The IMF in Tunisia: Transitional Injustices

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Summary

Tunisia has gone through two phases of transition since its independence from French colonial rule: The first phase was from Bourguiba’s rule (1959-1987) to that of Ben Ali (2011-2011), and the second was the 2010-2011 revolutionary phase, with steps taken towards the implementation of a democratic government. Both transitional phases were accompanied by two IMF agreements: an aid offer with a confirmation agreement (1986/2013), followed by a mechanism for increasing credit (1988 and 2016). In spite of an important discursive change in the IMF’s report following Tunisia’s 2011 Revolution, the conditionalities required by the IMF in a quid-pro-quo exchange for the transfer of the promised loan amounts are in the same vein as those found in the 1986 structural adjustment plan. History has been repeating itself as the IMF and the World Bank continue to coordinate with each other and work in concert to continue the deregulation and liberalization of the Tunisian economy - a task they have been attempting since 1986, in the context of shrinking state power and of successive governments that lack a genuine vision for the country. Liberalizing trade without first building up the country’s productive capacities results in a significant increase in unemployment and further deteriorates the balance of payments and trade balance. It is worth noting that Tunisia’s trade balance is already in a considerable deficit, and further liberalization given the current context will consequently increase the country’s indebtedness.

Recommendations

- To implement a working development strategy; in this instance, an industrial and agricultural strategy for the medium- to long-term that seeks to strengthen local production in order to generate secure and gainful employment, create value added and surplus value.
- To condition all negotiations with the IMF and the World Bank or other IFIs according to this strategy in order to objectively assess and maintain some instruments and leverage for the country's development that are currently being phased out through successive reforms. These include investment regulation based on industrial and agricultural operating strategies, targeted subsidies and incentive policy, exchange rate policy etc.
- To conduct regular audits of public foreign debt and the related conditionalities in order to better negotiate them and evaluate their impact given Tunisia’s exponentially expanding debt.
- To implement a debt negotiation strategy based on the objective assessment of regularly conducted audits.
- To revisit and further review the law granting independence to the Tunisian Central Bank (BCT) promulgated in April 2016 under pressure by the IMF, and to amend the articles which grant independence to the BCT in favor of the executive; and additionally to return to the goals of the BCT according to Law 199-88, which states in Article 33 that: “The general purpose of the central bank is to defend the value of the national currency and to maintain its stability.”

Key Words:
IMF, The World Bank, conditionalities, the General Compensation Fund, liberalization, deregulation
Introduction

In 2012, the Tunisian government solicited the International Monetary Fund (IMF) for financial assistance, which was granted on June 2013, in the form of a confirmation agreement (Stand-By Agreement, or SBA). In 2016, the government requested financial assistance from the IMF for a second time. This was granted on May 2016, with a mechanism for extending credit: the Extended Credit Facility (ECF) following Parliament’s adoption of the Central Bank Independence Law, the Banking Legislation Law, and the Bankruptcy Law in April 2016, all of which were preconditions for the negotiated funding. The Extended Credit Facility amounted to 2.9 billion US dollars, and was given in exchange for an “economic and financial reform program,” namely, a structural adjustment plan. The government has committed itself to implementing the harmful conditionalities in exchange for the ECF. In order to better understand the implications of this financial assistance by the IMF, it is important to put the IMF intervention in Tunisia in its proper context. Coming on the heels of the revolutionary process in January 2011, this intervention was part and parcel of the Deauville Partnership with Arab Countries in Transition. The Deauville Partnership is a trust comprised of the G8 countries, Turkey, and the Gulf countries, as well as international financial institutions. It was established in May 2011 during the G8 summit in Deauville, France, to address the revolutionary processes unfolding in Arab countries at the time. The aim was to coordinate member actions in order to ensure the protection and promotion of shared interests. Through this process, loans (project loans and budgetary support loans) would be offered to “Arab countries in transition” (Tunisia, Morocco, Jordan, Yemen, Egypt) in exchange for implementing a host of neoliberal and institutional reforms in their countries. The rarely spoken-about Deauville Partnership has been a cornerstone of the economic policies adopted in Tunisia during the transition period. It follows the same logic and historical patterns that had already been implemented with the IMF’s last structural adjustment plan in 1986, and it aims to enhance and extend liberalization of the Tunisian economy. Since 2011, the foreign public debt has increased substantially as a result of this partnership, expanding from 40.7% of the GDP in 2010 to 63.7% of the GDP in 2017. Successive governments have increasingly lost their ability to maneuver (e.g. “policy space”) on political and economic decisions because of this spiraling debt. This is a well-worn pattern that dates back to 1986 and the country’s first IMF mandated structural adjustment plan. It was further reinforced in 2011 through the Deauville Partnership’s promotion of a neoliberal agenda. In addition to impacting Tunisian sovereignty through increased indebtedness and reduced policy space, IMF intervention during this sensitive transitional moment also undermines the process of democratization. Due to the legal nature of IMF “agreements”, they are not adopted by the Assembly of the Representatives for the People (ARP) but rather exist as a unilateral commitment of the Executive Branch to the IMF in return for the implementation of extensive institutional restructuring and reforms. In this way the Executive Branch is able to pressure the ARP to precipitously approve economic reforms through bills, under threat of financial blackmail and without proper public debate. This process structurally undermines democratic procedures by entrenching executive power and weakening the legislature, all of which are features of the pre-revolution authoritarian state where the legislature performed the role of a simple rubber stamp. Starting from the IMF documents, including its June 2013 review concerning the “Stand-By Agreement” (based on Article IV), as well as the February 2106 request for an Extended Credit Facility, we will discuss the different policy conditionalities required by the IMF in return for the disbursement of loan installments. We will focus on three key conditionalities: the reform of the “business environment,” exchange rate policy, and food subsidies. We will unveil the extent to which these three conditionalities seek to expand the deregulation and liberalization of the Tunisian economy and how they risk deepening the inequalities and dysfunctionalities of the development model.
Since its independence, Tunisia has passed through two transitional phases: The first was from 1986-1987 with the transition from Bourguiba’s government to that of Ben Ali, and the second is from 2010-2011 with the implementation of a democratic government. In this section we draw a parallel between Tunisia’s two transitions (1986-1987 and 2010-2011) as they are both tied to the two same agreements with the IMF- the request for a Stand-by Agreement, followed by an Extended Credit Facility.

If we take a closer look at the period following the transition from Bourguiba’s to Ben Ali’s rule, we can see that Tunisia requested a Stand-by agreement with the IMF in 1986. This allowed Tunisia access to an installment loan through “withdrawals” from 1986 to 1988 with a repayment of the loan (capital and interest) extended over a period of six years, between 1987 and 1993. In 1988, Tunisia applied for an Extended Fund Facility (EFF) for which the withdrawal and repayment of the installments followed the same process from 1991 to 2001.
The proposed loan would support the completion in all major respects of the liberalization of external trade, prices and the financial sector and would permit market forces to operate effectively.

During this period, the IMF and the World Bank coordinated their efforts in order to ensure implementation of the required changes: “Coordination between the Bank and the IMF has been excellent.”

The main conditionalities for the IMF’s 1986 Stand-By Agreement and then their 1988 Extended Credit Facility Agreement are emblematic of the IMF’s standard structural adjustment program. Namely, the liberalization of external trade, investment, the financial sector, prices, and the withdrawal of the role of the state to make way for the private sector: “The proposed loan would support the completion in all major respects of the liberalization of external trade, prices and the financial sector and would permit market forces to operate effectively.”

The recourse to an Extended Credit Facility (ECF) in the aftermath of a Stand-By Agreement is a truly alarming sign, as it leads to far-reaching, medium-to-long term reforms and a monitoring of the IMF’s recommendations at junctures of 4 and 10 years. Although there has been a shift in the narrative discourse as evidenced in the IMF’s afore-mentioned reports on Tunisia, including reference to concepts such as “inclusive growth”, “tax equity”, “transparency and anti-corruption”, and “reduction of social and regional disparities”, we can, nevertheless, observe continuity and enhancement of the IMF’s policy recommendations from 1986 until today.

**A critical analysis of the main IMF recommendations**

**The replacement of food subsidies with a targeting system (targeting plans and social safety nets)**

A central element of the IMF’s policy recommendations is the call for the government replace food subsidies provided through the instrument of the General Compensation Fund with a targeting system for the most vulnerable in order to lessen the burden of national expenditures, claiming that “controlling the public sector wage bill would create the fiscal space for more public investment.” According to the February 2016 ECF request (Request for an EFF), the government has committed itself to setting up a database of vulnerable households and to develop a unique identifier: “In addition to existing cash transfer schemes, whose coverage and importance increased over the past two years, a better-targeted social safety net would be introduced in June 2017, with the introduction of a unique social identification number and a new database on vulnerable households (end-March 2017 SB).”

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*Request for an EFF, p 17
It is important to note that this reform was also requested by both the IMF and the World Bank during their coordinated intervention in the 1988-1986 transitional period, adopting the same argument they use today: “The present system of consumer subsidies is an inefficient way of helping the poor in that it subsidizes prices and, hence, benefits the better-off to the extent that they consume more of the same products than the poor. The items subsidized consist of basic articles of consumption such as certain heat products, milk, sugar, and vegetable oil, and some agricultural inputs such as fertilizers and animal food. Since these items are widely consumed, their subsidies have high budgetary costs and are politically sensitive.” Under pressure from these two institutions, the Bourguiba government decided to increase the price of bread and flour by 100% at the end of 1983, which led to the Bread Riots in January 1984. The 1984 Bread Riots were a popular uprising that started in the south and then progressed to the north and were primarily made up of young and impoverished people from the countryside, seasonal workers, or the unemployed. In light of the sociopolitical impact of these reforms, their unpopularity as well as continued pressure from the Bretton Woods institutions, the governments from this time period chose a gradual increase in some products of less social importance than the cereal derivatives—such as beef. What the IMF and World Bank reports during the 1988-1986 transitional period and during the ongoing transition leave out is that since 1970 the compensation policy has not only sought to help protect the purchasing power of low-income segments of the population against fluctuations in food and oil prices, but also to provide support to Tunisian farmers. Indeed, the Tunisian agricultural policy includes subsidies for grain prices, as well guarantees that the state will purchase local production and support farm income. The General Compensation Fund is therefore also a policy for production and employment support, and entailing price regulation of both production and consumption in the agriculture sector and other sectors of the economy. In that respect, this compensation policy does not only target the poorest section of society by enabling the consumption of basic products, and the middle class, through supporting its purchasing power, but it also responds to the country’s development objectives by supporting farmers and local production. From 1994 to 2014, over the course of the neo-liberal economic reforms, the agriculture and the fishery sector went from the first sector in terms of employment to the sixth in a span of just 20 years.
Indeed, the reduction of government subsidies for farming inputs\textsuperscript{11} and the elimination of subsidies that seek to ensure producer prices and farmers’ income, can further jeopardize farmers and their jobs and increase the deficit balance for agriculture and food. However, the IMF’s various reports make unique reference to the “poor” and “non-poor” classes without defining which social groups are actually represented by these categories obscuring the existence of the middle class by presenting only the poor classes and the wealthy classes. According to a joint study carried out in 2012 by the African Development Bank (AfDB) and the National Institute of Statistics (NIS),\textsuperscript{12} 9.2% of subsidies go to the poorest households, 60.5% to middle-class households, 7.5% to the well-off population, and 22.8% are transferred out of household use (catering sector, coffee shops, tourists, illegal border trading). In this joint study, a clear definition in terms of revenues of what is defined as “the poorest households”, “middle class” or “wealthy population” would have been useful in order to better understand who truly benefits from subsidies and the IMF report is unclear on whether the middle class is included under the category of “non-poor” or “poor”. The joint study concludes that 60.5% of subsidies benefit the middle class, which means that the elimination of government subsidies may face a reduction in their purchasing power and impoverishment. Finally, the IMF’s recommendations to establish a targeting system for the most disadvantaged through direct transfers in a way that effectively targets only those most needy to the exclusion of others would be difficult to achieve in the Tunisian context, where informal labor is a significant factor. As explained in the precited joined study: “When it comes to direct transfers, the ideal system requires a clear view of each household’s income and of each head-of-household’s earning ability. However, such information is poorly shared and lacks reliability in a country where informal labor plays an important role in the economy.”\textsuperscript{13} Though the General Compensation Fund has significant management issues that need to be audited in order to optimize its management without affecting the most vulnerable groups and farmers, the IMF recommendations are incapable of adequately addressing them. The IMF and the World Bank’s solution to remove subsidies (including price support for farmers, fertilizer subsidies, sector targeted incentives, etc.) and to abolish regulation-eliminates two of the principal tools of development available for developing countries. This is a similar pattern that we also notice to that of the new Code for Investment Reform.

“Business Environment” Reform

The IMF has been working in conjunction with other international financial institutions such as the World Bank and the African Development Bank since 2012 to firmly urge the government to reform the “business environment” meaning specifically, adopting a legal framework for public-private partnerships and reforming the Code for the Public Procurements and the 1993 Code for Investments Incentives. The high degree of emphasis placed by the IMF on the need to reform the “business environment” can be seen in the 6th review of the IMF’s Stand-By Agreement in June 2013 as well as the request for an Extended Credit Facility in February 2016 (request for an extended arrangement under the Extended Fund Facility), in which it calls for an: “Effort to streamline existing business procedures and enhance market access through a new investment code and the implementation of the competition law and the law on PPP are essential to promote private sector developments and create jobs”\textsuperscript{14}.
Through the conditionality of the 1988 EFF and the 1991 “Economic and Financial Reforms Support Loan”, the IMF and the World Bank took advantage of the 1986/87 transitional crisis to implement a unified single investment code and to abolish several approvals and regulatory measures previously governing the private sector: “The existing investment codes, which target sector-based activities, have to be replaced by a single code.”15 The World Bank conditioned the disbursements on its adoption: “The loan became effective, with release of the first tranche of US$100 million equivalent, on December 23, 1991 (…) The third tranche was released a year after the release of the second. It could have been released earlier but the promulgation of the Investment Code implementing legislation took longer than anticipated.”16 Despite the fact that the IMF and the World Bank were largely responsible for promulgation of the 1993 Investment Incentives Code reform- they denounce that Code today without acknowledging their responsibility for its failure. Together, these two institutions have manipulated and falsified data in order to support their neoliberal agenda.17 Since 2011, the IMF and the World Bank have encouraged the Tunisian government to reform its Investment Incentives Code to “improve the business climate”. This includes calls to establish a legal framework on Public-Private Partnerships (PPPs) in order to enhance market access (in the form of deregulation) as well as to strengthen the protection of investors’ rights (e.g. the role of international arbitration, free repatriation of capital, the less favorable treatment clause and the fair and equitable treatment clause, access to farmland ownership to foreign investors).19 « Improving the business climate » Key measures include improving the adoption of a new investment code, the streamlining of tax incentives and the simplification of procedures to reduce entry barriers and protect investor rights. The simplification of about 530 tax, customs, and business formalities completed over the past two years are expected to reduce administrative burden faced by businesses and increase government efficiency.”20 The New Investment Code is guided by the “Regulatory Guillotine Strategy,” which falls within the framework of the Business Environment and Entrepreneurship Development Policy Loan program financed by the World Bank (the International Bank for Reconstruction and Development- the IBRD- and International Finance Corporation- the IFC). In other words, it is a deregulation strategy that aims to rapidly eradicate and simplify up to 50 per cent of the regulations and texts for regulations in all economic sectors in a very short amount of time. This deregulation operation was already launched before the Revolution as a result of the World Bank’s interventions. This Guillotine Strategy emerged from the “Regulatory Capture Theory,” or “Capture Theory,” a theory first propounded by Samuel P. Huntington (1953) and Marver H. Bernstein (1955). It was later formalized and developed by Georges Stigler, an American economist close to Milton Friedman (1971) and Peltzman (1976). In short, this theory analyzes regulation as the product of relations between corporations, the legislature, and/or the regulatory authority, and hence shaped by the influence of pressure/lobby groups serving private interests. This approach is known as the regulatory capture theory, because the legislator/regulatory authority becomes an agent entirely in the service of business interests. In order to limit the action of pressure groups for private interests at the expense of the general interest, the proponents of this theory- in this case Stigler- advocate a radical solution: to remove the state’s regulation power. According to this theory, when regulations are subject to pressure/lobby groups or private interest groups, they no longer work to ensure the general interest and therefore must be abolished. Based on the IMF and the World Bank’s recommendations, regulatory capture theory seeks to justify the withdrawal of regulatory measures as a means to limit the influence of private interest.
Yet, the converse conclusion can also be reached: that by regulating or even banning these pressure/lobby groups’ activities private interests can be kept out of policy-making for the benefit of the public good. Required by the World Bank and IMF, this reform of the investment leads to the simplification and the dismantling of non-tariff barriers (e.g. approvals and incentives of the Investment Incentives Code, the regulatory measures of the public procurement code, or even the law on PPPs.25) in order to make it easier for foreign companies to operate and have access to the Tunisian market without boundaries. It is clear that the main utility of deregulation is to serve the interests of foreign companies and private-interest groups at the expense of the local companies and producers who may not be able to cope with foreign competition. Yet attempts to liberalize the economy and amplify market access for foreign companies through deregulation, without first enhancing and improving the country’s production capacity, will likely further deteriorate the balance of payments and the balance of trade, which is already largely in the red. This will consequently lead to further recourse to foreign loans and therefore increased debt.

**Exchange rate policy**

Tunisia’s exchange rate policy is set by the Central Bank of Tunisia (CBT). The CBT has traditionally aimed at stabilizing the value of the dinar in support of the economic interests of the country. In fact, Article 33 of Law 88-119 stipulates that “the Central Bank’s overall task is to defend the value of the currency and to safeguard its stability.” In the context of Tunisia’s increased economic and financial integration within the global economy, the CBT chose to select a controlled exchange rate regime that seeks to adjust the value of the dinar against a handful of currencies - mainly the euro, due to the significance of foreign trade with the EU, but also the dollar because of the country’s foreign debt. Accordingly, this controlled exchange rate regime gives enormous power to the CBT, as it is responsible for stabilizing, whenever possible, the value of the dinar while adjusting it to promote the competitiveness of Tunisian export-oriented companies. Despite its relative success in maintaining the stability of the dinar, the IMF and the World Bank have consistently sought to liberalize exchange rate policies and to transfer the management of exchange rate policies from the public sector (through the CBT’s management) to the private sector (through management by commercial banks and “market power”). The intentional weakening of the CBT has come at the same time as the IMF and World Bank’s structural adjustment policy measures have resulted in the destabilization of the dinar’s value, making it impossible for the Bank to intervene in a helpful way.26 The Impossible Trinity principle or Mundell–Fleming model is vital to grasping the aims of the IFIs in regards to the governance of Tunisia’s central bank and monetary policy.27 This principle holds that it is impossible to simultaneously maintain all three of the following objectives: A fixed foreign exchange rate, an independent monetary policy, and a perfectly free movement of capital. So far the CBT has attempted to keep a degree of freedom in its monetary policy through maintain a balance between a controlled exchange rate regime and an asymmetrically and partially liberalized capital account. However, the IMF and the World Bank pushed the CBT to fully liberalize capital flows - and more specifically short-term capital outflows- through the new investment code approved in September 2016. In the context of a total liberalization of capital flow, the CBT is forced to give up to “market power” its control over the dinar exchange rate regime. This was confirmed by the CBT which, in a recent study,28 pointed out that “the CBT’s control of exchange rates was made easier by the limitations to capital transactions and more specifically by short-term capital.”

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29 Request for EFF, note 1, P15.
The inevitable short term entry and exit of large quantities of capital that will be enabled by this liberalization, could render the dinar vulnerable to attack by malevolent speculators. This is precisely what happened with the Asian crisis of the late 1990’s. Furthermore, starting from the vote for the law on CBT’s independence in April 2016, the rates of exchange between the Tunisian dinar and the dollar have plummeted.

The result of the dinar’s devaluation is an increase in the price of imports when the main exports (phosphates and tourism) are in crisis and cannot offset these new costs. The IMF, throughout its Stand-By Agreement reviews, has time and again called for the depreciation of the Tunisian dinar. However, the IMF is well aware of the consequences of the dinar’s depreciation on public debt: “For the public sector, a large exchange rate depreciation would raise public debt ratios and increase external debt service.”

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**Exchange rates evolution since early 2016**

Source: General Population and Housing research - 2014
Conclusion

There is a significant contradiction between reality and rhetoric in the IMF policy conditionalities. Though they claim to foster employment and Tunisian socio-economic resilience, in fact, these conditionalities increase the dysfunctional nature of Tunisia’s development model. The IMF issued an audit in October 2014 which turned out to be very critical on IMF’s policy advice, including the excessive austerity measures mandated during the 2008-2009 crisis. The austerity and liberalization measures required under the Extended Fund Facility represent a source of high social and political tensions, and the government is biding its time in carrying out socially costly reforms. Evidence of government foot-dragging can be found in the IMF’s decision to block the disbursement of the second installment, scheduled for December 2016. It also delayed the first economic review of the Extended Fund Facility (EFF) in order to apply pressure on the Tunisian authorities due to the slow progress of “reforms”. A review mission launched on April 7, 2017 to assess progress and make recommendations regarding the release of the expected second and third installments of the EFF, is still underway. The reforms identified as priorities in the EFF review include the highly unpopular demands to restructure public/state-owned banks and reduce the public wage bill. The severe pressure to which the current government has been subjected to by the IMF is reflected in the statements made by the Ministry of Finance Lamia Zribi, as well as the contradictory and vacillating statements on banking sector reforms made by the head of government, Youssef Chahed. The reform packages to which the Executive Branch is committed must be debated and adopted by the Parliament before engaging with the IMF and forwarding the Letter of Intent. Furthermore, it is incumbent upon the current government to implement a genuine development strategy through organizing a medium-to-long term industrial and agricultural strategy that works on strengthening local production in order to generate employment and provide added and competitiveness. This strategy must form the basis for all the reform negotiations with the IMF and the World Bank in order to maintain the instruments and levers of the development policies which are dismantled little by little through the reforms (maintain investment strategy oriented towards regulation of industry and agriculture, incentives and targeted subsidies policy, exchange rate policy etc.). Furthermore, in view of Tunisia’s spiraling debt and thus the loss of its policy space when it comes to economic policy-making, the government must establish a regular audit of the country’s external public debt in order to better negotiate conditionalities and evaluate their impact.

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Bibliography