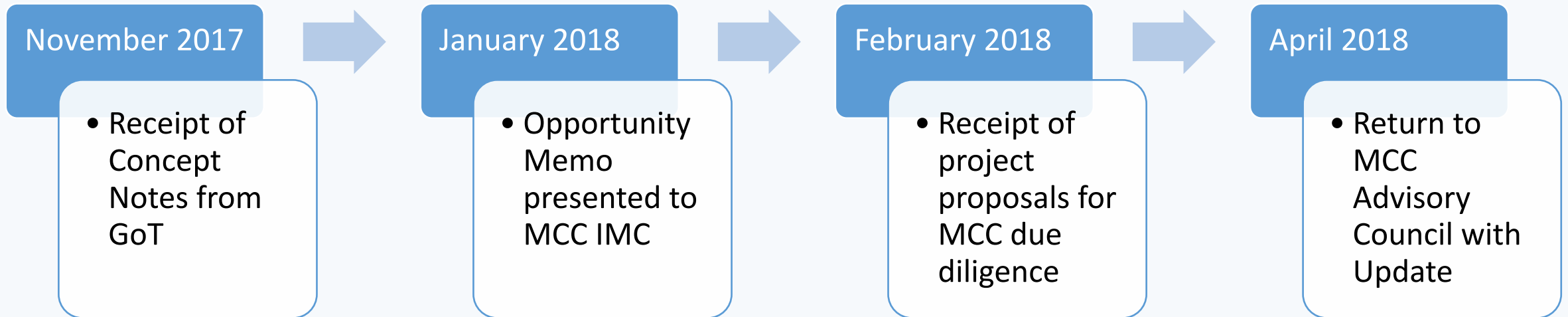
Water Scarcity:

- Reforms related to water tariffs and subsidies, coupled with potential investments in:
 - PPPs for desalinization
 - Rehabilitation of irrigation and water storage and transport networks
 - Drip irrigation, with other support for agricultural yield improvements
 - Improved supply, including rainwater capture and conservation of groundwater reservoirs

Restrictive Labor Market Regulations:

- Proposed solutions are at a preliminary stage, including targeted support for labor regulations that complement market controls or water scarcity projects
- Programs to match available labor with jobs, coupled with some limited training on soft skills

Next Steps



Issues for Discussion

General

- How do you support investments in areas with security concerns, water scarcity, or infrastructure constraints?
- How can Tunisia capitalize on their proximity to European and Sub-Saharan African markets and what is its comparative advantage versus peer countries? Are there specific companies that may want to invest?
- How might we become aware of and exploit technology to achieve our compact objectives (ie: labor market data collection, customs systems, e-government, etc.)?

Market Reforms

- How might we select and prioritize reforms that will attract private investment, maximize job growth, and impact poorer interior regions and communities?
- How might we better engage the local private sector in the reform agenda? US businesses?
- Loosening controls/subsidies may hurt businesses and employment in the short term; how should we mitigate this?

Water

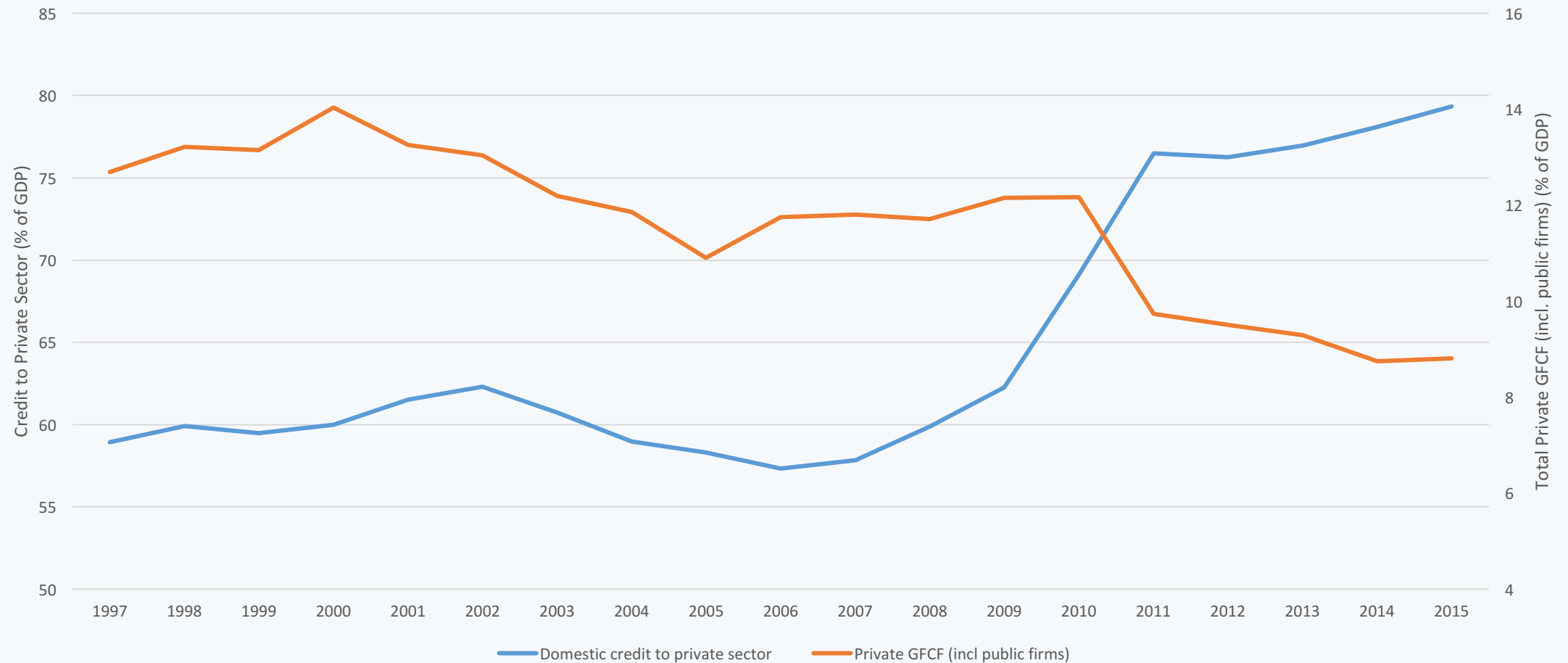
- How might we incentivize the private sector to conserve water, given that water and power are subsidized?
- What types of investments could allow us to attract businesses to interior regions while also conserving water?

Labor

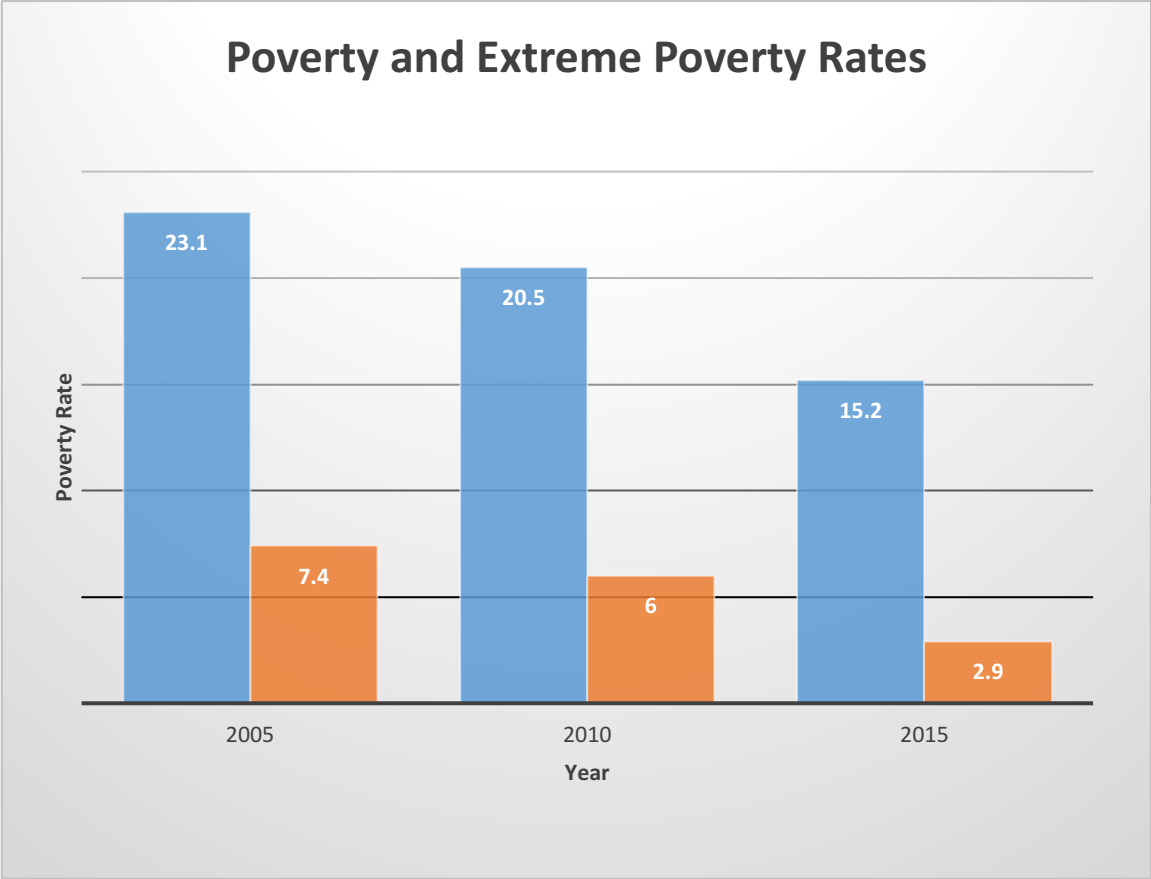
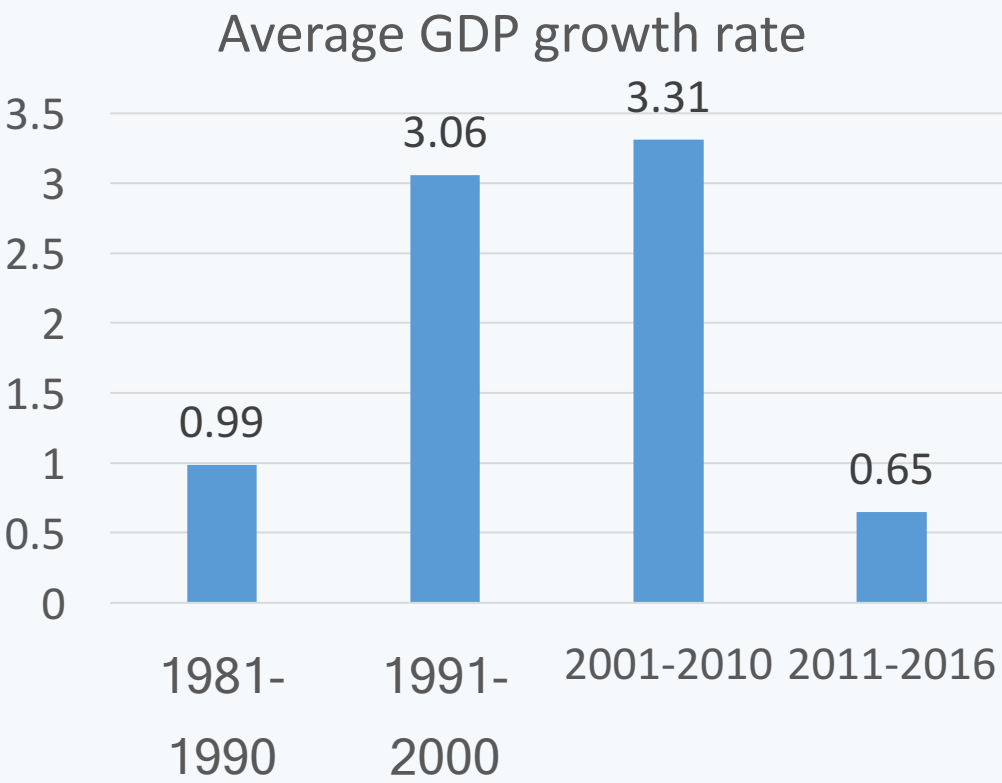
- What reforms are feasible given strength of labor unions?
- How does MCC remove labor protections without exacerbating unemployment and political instability?

Thank you

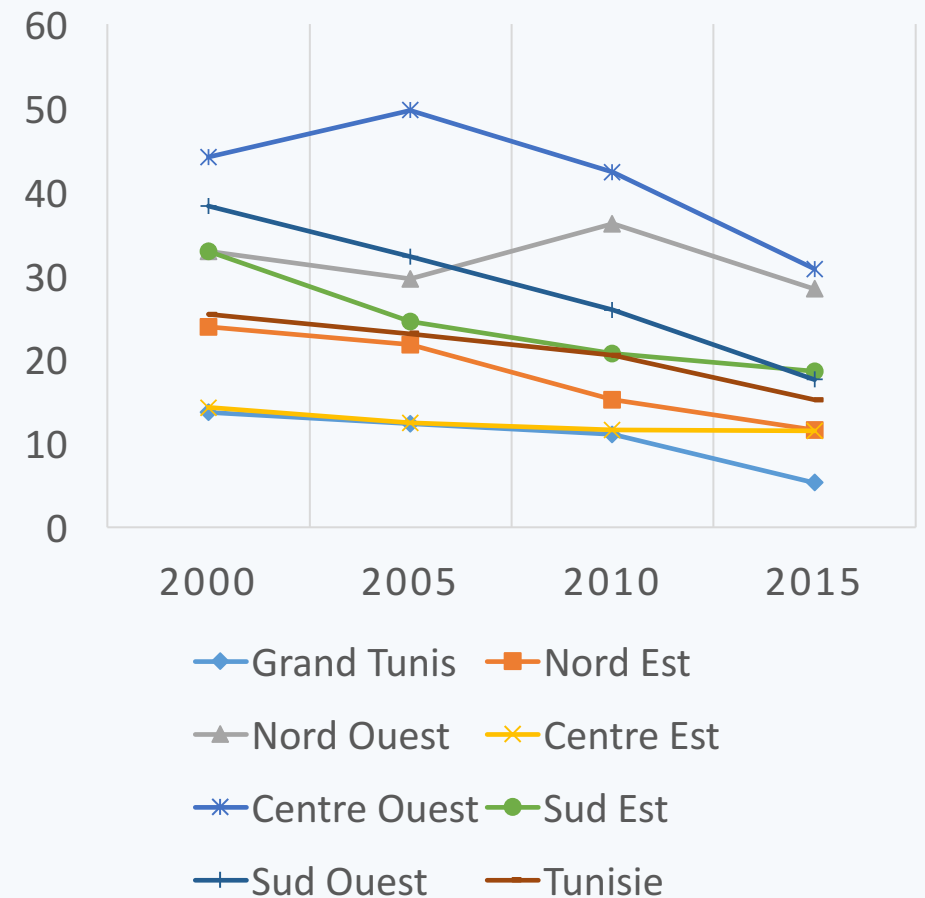
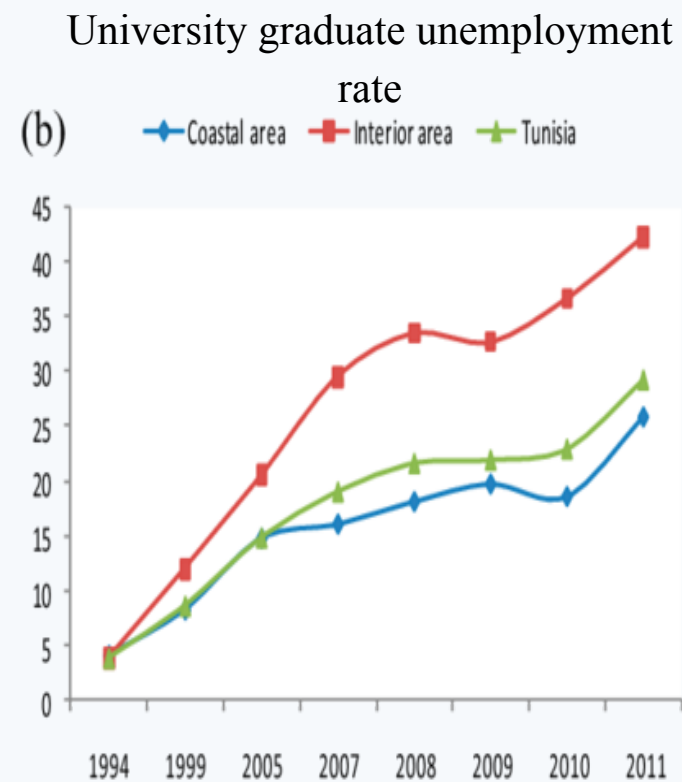
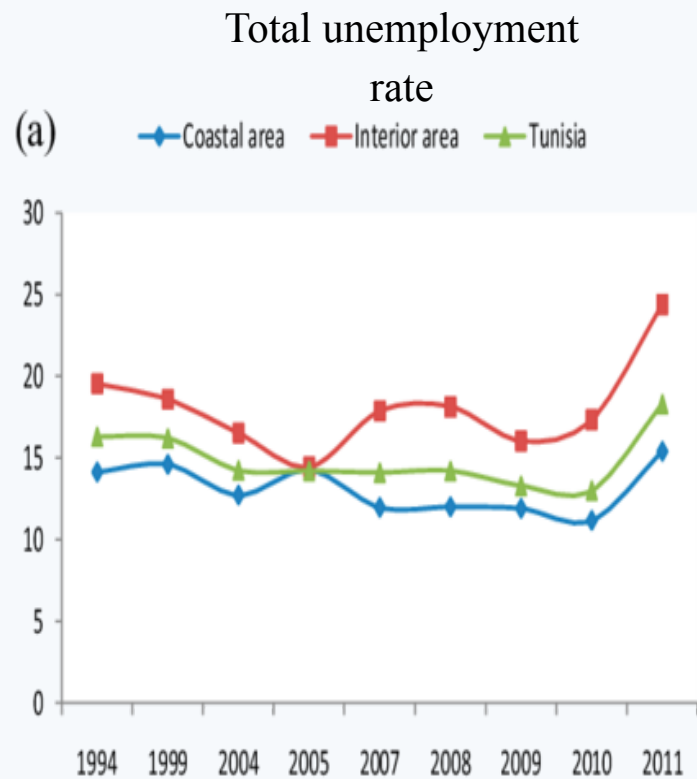
Access to Finance: Although credit is increasing, private investment is decreasing



Tunisia's pre-2011 growth and poverty reduction were significant

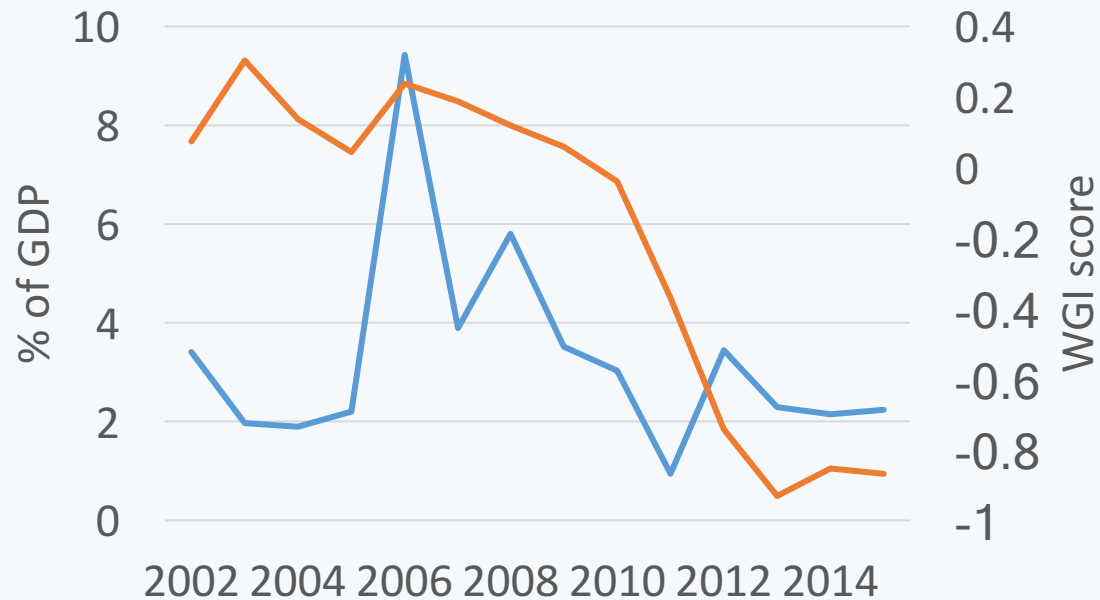


Pre-2011 growth and employment favored certain groups, areas; marginalizing interior, young graduates



Post-2011 growth and investment are low; likely due to instability, uncertainty and slow reform efforts

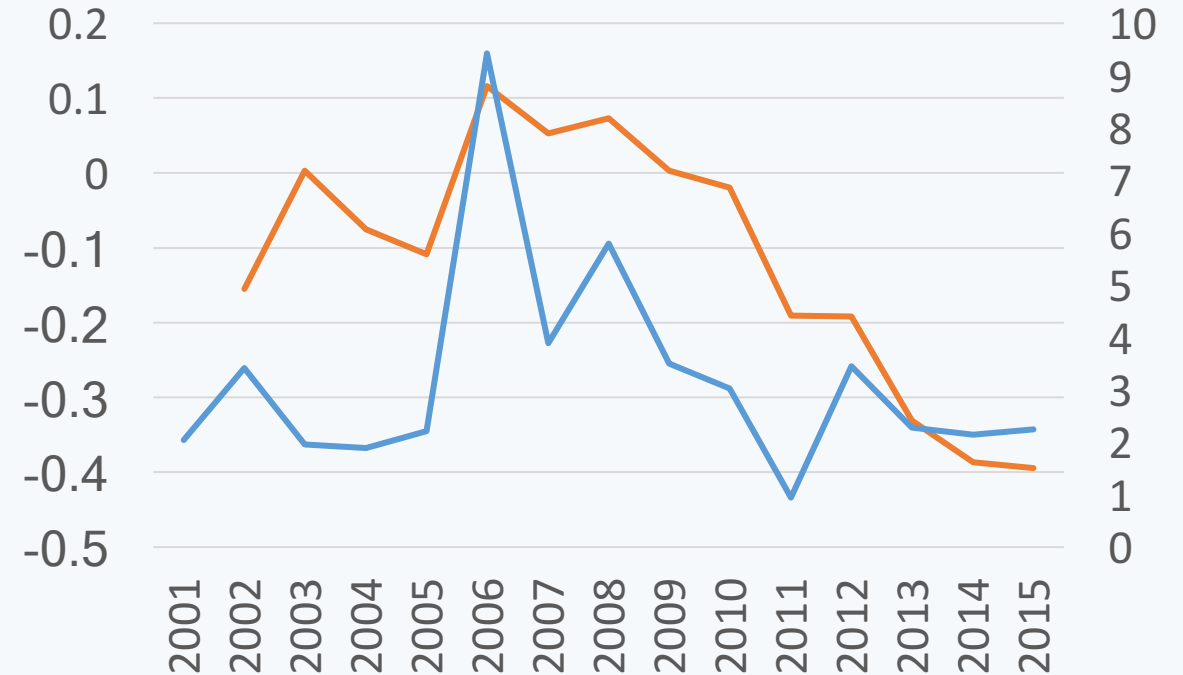
FDI and WB Political Stability Score



— Foreign direct investment, net inflows (% of GDP)

— Political Stability and Absence of Violence/Terrorism: Estimate

FDI and Regulatory Quality

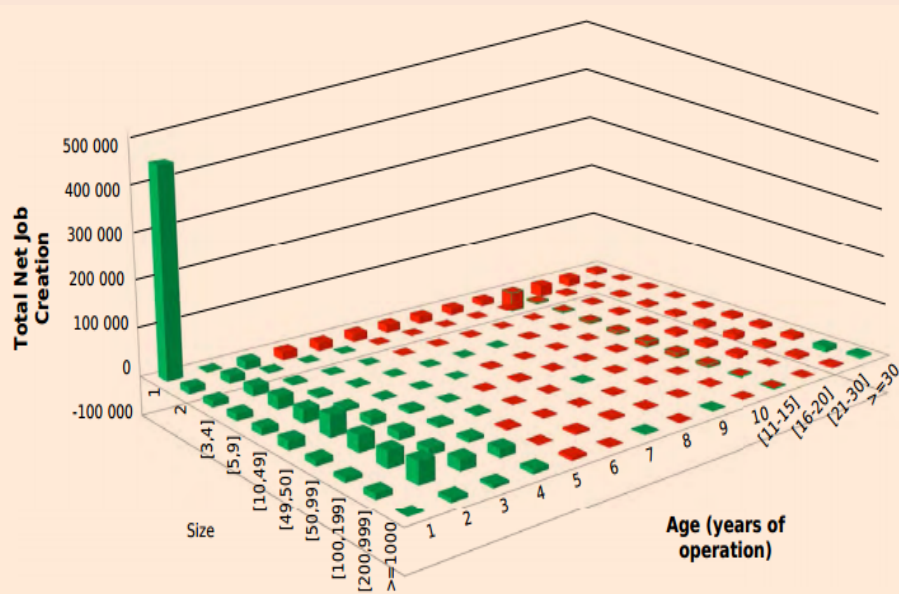


— Regulatory Quality: Estimate

— Foreign direct investment, net inflows (% of GDP)

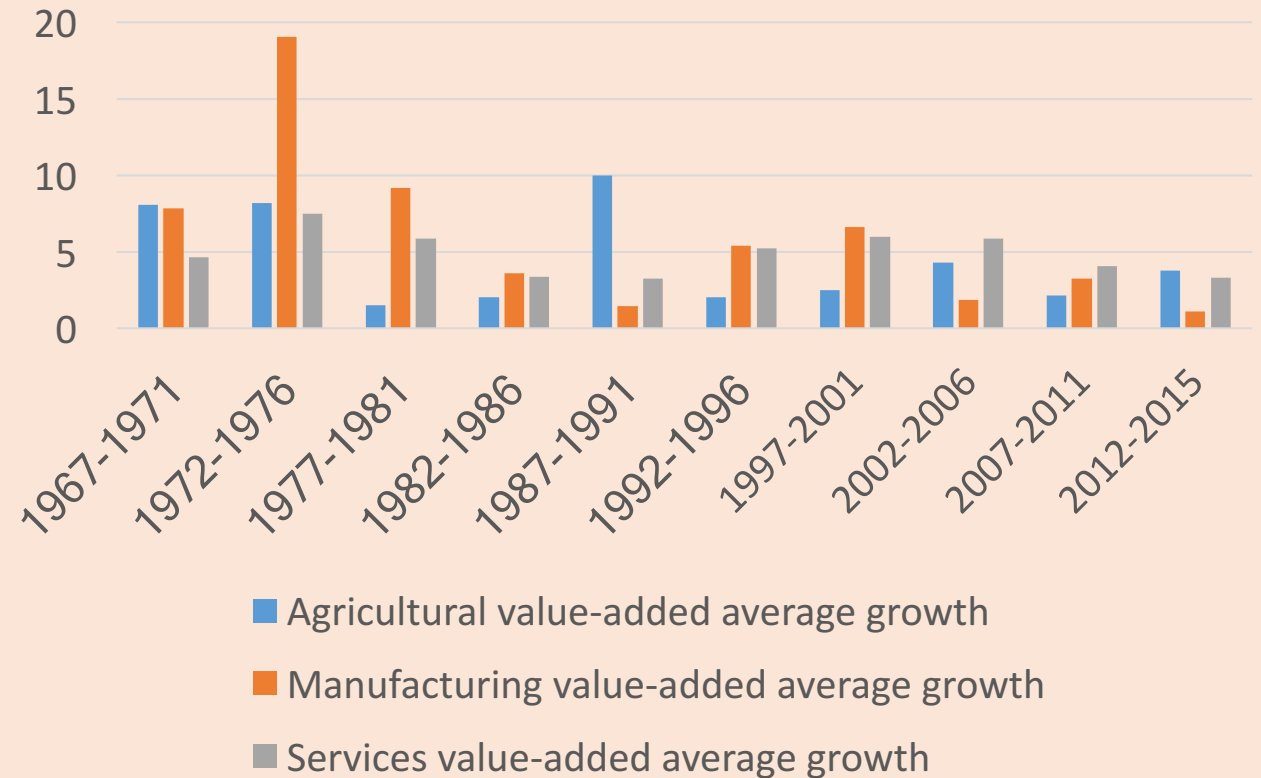
Tunisian economy lacks dynamism; resources unable to shift to high productivity uses

Firm sizing up/down is rare after 1-2 years



Source: Authors' calculations using RNE.

Average annual growth in value-added



Government of Tunisia 2020 Plan

- Participatory Approach intended to build on recent reforms and put Tunisia on the Road to “Inclusion, Sustainability & Efficiency”

1. Speed up the implementation of good governance & fight against corruption
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2. From a low-cost economy to an economic hub

3. Human development & social inclusion

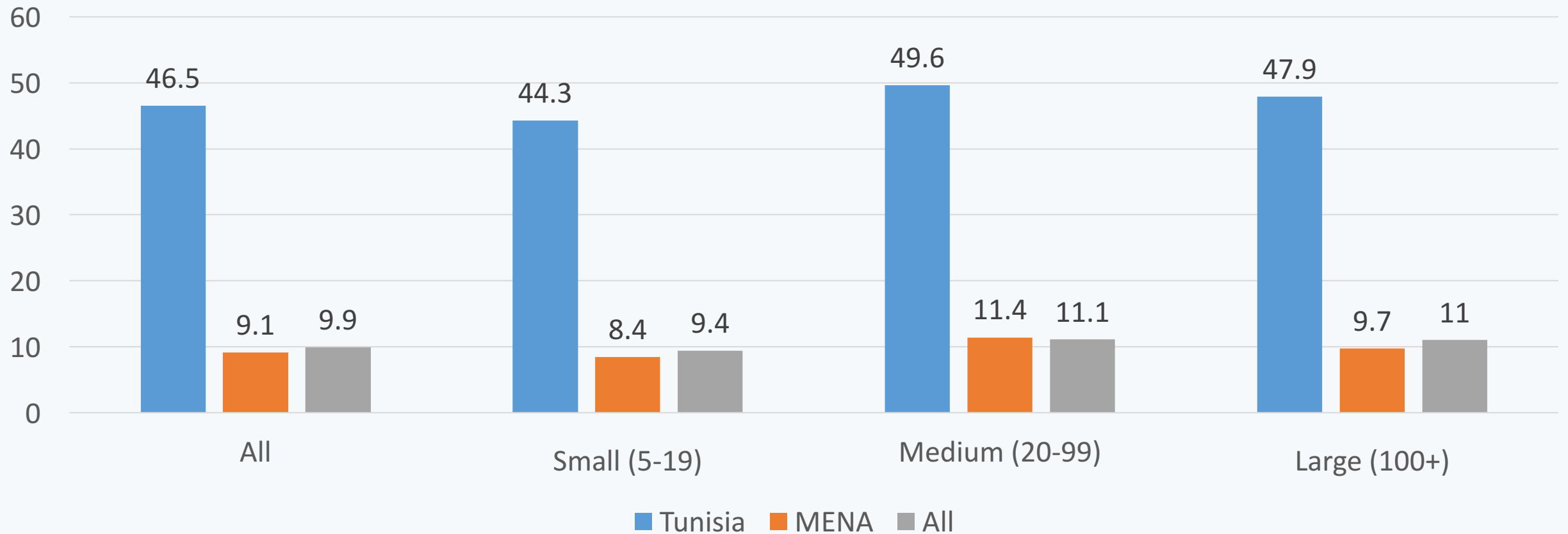
4. Fulfilling the ambitions of the regions
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5. Green economy a driver of sustainable development
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- MCC will keep 2020 plan and other GOT Priorities (reducing unemployment and regional inequalities) in forefront during compact development

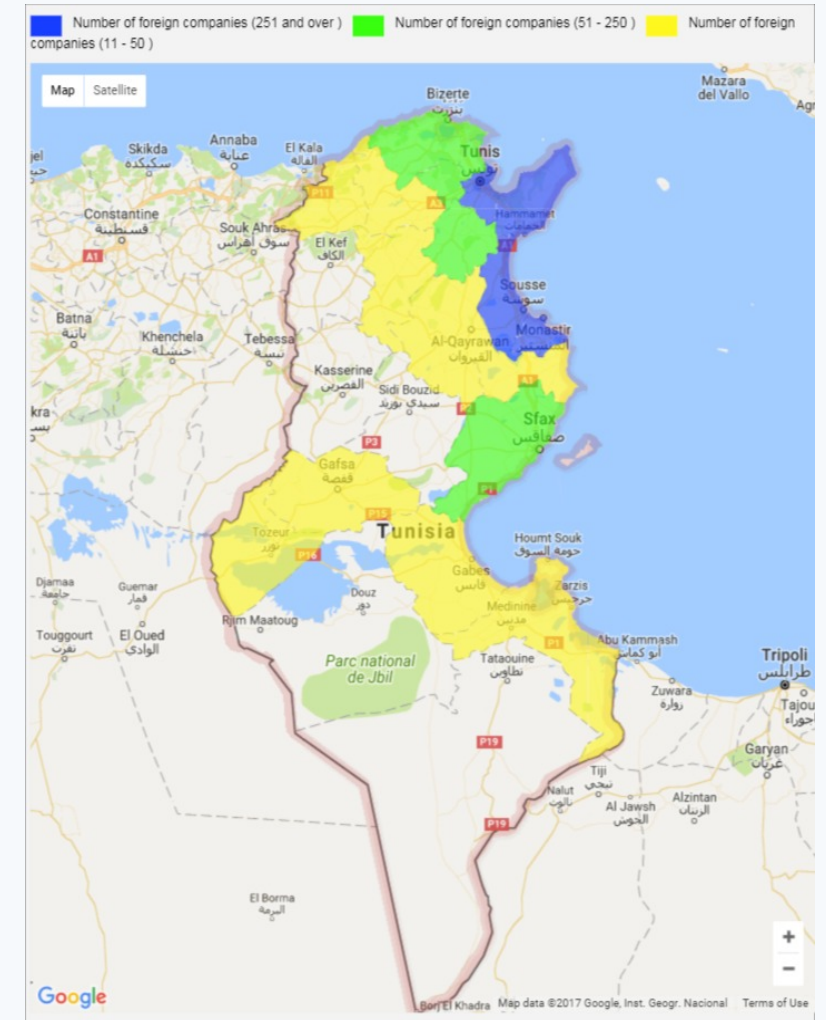
Market Controls: Firms in Tunisia face excessive bureaucratic requirements

% of manager's time spent on dealing with regulatory requirements of government

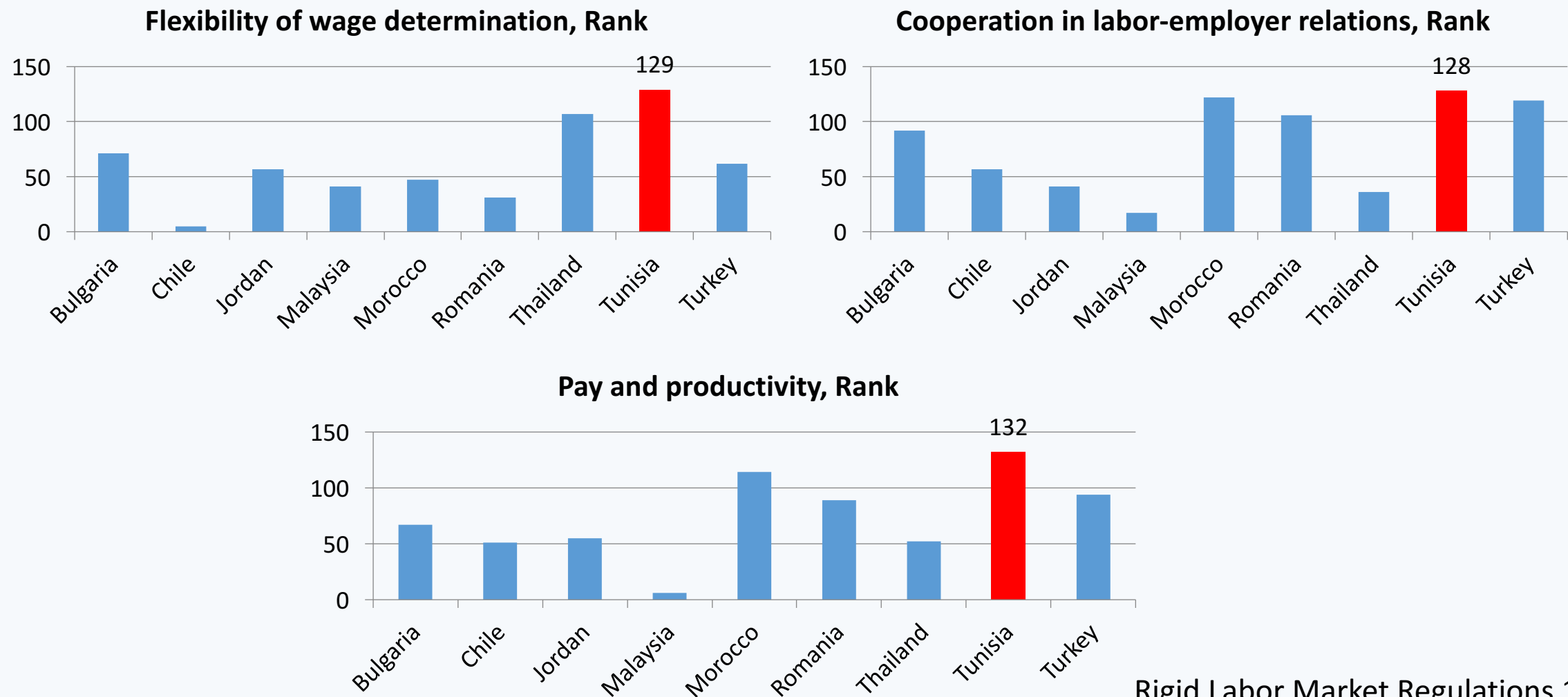


Market Controls: Offshore firms favored coastal areas; little domestic entrepreneurship has emerged

- Offshore firms favor coastal areas for logistical and trade purposes, disadvantages interior areas
- SMEs are least able to manage regulatory burden, hurting local entrepreneurship, and/or increasing informality
- 86% of all Tunisian firms are one person enterprises, making up 25% of employment; in comparison, in Morocco, just 37% of firms are small (less than 10 people overall).

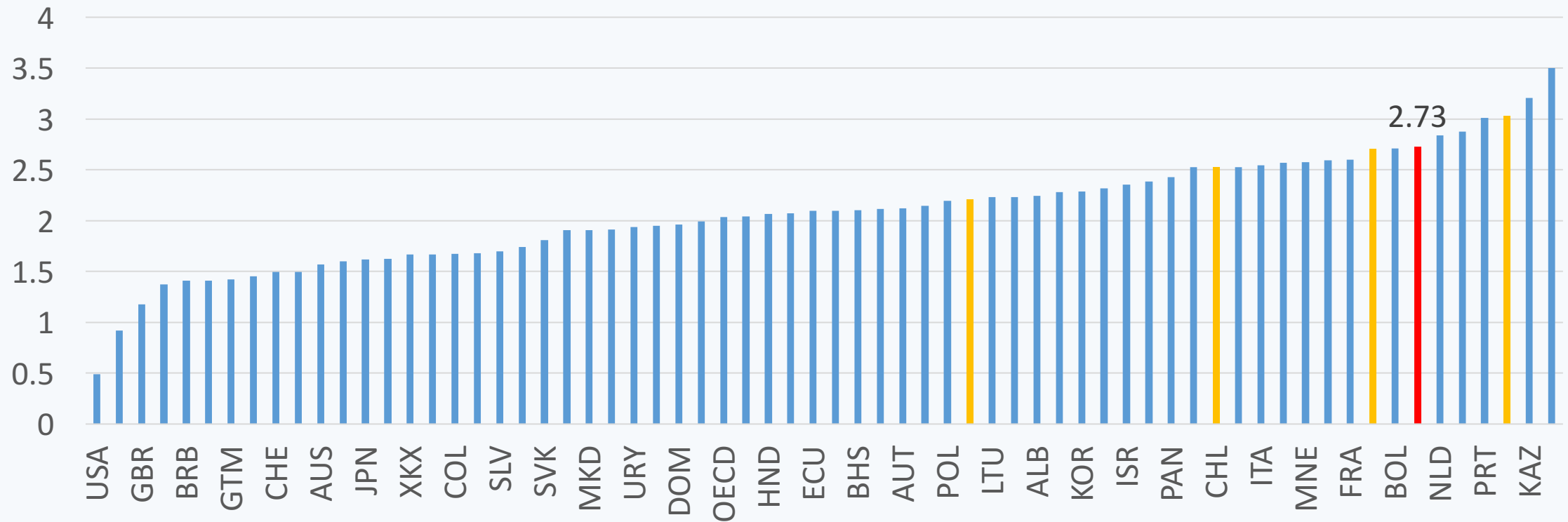


Labor Market Regs: Wage determination is highly inflexible, affects pay-performance relationships



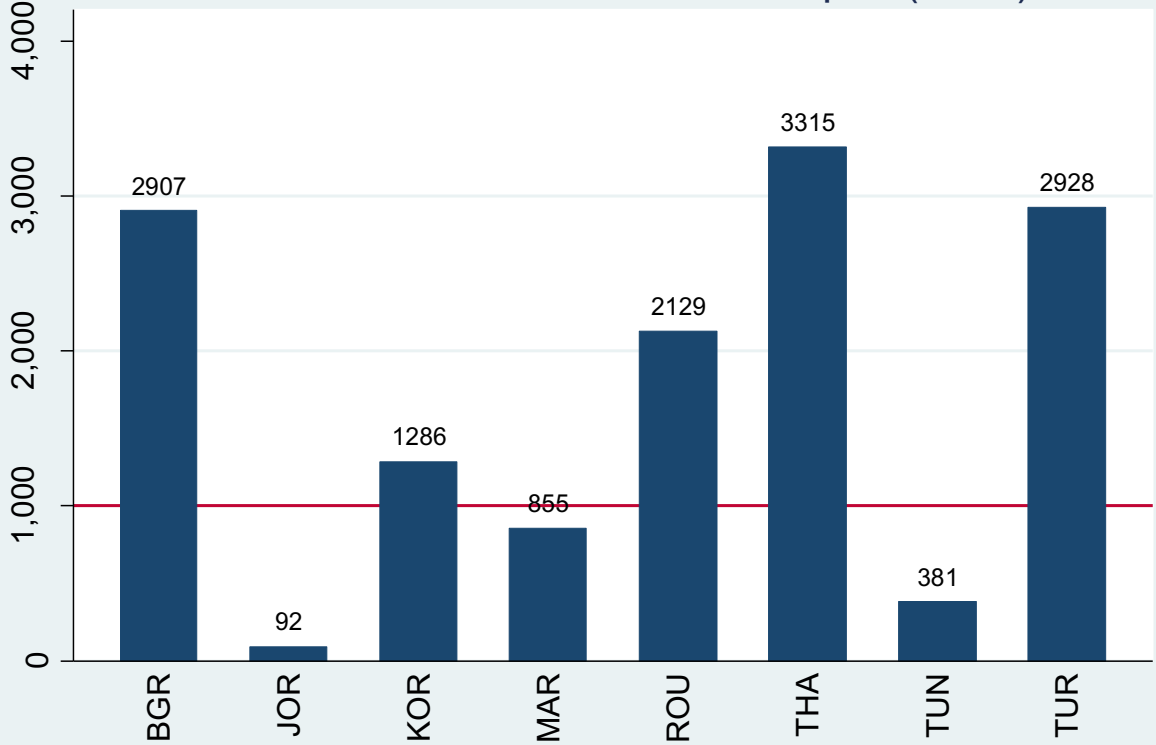
Labor Market Regs: Employee termination is risky and difficult

OECD Index of Strictness of Individual Dismissals, Permanent Workers (2013-2014)

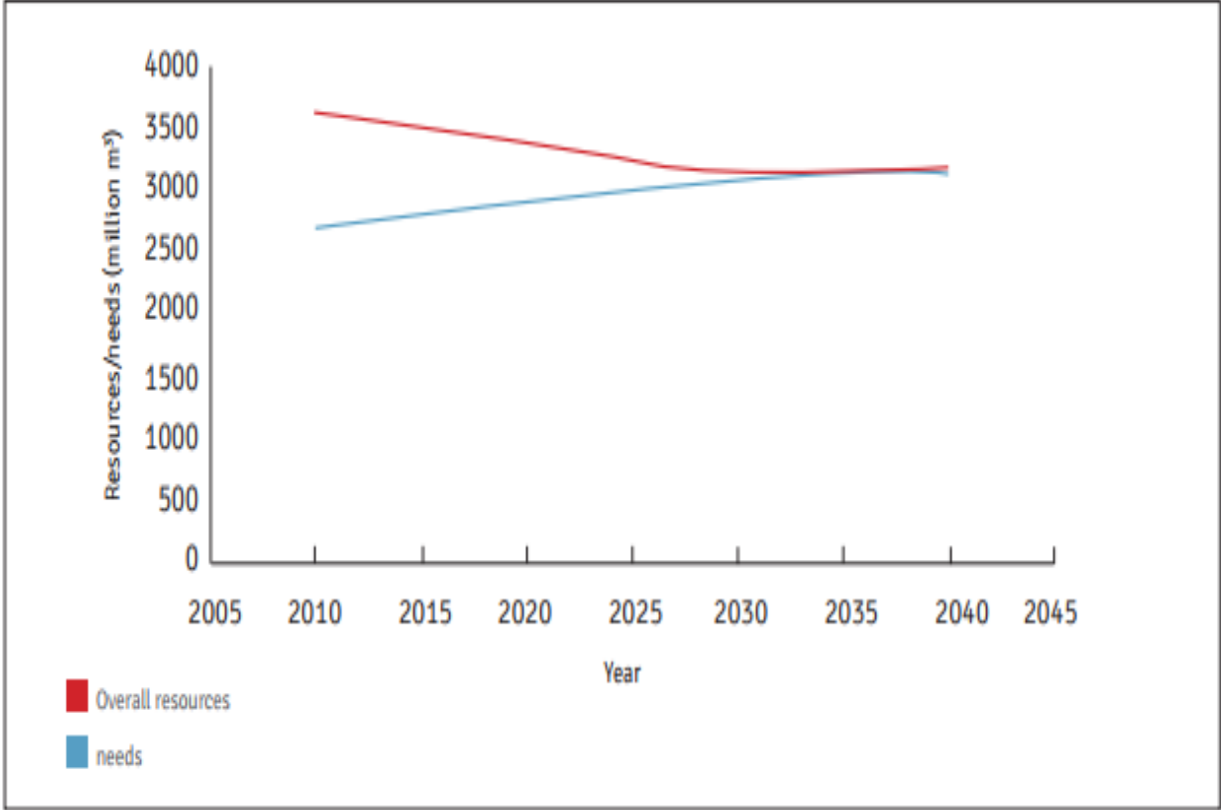


Water Scarcity: Tunisia is water poor; water scarcity is exacerbated by climate change and over exploitation

Internal Water Resource Per Capita (2014)



Source: World Development Indicators



(Source: Ministry of Agriculture and Water Resources, 2007)

Water Scarcity: Due to insufficient water availability, farmers and firms operating in the interior regions are using illegal / unsustainable / costly methods

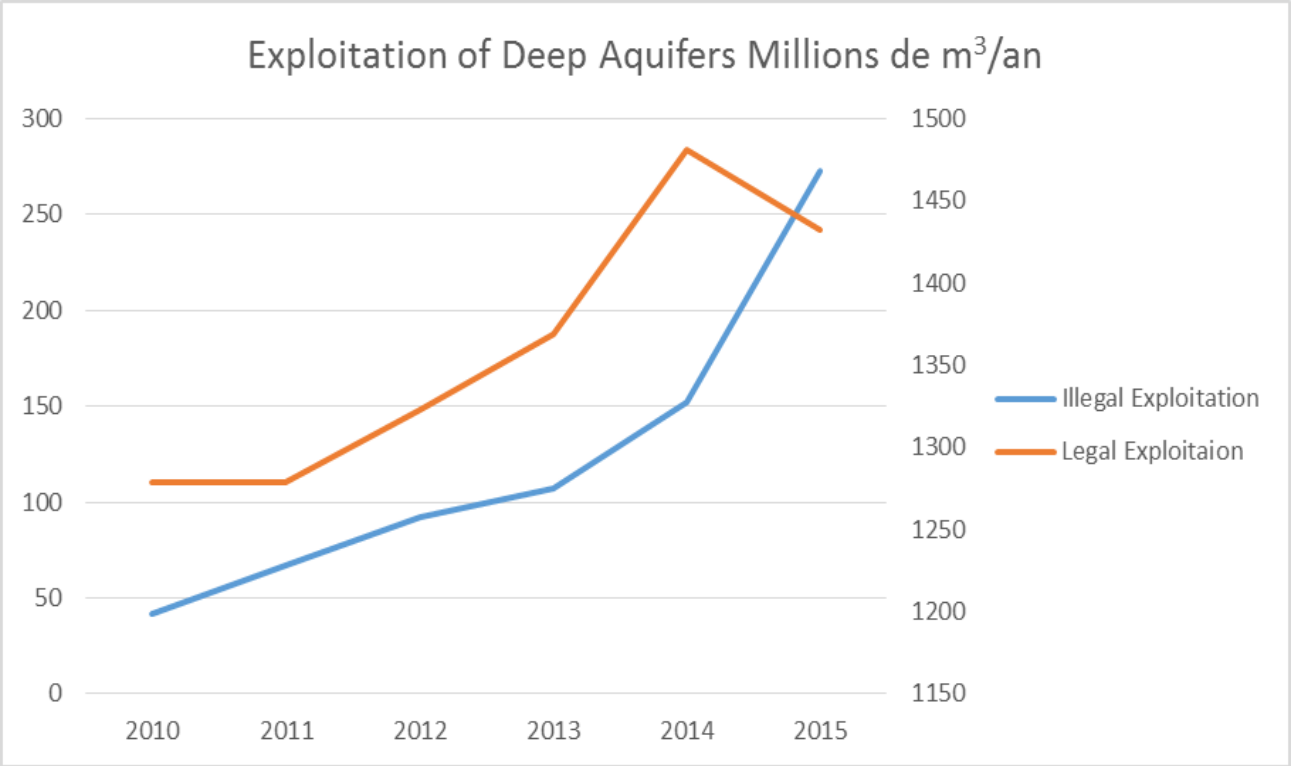
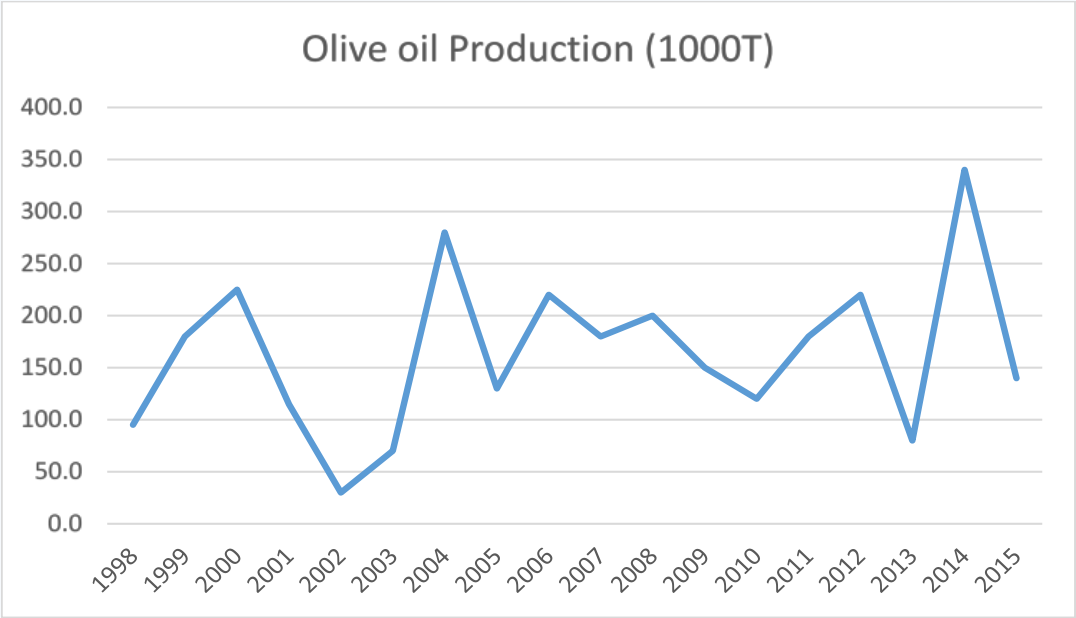


Figure: Variability in olive oil production, 1998-2015/2016



Source: INS