PD-ABF-484

DATE: 3/9/93

ISN 81377

TO: CDIE

FROM: NE/DR/EPS

SUBJECT: PROJECT PAPER Tunisia 664-0346

The attached document, for your files, contains cost estimates and other procurement related information which may be procurement sensitive (PSI)

All employees receiving copies of the document are therefore reminded of their obligation, under both law and policy, NOT to discuss or make such data available to other than authorized Agency personnel

Procurement sensitive information (PSI) should not be released outside of the A I.D until expiration of the PACD ____________ or 9/30/97 whichever comes first.

DATE RECEIVED ______________
RECEIVED BY· ______________

A

PD-ABF-484
ISN 81311

UNCLASSIFIED

<u>AGENCY FOR INTERNATIONAL DEVELOPMENT</u>
WASHINGTON, DC 20523

PRIVATE ENTERPRISE PROMOTION

TUNISIA

664-0346

PROJECT PAPER

DATED SIGNED <u>09/01/92</u>

UNCLASSIFIED

RESTRICTED

B

ACTION MEMORANDUM FOR THE MISSION DIRECTOR

From Richard Rousseau, PSO

Subj Authorization and approval of the Private Enterprise Promotion Project (664-0346)

Ref: State 239552, dated 22 July 1991

PROBLEM:

Your approval is requested to authorize the Private Enterprise Promotion (PEP) Project for Tunisia at the life-of-project level of $10.0 million on a grant basis from ESF funds and to proceed with the initial obligation of $1.5 million as project funding for FY 1992

DISCUSSION:

The purpose of the PEP Project is to expand private sector employment and income by privatizing state-owned enterprises and decentralizing government functions, and improving the efficiency of financial markets The project is entirely consistent with the recently approved Government of Tunisia Eighth 5-year Plan which places maximum emphasis on mobilizing private sector resources for national development The Project is also entirely consistent with the approved Mission strategy as set forth in the AMP approved in June 1990

The Project supports the GOT efforts to launch a new phase in its privatization program that depends on the ongoing development of financial markets In turn, the process of privatization (essentially refinancings of existing enterprises) will in itself serve as a means for the growth of modern financial institutions and practices The components are: (a) Privatization/Decentralization; and (b) Financial Markets Development.

The Project will support the sale of state-owned enterprises (SOEs) to the private sector, and on a limited scale, greater decentralization of government services from the central government to the municipalities and further devolution from the latter to the private sector The Decentralization activities to be carried out in connection with the Housing Investment Guaranty Program.

Privatization activities involve four key activities. studies and diagnostics, transactions, including valuations, marketing strategies, schedules, and prospecti; an Information, Education, and Communication Campaign, and finally, a comprehensive evaluation effort.

The Decentralization Activity supports the decentralization of authority for the planning, construction and operation of public services from the central government to the municipalities, as well as the private provision of such services.

The objective of the Financial Markets Development Component is to increase the availability of capital to the private sector, especially for the privatization of state-owned enterprises and the expansion of exports. The Project will work towards increasing market forces, reducing the level of government intervention in financial markets, and strengthening private intermediaries.

The Project's activities will be implemented under the guidance of three separate but interlocking committees. The Privatization Committee will comprise only representatives of the GOT, the Institutional Contractor, and USAID while the Financial Markets Committee will draw at least 50% of its members from the private sector. The Decentralization Committee will also have private membership Most Project assistance will be delivered through a single U.S. Institutional Contractor who will provide U.S. as well as local expertise, the latter through subcontracts with local accounting and financial firms.

Project beneficiaries will fall into two major categories. First, the economy of Tunisia will be strengthened by privatization activities as well as the development of financial markets. The stronger economy will generate increased employment opportunities Second, individuals who invest in the privatization transactions, especially through more extensive financial markets, will be able to realize benefits accruing to their investments This feature should not be overlooked, as there are numerous individuals with small amounts of savings which they have shown a willingness to invest in stock offerings in Tunisia

The total cost of the Project is estimated at $15.9 million. Of this total, $10 0 million will be financed by A I.D. The balance will include a contribution of the GOT of approximately $4.5 million and a contribution from the private sector of $1 4 million. The total Tunisian contribution will be no less than 25% of the resources of the Project

The Mission Review Committee met on July 24, 1992 and found that the Project was acceptable in terms of technical and socio-economic soundness. Particular issues addressed were the need to define performance indicators more carefully, requirements that privatization transactions include an assessment of potential environmental liabilities, and better definition of the process of diagnosis of potential state-owned enterprises selected for privatization. It was also felt that the decentralization component needed to be blended into the narrative more carefully

Regarding special concerns, it was noted that the contracting arrangements made satisfactory provisions for inclusion of minority contractors and/or sub-contractors The question of gender was more difficult, as the principal Project activities constitute privatization transactions and expansion of financial markets Access to either activity is based on financial resources which are owned by the private sector and are not under the influence of A I D. in terms of gender considerations

The Project was included in the Congressional Presentation for FY 1992 (p. 653). That inclusion constitutes due notification to Congress

RECOMMENDATION:

That you sign the attached Project Authorization and thereby approve life-of-project funding of $10 0 million

Attachments:
1. Project Authorization
2. Project Paper

Clearances:

PRM: HPKolar	(draft)
EXO: GDietz	(draft)
CTR: GDietz	(draft)
RLO. BBarrington	(draft)

AGENCY FOR INTERNATIONAL DEVELOPMENT

PROJECT DATA SHEET

1 TRANSACTION CODE: A (A = Add, C = Change, D = Delete)

Amendment Number:

DOCUMENT CODE: 3

2. COUNTRY/ENTITY: TUNISIA

3. PROJECT NUMBER: 664-0436

4. BUREAU/OFFICE: NEAR EAST BUREAU

5. PROJECT TITLE (maximum 40 characters): PRIVATE ENTERPRISE PROMOTION

6. PROJECT ASSISTANCE COMPLETION DATE (PACD): MM DD YY 09 30 97

7. ESTIMATED DATE OF OBLIGATION (Under 'B' below, enter 1, 2, 3, or 4)

A. Initial FY 92 B. Quarter 4 C. Final FY 97

8. COSTS ($000 OR EQUIVALENT $1 =)

A. FUNDING SOURCE	FIRST FY B. FX	C. L/C	D. Total	LIFE OF PROJECT E. FX	F. L/C	G. Total
AID Appropriated Total						
(Grant)	(1,500)	(-0-)	(1,500)	(10,000)	( )	(10,000
(Loan)	(1,500)	(-0-)	(1,500)	(10,000)	( )	(10,000
Other U.S. 1						
Other U.S. 2.						
Host Country (GOT & Private Sector)					5,900	5,900
Other Donor(s)						
TOTALS	1,500	-0-	1,500	10,000	5,900	15,900

9. SCHEDULE OF AID FUNDING ($000)

A. APPROPRIATION	B. PRIMARY PURPOSE CODE	C. PRIMARY TECH. CODE 1. Grant	C. 2. Loan	D. OBLIGATIONS TO DATE 1. Grant	D. 2. Loan	E. AMOUNT APPROVED THIS ACTION 1. Grant	E. 2. Loan	F. LIFE OF PROJECT 1. Grant	F. 2. Loan
(1) ESF	730	840		-0-	-0-	10,000	-0-	10,000	-0-
(2)									
(3)									
(4)									
TOTALS				-0-	-0-	10,000	-0-	10,000	-0-

10. SECONDARY TECHNICAL CODES (maximum 6 codes of 3 positions each): 830 | 810

11. SECONDARY PURPOSE CO[DE]

12. SPECIAL CONCERNS CODES (maximum 7 codes of 4 positions each)

A. Code							
B. Amount							

13. PROJECT PURPOSE (maximum 480 characters)

To expand private sector employment and income by privatizing state-owned enterprises, decentralizing government functions and improving the efficiency of financial markets

14. SCHEDULED EVALUATIONS

Interim MM YY 06 95 | MM YY | Final MM YY 06 97

15. SOURCE/ORIGIN OF GOODS AND SERVICES

☐ 000 ☐ 941 ☐ Local ☐ Other (Specify)

16. AMENDMENTS/NATURE OF CHANGE PROPOSED (This is page 1 of a ____ page PP Amendment.)

17. APPROVED BY

Signature: James A. Graham

Title: Director USAID/Tunisia

Date Signed: MM DD YY 09 01 92

18. DATE DOCUMENT RECEIVE[D] IN AID/W, OR FOR AID/W DOC[U]MENTS, DATE OF DISTRIBUT[ION]: MM DD YY

AID 1330-4 (8 79)

PRIVATE ENTERPRISE PROMOTION (PEP) PROJECT PAPER

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ACRONYMS/ABBREVIATIONS

A.I D.	US Agency for International Development, Washington, D.C.
AMP	Assistance Management Plan
BCT	Banque Centrale de Tunisie
BDE	Bons d'Equipement
Bourse	Bourse de Valeurs Mobilières, the Tunis Stock Exchange
CAREPP	Committee for Restructuring of Public Enterprises
COECT	Conseil de l'Ordre des Experts Comptables de Tunisie
COTUNACE	Compagnie Tunisienne pour l'Assurance du Commerce Extérieur
CSC	Conseil Supérieur de Comptabilite
CTAREPP	Technical Committee for Restructuring Public Enterprises (work group for CAREPP)
EFRL	Economic and Financial Reform Loan (World Bank)
EC	European Community
ESF	Economic Support Funds
ESOP	Employee Stock Ownership Plan
FCIA	Foreign Credit Insurance Association
FDI	Foreign Direct Investment
GOT	Government of Tunisia
IQC	Indefinite Quantity Contract
IPO	Initial Public Offering
MNE	Ministry of National Economy
MTPS	Management Training for the Private Sector
PE	Public Enterprise
PRE	Private Enterprise Bureau, AID/Washington
PSO	Private Sector Office(r)
PID	Project Identification Document
RHUDO/NENA	Regional Housing & Urban Development Office for the Near East and North Africa (based in Tunis)
SICAF	Sociéte d'Investissement a Capital Fixe
SICAV	Société d'Investissement à Capital Variable
STB	Societe Tunisienne de Banque
SOE	State-owned Enterprise
USAID	United States Agency for International Development/Mission to Tunisia

PROJECT DESIGN AND REVIEW MEMBERS

USAID Project Committee:

Richard Rousseau	Project Officer, Chairman
Aylette Villemain	Private Sector Office
Rachid Nafti	Private Sector Office
Robert Rucker	Program Economist
Lane Smith	RHUDO/NENA

Resource People:

Andres Acedo del Olmo	Procurement Specialist
Fatma Douiri	Controllers Office

Senior Review Committee:

James A. Graham	Director
Peter Kolar	Program Officer
Belinda Barrington	Regional Legal Advisor
Richard Rousseau	Private Sector Officer
Barry Hill	Agribusiness Officer
Gilbert Dietz	Executive Officer/ Acting Controller
David Painter	RHUDO/NENA Director

Consultant Design Team -- Coopers & Lybrand

James Emery	Team Leader
Edward Dey	Banking & Finance
Jean-Pierre Schwartz	Privatization

PROJECT PAPER
TUNISIA 664-0346
PRIVATE ENTERPRISE PROMOTION (PEP)

PROJECT SUMMARY AND RECOMMENDATIONS

A. Grantee: The Government of the Republic of Tunisia (GOT)

B. Implementing Agencies: The Prime Ministry, Ministry of Finance, and the Central Bank.

C. Amount: The Project is authorized for $ 10,000,000 of ESF grant funds, of which $1,500,000 will be obligated in FY 1992 The remainder of Project funding will be obligated in FYs 93-97

D. Total Project Costs: The total cost is estimated to be $15,900,000 including a GOT contribution of $4,500,000 and private sector contributions of $1,400,000 over the life of project.

E. Project Goal and Purpose· The Project Purpose is to expand private sector employment and income by privatizing state-owned enterprises and decentralizing government functions, and improving the efficiency of financial markets. This will contribute to the broader Goal to support the continued emergence of a market-driven, competitive economy.

F. Summary Project Description:

The Project supports the GOT efforts to launch a new phase in its privatization program that depends on the ongoing development of financial markets. In turn, the process of privatization (in one sense, refinancing of existing enterprises) will in itself serve as a means for the growth of modern financial institutions and practices. The components are: (a) Privatization/ Decentralization; and (b) Financial Markets Development.

1. Privatization/Decentralization

The Project will support the sale of state-owned enterprises to the private sector; and on a limited scale, greater decentralization of government services from the central government to the municipalities and further devolution from the latter to the private sector. Decentralization activities will be carried out in connection with the Housing Investment Guaranty Program.

(a) <u>Privatization of State-Owned Enterprises</u>

Privatization activities involve four key activities: studies and diagnostics; transactions, including valuations, marketing strategies, schedules, and prospecti; an Information, Education, and Communication Campaign; and finally, a comprehensive evaluation effort.

(i) Study and Analysis

The Project will support the Government in its efforts to improve the process of analyzing and selecting candidates for privatization. The key element in this process is the performance of brief, business-minded analyses of selected public enterprises to assess their overall prospects for privatization. Based on the information provided, the GOT and USAID will select between 20-25 firms to move on to privatization. The Project will also fund more general studies needed prior to refining the Government's overall privatization strategy or to further developing particular methods of transfer to private ownership An example is that of Employee Stock Ownership Plans (ESOP's) where additional analysis may be needed prior to implementation.

(ii) Transactions

Once privatization candidates have been identified and agreed to by the Privatization Committee, detailed privatization plans will be developed for each enterprise. These plans will generally include valuations, marketing plans, and schedules. Prospecti and/or bidding documents will follow after adoption of the action plan. Work will be conducted by joint teams of expatriate and Tunisian financial and industry experts fielded through a U.S. institutional contractor contracted by AID. Such joint efforts will encourage the transfer of international practice to Tunisian financial institutions and accountants. Transactions may involve public share offerings, public bids, employee stock ownership plans, or other methods agreed to by the GOT and AID.

(iii) Information, Education, and Communication (IE&C)

The Education, Information and Communication program is an action oriented process to broaden and heighten public debate and/or understanding of the privatization program. The principal vehicles for this process will be seminars and observation trips.

(iv) Follow-up/Evaluation Program

The Project will finance technical assistance to the GOT to establish a Follow-up/Evaluation Program designed to monitor and evaluate the performance of privatized firms. The objective is to analyse past transactions to apply lessons learned in future operations and to document and publicize "success stories."

b Decentralization/Privatization of Public Services

The Decentralization Activity supports the decentralization of authority for the planning, construction and operation of public services from the central government to the municipalities, as well as the private provision of such services.

2. Financial Markets Development Component

The objective of the Financial Markets Development Component is to increase the availability of capital to the private sector, especially for the privatization of state-owned enterprises and the expansion of exports. The Project will work towards increasing market forces, reducing the level of government intervention in financial markets, and strengthening private intermediaries Activities are grouped into the following two areas

a. Financial Markets Environment/Policy: The Project will support the continuation of reforms initiated under the Structural Adjustment Program by funding studies on policies, regulations, and practices that inhibit the development of financial markets and institutions. Priority areas include: increasing the transparency of financial statements; dinar convertibility; GOT debt management; securities laws and regulations; and the taxation of financial instruments.

b. Financial Products/Services Development: As a direct corollary to policy and environment issues to be addressed above, the Project will also provide funding for training and advisory services for financial intermediaries to help them introduce and/or improve the financial services required by an open and competitive economy. The following subjects will receive high priority for training and technical assistance: establishment of mutual funds; foreign exchange risk management; securities issuance and trading; export credit insurance. Other priorities may be identified during the implementation of the Project.

G. Implementation

The Project's two major activities, Privatization of SOEs and Financial Markets Development, will be implemented under the guidance of two separate but interlocking committees. The Privatization Committee will comprise only representatives of the GOT, the Institutional Contractor, and USAID while the Financial Markets Committee will draw at least 50% of its members from the private sector. Most Project assistance will be delivered through a single U.S. Institutional Contractor who will provide U.S. as well as local expertise, the latter through subcontracts with local accounting and financial firms. Buy-ins, IQC's, and local direct contracts will be used to conduct evaluations and to bridge the gap until the Institutional Contractor is in place.

Decentralization activities will be implemented separately under the guidance of a GOT Decentralization/Municipal Development Monitoring Committee. Most Project assistance for Decentralization will be delivered by buy-ins, IQCs, and local direct contracts.

H. Recommendation: The Project is recommended for FY 1992 authorization in the amount of $10,000,000 with an obligation of $1,500,000 in FY 1992 and the remaining $8,500,000 to be obligated in FYs 1993-1997.

PROJECT AUTHORIZATION

NAME OF COUNTRY: TUNISIA

NAME OF PROJECT: PRIVATE ENTERPRISE PROMOTION (PEP)

NUMBER OF PROJECT: 664-0346

1. Pursuant to Section 531 of the Foreign Assistance Act of 1961, as amended, I hereby authorize a Grant to the Republic of Tunisia (the "Cooperating Country") of not to exceed Ten Million United States Dollars ($10,000,000) over a five year period from date of authorization, subject to the availability of funds in accordance with A.I.D.'s OYB/Allotment process, to help in financing foreign exchange and local currency costs of goods and services required for the Project. The planned Life of the Project is five years from date of initial obligation.

2. The Project consists of assistance to the Cooperating Country to expand private sector employment and income by aiding in the privatization of State-owned enterprises, the decentralization and devolution government functions, and improvements in the efficiency of financial markets.

3. The Project Agreement, which may be negotiated and executed by the officer to whom such authority is delegated in accordance with A.I.D. Regulations and Delegations of Authority, shall be subject to the following essential terms and covenants and major conditions, together with such other terms and conditions as A.I D. may deem appropriate.

a Privatization and Financial Markets Activities

Except as A.I.D. may otherwise agree in writing, prior to disbursement under the grant or the issuance of documentation pursuant to which disbursement will be made to finance the U.S. technical assistance contract, the Government of Tunisia will furnish to A.I.D , in form and substance satisfactory to A.I.D.:

1. Evidence that a Privatization Committee has been established to carry out the functions described in the Project Agreement, and that it includes participation by the Office of the Prime Minister, the Ministry of Finance, the Central Bank, the Ministry of National Economy, the Ministry of Plan, and A.I.D

ii. Evidence that a Financial Markets Committee has been established to carry out the functions described in the Project Agreement, and that it includes participation by the Central Bank, the Ministry of Finance, selected members of the Privatization Committee, members of the private financial and business communities in a number at least equal to that of the GOT representatives, and A.I.D.

b. Decentralization Activities

Except as A.I.D. may otherwise agree in writing, prior to disbursement under the grant or the issuance of documentation pursuant to which disbursement will be made to finance any assistance for the Project's Decentralization activities, the Government of Tunisia will furnish to A.I.D., in form and substance satisfactory to A.I.D.:

Evidence that a Decentralization/Municipal Development Monitoring Committee has been established to carry out the functions described in the Project Agreement, and that it includes participation by the Ministry of the Interior, the Ministry of Plan and Regional Development, the Ministry of Finance, the Urban Rehabilitation and Renewal Agency, and the National Federation for Tunisian Cities.

The Project Agreement will also include the following covenants:

The Cooperating Country will covenant that, over the life of the Project;

a. It will provide A.I.D. on at least a quarterly basis with information on the progress of the GOT's privatization program. Reports shall provide the names of the entities privatized, the names and nationalities of the purchasers, the value of the assets and shares transferred, the number of employees affected and their disposition, and the method of sale;

b. It will undertake an evaluation of the privatization program to date employing terms of reference acceptable to A.I D.;

c. It will ensure that information on the progress of the GOT's privatization program will be made available to the general public on an on-going basis;

d. It will ensure that opportunities to purchase state owned enterprises are widely publicized and that small businesses and individual investors are given adequate opportunity to purchase such enterprises.

4 Source and Origin of Commodities, Nationality of Services

Commodities financed by A.I.D. under the Project shall have their source and origin in the United States, except as A.I.D. may otherwise agree in writing. Except for ocean shipping, the suppliers of commodities or services shall have the United States as their place of nationality, except as A.I.D. may otherwise agree in writing. Procurement from local sources will be authorized to the extent permitted by the Agency's "Buy-America" Initiative Guidance cable, dated December 5, 1990 (90 State 410442), as may be from time to time amended. Ocean shipping financed under the Grant shall, except as A.I.D. may otherwise agree in writing, be financed only on flag vessels of the United States.

James A. Graham
James A. Graham
Director, USAID/Tunisia
Date: Sept 1, 1992

Clearances:

PROG:PKolar	(draft)
PSO:RRousseau	(draft)
EXO/A/CONT:GDietz	(draft)
RLA:BBarrington	(draft)
RCO:MReynolds	(draft)

I. PROJECT BACKGROUND AND RATIONALE

A. BACKGROUND

1. Tunisian Public Sector

Like many LDC's, Tunisia is today faced with the legacy of overexpansion of its public sector during the 1960s and '70s. In 1985, Public Enterprises (P.E.) accounted for 31% of GDP (almost 70% of non-agricultural GDP), 39% of investment, 36% of domestic credit, and 29% of external debt. P.E. employment had reached about 150,000 or close to 30% of total formal sector employment. Overall the State controlled about 200 enterprises (with at least 50% ownership) and had direct or indirect minority holdings in approximately 300 other industries.

Public enterprises were, and continue to be, a serious drain on public resources. Moreover, they produce high cost and low quality outputs that are forced upon downstream enterprises because of trade barriers which keep out competing imports. This, in turn, undercuts Tunisian competitiveness in export markets. Public enterprises monopolize sources of financing, crowding out potential private sector investors and then squander their resources on highly capital-intensive investment in often inappropriate technologies.

Recognizing such problems, the Government of Tunisia has embarked on an ongoing program of privatization in conjunction with structural adjustment. While the program started off slowly at first, it picked up momentum in 1988 and 1989 with the revision of legislation governing the process and the appointment of a senior level director and expatriate consultants, the latter funded by AID. As of December 31, 1991 about 100 transactions concerning 35 enterprises and generating a total of about $130 million had been completed. Another dozen operations of privatization (or preparations for future privatizations) were also realized without monetary transfer. In addition, some 25 transactions are presently at various stages of processing; they include potentially large operations and/or candidates for Initial Public Offerings (IPO) such as the divestment of state ownership in ICF (Industrie Chimique du Fluor), Ceramique Tunisienne, and the recent decision to open the capital of Tunisair.

Privatizations to date have essentially involved companies in the tourism (hotels), trade, textile, and construction sectors These companies were often chosen because they appeared easier to privatize given their smaller sizes and the absence of public policy implications; also many of these companies experienced financial difficulties which required rapid/radical solutions. Given this situation the majority of transactions have consisted of asset sales with only 11 operations made through sale of shares.

Sales have predominantly been made to Tunisian investors and entrepreneurs (also some banks). Four transactions have attracted foreign partners, while a few operations have involved stock sales to company employees and management "buy outs." The financial costs of privatization have been high since many transactions have required substantial financial restructuring through cancellations, rescheduling, and conversion of existing liabilities. As of June 1990 it was estimated that over $330 million of debts had been restructured by the Government, State organizations and the Banks; of this close to $130 million had been cancelled or converted into equity.

Conversely, social costs have been less important than initially feared. This reflects both the often strict labor constraints imposed by Authorities during negotiations with potential acquirers but also the turnaround (and expansion) of many enterprises following their privatization. A recent analysis done by Inspection du Travail indicates a personnel reduction of 7,500 out of a total of 31,200 employees potentially affected by privatizations. Of the 7,500, only 1,050 persons were actually fired while the remainder left on early retirement or voluntarily.

Tunisian authorities have adopted a very pragmatic and flexible approach throughout the privatization process. First an overall policy was established, stating that **all** enterprises in the "commercial"/competitive sectors were candidates for privatization; conversely all enterprises in the so-called "strategic" sectors (including water and electricity distribution, urban transport...etc) were to be maintained in the public sector for later decisions. Within that framework, the responsible government commission, the Commission for the Reform and Restructuring of Public Enterprises (CAREPP) has made company selections and conducted all operations on an ad-hoc basis refraining from any narrow plan or publication of lists of companies. Selection and publication of companies to be privatized was done with little or no "advance notice." In CAREPP's opinion this approach has eliminated possible lobbying efforts to be removed from lists, collusion between potential acquirers, and possible labor unrest instigated by labor unions.

The Tunisian Privatization program is now entering what CAREPP authorities call its third phase. During the first phase (1987-1990) a large number of smaller enterprises, often in financial difficulties, were privatized. Transactions were relatively simple with a majority realized by asset sales. The financial burden on the State, created by necessary debt cancellations and restructuring, was high. During the second phase (1991-1992) privatizations continued (albeit at a slower rhythm) while Authorities made preparations and identified P.E. candidates for the following phase.

The third phase, which started in 1992 and is to be assisted by this Project, is to involve much larger companies and more complex transactions, principally through stock sales. CAREPP has identified a group of over 75 companies, in a broad range of competitive sectors (including chemical, construction, transportation, mechanical/electrical, manufacturing, agroindustry...etc.) which could be privatized over the next five years. CAREPP asserts that most companies to be privatized are profitable and that 10/15 privatizations per year should be a feasible target. While no consolidated information could be provided on these 75 candidate P.E.s, CAREPP projects the total proceeds from these privatizations at an average of about $100 million/year over the next five years.

2. Tunisian Financial Sector

The Tunisian financial system is similarly dominated by Government-owned institutions and Government borrowing, in spite of significant reforms undertaken in conjunction with the Structural Adjustment Program (SAP). Four of the five largest banks are parastatals; government-owned banks have large shareholdings in Government-owned commercial and industrial enterprises, reinforcing Government dominance of the economy. The Tunisian "financial system," which largely equates to the "commercial banking system", controls 74% of all assets, 76% of credit to the economy, and 91% of deposits. The four largest commercial banks control 76% of banking system assets.

Since the start of the SAP, the Government has partially freed interest rates, given banks autonomy in credit decisions, provided fiscal incentives for investments in the stock market, restructured the tax code, and increased the price at which government debt is sold to financial institutions. These changes have begun to introduce more competition into the system and broaden access to credit.

In spite of these laudable reform efforts, including substantial tax advantages for equity securities, the latter market has expanded little over the past five years in a kind of "chicken and egg" dilemma. Absent a continuous stream of new issues and an active secondary market, demand has not developed. Absent demand, private investors and the

Government (in the form of privatizations) have been reluctant to come forward with new issues. Part of the problem can be attributed to the absence of parallel (or prior) development of bond markets, which remain restricted and limited by inappropriate government policy.

In the commercial banking sector, banks still suffer from the legacy of government controls, in the form of poor quality loan portfolios and the lack of technical and managerial capacity to dynamize a competitive financial sector. The sheltered environment in which they operate has made the banks particularly risk-averse, and kept them insulated from technical and marketing advances found in banking systems elsewhere.

These features, combined with a lack of real competition from other financial institutions, makes it particularly difficult for non-traditional borrowers to obtain access to bank credit In other words, the major segment of the financial system does not respond to private sector business financing needs. These weaknesses will not only make it more difficult to finance efficiently the next wave of privatizations, but also constrain the development of the private sector as a whole.

Further reforms are to be implemented under World Bank guidance which will address some of the weaknesses of the banking system. Other World Bank-encouraged reforms will, at a macro-economic level, reduce the burden of Government deficit financing on the rest of the financial system by eliminating mandatory purchases of Government securities by commercial banks and other financial intermediaries by the end of 1993.

3. Public Services and Infrastructure

The overly centralized nature of the planning, finance and delivery of public services, including infrastructure, is impeding enterprise formation and operation. Infrastructure financing is primarily derived from the national budget, and has been therefore drastically affected by the Structural Adjustment Program and reductions in the public sector deficit. Two principles undergird a modern system of infrastructure finance - municipal borrowing in the private capital markets and the recovery of investment costs from the beneficiaries. Both activities, although permitted by Tunisian law, are poorly accepted and rarely applied.

Appropriate use of the private sector would have a stimulation effect on the formation of SMEs, both in the initial construction phase and later support and service industries. The privatization of urban services such as solid waste and wastewater collection and treatment would directly create new SMEs in an area of emerging environmental technology of great importance in the region.

B. GOT STRATEGY: INCREASE PRIVATE SECTOR ECONOMIC PARTICIPATION

The recently adopted Five Year Plan for 1992-1996 has as a principal objective the continuation and completion of the Structural Adjustment Program (SAP) introduced by the GOT in 1986 with the support of the International Monetary Fund and the World Bank. The PEP Project directly complements the objectives and the stratgies of the new Five Year Plan.

In broad terms the objectives of the Plan are to: maintain a level of growth of six percent per annum; create 320,000 new jobs while reducing the rate of unemployment from 15% to 13%; reduce the current account deficit to 2% of GDP; limit the budget deficit to 1.2% of GDP; and bring inflation down to 5%.
For the first time ever the Plan envisions private investment outpacing public investment.

To attain these objectives the Plan calls for further liberalization of prices and foreign trade; modernization of the financial system; an acceleration of the privatization program; and restriction of the public sector to the provision of key infrastructure (such as communications), social services such as education and health, and the creation of an attractive business environment. The private sector continues to be viewed as the economy's engine of growth.

The Plan places special emphasis on regional development, in particular the poorer regions of the Northwest and South. It also calls for greater decentralization of central government functions and an enhanced role for municipalities in providing public services and infrastructure.

C. USAID/TUNISIA STRATEGY

USAID/Tunisia's strategy is to support the continued emergence of a market-driven, export-oriented economy based on the private sector. The dominant role of parastatals in the Tunisian economy has been identified by USAID, the IBRD, the GOT and others as a key constraint to rapid private sector expansion and its increased competitiveness in international markets. The lack of innovation in the financial sector has also been identified as a key constraint, not only to the privatization program, but also to the growth of the private sector in general.

The Project directly complements two other major activities to be launched by the Mission within the coming year: Management Training for the Private Sector (MTPS) and the Agribusiness Program Grant. Where the PEP Project helps the GOT to create an environment that provokes private firms to increase their economic participation, the MTPS Project helps private sector firms to understand their new environment, and adopt new strategies to take advantage of it. The Agribusiness Program Grant, to be obligated in 1993, focuses on the development of four key agricultural subsectors (olive oil, dates, seafood, and tomatoes) through a combination of policy reform supported by cash transfers and technical assistance. PEP's Decentralization activities are the forerunner to a planned FY 93 project tentatively titled "Private Sector Initiatives in Municipal Development". The latter would combine Housing Guaranty and grant resources to support GOT reforms that will expand the role of the private sector in managing urban growth. Together with the ongoing Development Studies Project, these five activities comprise the Mission portfolio over the next five years.

D. RELATIONSHIP TO OTHER DONORS

The World Bank is the preeminent donor in Tunisia. Its interventions focus on the Structural Adjustment Program (a $250 million Economic and Financial Reform Loan sets the timetable for the SAP over the next three years).

In addition, the World Bank is providing a $130 million Public Enterprise Reform Loan (PERL) to replenish the Fond de Restructuration des Entreprises Publiques (FREP). The action program to be supported by the PERL consists of three components:

(1) institutional reforms (largely studies); (2) program of restructuring and divestiture (labor compensation, redeployment efforts, debt repayments), and (3) action programs for "Priority PEs", namely, the phosphate mining company (CPG), the fertilizer companies (Groupe Chimique) and the railway (SNCFT). The GOT recently submited a request for the next tranche ($60 million) of the PERL to support the upcoming, third phase of the Privatization Program.

The World Bank has also recently signed a Municipal Sector Investment Project for $75 million to encourage greater decentralization and municipal development.

II. DETAILED PROJECT DESCRIPTION

A. PROJECT GOAL AND PURPOSE

The **Project Purpose** is to expand private sector employment and income by privatizing state owned enterprises and decentralizing government functions and improving the efficiency of financial markets. This will contribute to the broader **Goal** of supporting the emergence of a market-driven, competitive economy.

B. PROJECT OVERVIEW

The Project supports the GOT efforts to launch a new phase in its privatization program that depends on the ongoing development of financial markets. In turn, the process of privatization (largely, refinancings of existing enterprises) will in itself serve as a means for the growth of modern financial institutions and practices.

The Privatization/Decentralization Component supports: the sale of state-owned enterprises to the private sector; and on a limited scale, greater decentralization of government services from the central government to the municipalities and further devolution from the latter to the private sector. Decentralization activities will be carried out in connection with the Housing Investment Guaranty Program.

The Privatization of SOEs subcomponent will help launch the third, and potentially liveliest, phase of the Tunisian Program, and will involve four key activities:

-Study and Analysis, including short, business oriented assessments of approximately 50 public enterprises, which would then yield between 20-25 candidates for privatization;
-Transactions, including valuations, marketing strategies, schedules, and prospecti;
-Information, Education, and Communication Campaign; and
-Follow-up and Evaluation.

The Decentralization subcomponent supports technical assistance and studies to help municipalities take on new responsibilities and contract with private sector developers to provide public services.

The Financial Markets Development component is designed to increase the availability of capital to the private sector, especially for the privatization of State-owned enterprises. The Project will address policy and other general issues affecting the financial markets environment, such as the transparency of financial information; and will assist financial intermediaries in the development of new services.

C. PROJECT COMPONENTS

1. Privatization/Decentralization

1.1 Privatization of State-Owned Enterprises

a. Objectives

The overall purpose of this subcomponent is to broaden and accelerate the process of privatization. Over a five year period the GOT has set an objective of privatizing 75 companies, of which approximately 20-25 would be directly assisted by AID. In order to reach this target, the Project will assist the GOT in adopting more sophisticated techniques and approaches. Specific objectives include the following.

(i) Improve the planning and execution process, in particular through minimum levels of transparency, to provide a "level field" to all potential actors in the privatization process: investors, service and intermediary firms, labor unions, and employee groups. This will help fulfill government commitment to democratize public ownership (see iii, below), and foster proactive collaboration with labor unions. It also avoids "bunching" risks at various stages of the privatization process. This includes requiring professional valuations, a sense of balance between a "fair" price and successful/timely execution, and appropriate levels of "public relations" throughout the privatization process.

(ii) Establish feedback mechanisms to progressively introduce and adjust regulations, procedures, and instruments to improve the efficiency of the process and the supply of both projects and funding, in effect capitalizing on a dynamically maturing situation.

(iii) Diversify ownership to expand the number of private sector individuals and companies acquiring SOEs in order to address the criticism that previous sales were made to a limited group of individuals. To fulfill this objective, there will be a deliberate Project focus on developing transactions which attract (a) first and second tier Tunisian investors, and (b) foreign investors.

(iv) Maximize returns to the GOT Treasury within the overriding objective of diversifying ownership.

b. Program

Two key principles guided the design of this Component. First, to design privatization packages to maximize synergy with financial market development. Rapid expansion of financial markets through the Bourse, increasing the funding and stabilizing influence of institutional investors and fostering transparency of operations together with higher quality of financial information and professional standards will help expand the private sector as a whole.

Second, the technical assistance delivery mechanism relies on teaming US banking and industry specialists with Tunisian financial experts. The US experts will bring specialized banking and industry experience, the Tunisian experts will bring not only the requisite accounting and financial skills, but necessary language skills and familiarity with the local context. This mechanism therefore maximizes "transfer of technology" as well as ensuring that the best possible information is obtained in the least possible time.

Specific interventions include technical assistance, studies and observation trips to support: (i) Study and Analysis; (ii) Transactions; (iii) an Information, Education, & Communication Campaign; and (iv) Follow-up/Evaluation Program.

<u>i. Study and Analysis</u>

GOT decisions on which PEs to privatize, and how, are largely based on information provided by the enterprise. This information is typically incomplete, unreliable, and static (accounting oriented rather than providing a complete picture of the business and its prospects). The GOT does not have the technical expertise to evaluate (a) the actual state of health of the enterprise, (b) its prospects for privatization, or (c) the appropriate privatization methods to use in order to attract a broader spectrum of investors, including foreigners. This creates difficulties in developing or effecting strategic plans and there is general dissatisfaction with the valuations (too low) and ownership patterns in the private sector (too concentrated).

In order to assist the Privatization Committee in establishing priority enterprises for Project assistance, the Project will undertake relatively short, business-minded analyses of each proposed enterprise. These analyses, which may be performed individually or for groups of companies, will examine the overall business outlook for the firm, its attractiveness to private sector investors, and possible privatization strategies.

More specifically, these analyses should provide the following.

-- Description of all components of the business
-- Diagnosis of strengths and weaknesses
-- Assessment of financial position, performance, and prospects
-- Identification of needs for additional studies (market, technical, financial audits, etc.)
-- Preliminary identification of possible privatization strategies/alternatives including restructuring needs and estimates of possible value
-- An action plan for proceding with privatization

The analyses will be conducted on up to 50 privatization candidates (roughly 10 the first year, 15 each the second and third years and 5 each in years four and five). They will generally be conducted by Tunisian/American teams composed of an investment banker, accountant and/or financial analyst, and an industry specialist. The exact mix of US and Tunisian experts will depend on the complexity of the enterprise. These teams will conduct 2-3 day site visits in order to update information necessary for decision-making with regard to restructuring and/or privatization.

Based on the information provided, the GOT and USAID will select 20-25 firms to move on to privatization transactions, as discussed below.

The Project will also fund more general studies needed prior to undertaking an action in a particular area. A good example is that of Employee Stock Ownership Plans (ESOPs) where additional study may be needed prior to the GOT making a major commitment to this method of privatization.

ii. Privatization Transactions

According to selections made under the Study and Analysis phase described in (i), above, the Project will help finance technical assistance for the development of detailed privatization action plans including valuations, financial packaging, and marketing for 20-25 public enterprises.

As with the business analyses described in (i) above, all USAID-assisted privatizations will be carried out by mixed "core" teams which will act as privatization advisors to the GOT for a specific operation. This team will be typically composed of one foreign expert (investment banking profile) and one local expert (financial profile). This core team will be assisted/augmented by other experts (US and/or local) such as technical (operations, technology), appraisers (asset valuation), external creditors, lawyers, financial intermediaries (for IPOs, marketing, etc.)

iii. Information, Education and Communication

As the program moves on to the more complex privatizations, the GOT needs to explore new strategies, and publicize more broadly both the rules governing the privatization process, and the evaluation results emerging from the Follow-up/Evaluation Program.

The Information, Education and Communication Campaign is conceived as an action oriented process to broaden and heighten public debate and/or understanding. The principal vehicle for this process will be local seminars and observation trips.

Seminars will be used to raise general awareness. For example, a "sensitization" seminar for the general public would address the pros and cons of privatization in general, present success stories (Tunisia and worldwide), and explain the current Tunisian procedures and program. Emphasis would be placed on benefits of privatization in terms of efficiency, broad participation by public and employees, and the catalytic role of the privatization program in the development of the private sector.

Observation trips would be used to build consensus within the GOT and private sector on appropriate roles, approaches and techniques. For example, a trip to foreign stock exchanges could reassure and motivate GOT policy makers about their new directions and policies; visits to privatized companies and companies that have gone public could help reduce anxieties among Tunisian entrepreneurs concerning the risks of going public.

iv. Follow-up/Evaluation Program

The Project will finance technical assistance to the GOT to establish a Follow-up/Evaluation Program designed to monitor and evaluate the performance of privatized firms. The objective is to analyse past transactions to apply lessons learned in future operations and to document and publicize a few "success stories."

Specific activities include:

-A summary analysis of all past privatization operations to document the transactions' financial parameters and review the before and after (1992) situations in terms of structure, operations, personnel, etc. Information will be obtained from CAREPP files and directly from privatized companies.

-A detailed analysis of six to eight transactions (success stories) covering employee stock participation, management buyout, labor impact, broadened ownership. These studies would then be publicized to "concerned" audiences such as labor unions, professional associations, the press, and universities. Some studies could be built into case studies to be used in university courses.

1.2. Decentralization

i. Objectives

PEP will assist the GOT in the implementation of the Municipal Development Program (HIG 004D), the purpose of which is to increase the involvement of municipalities in the planning, financing and implementation of infrastructure for urban shelter and economic growth. It will support policy analysis and institutional development towards the following objectives:

a. Improve systems for financing municipal development,

b. Adapt infrastructure investments to the requirements of urban economic and shelter growth, encouraging enterprise formation;

c. Devolve responsibility for planning and delivering infrastructure to the municipalities;

d. Increase the role of the private sector in planning, financing, implementing and managing infrastructure and services.

ii. The Program

At the policy analysis level, PEP will provide technical assistance for the review of a number of GOT policies regarding the planning, financing and delivery of urban infrastructure and services. Among the planned studies is an analysis of alternative financing models, including mechanisms for raising private sector capital. Other subjects include taxation, privatization of municipal services and urban environmental policies.

At the institutional development level, the Project will support technical assistance for the following activities:

a. Municipal Development Authority: The Project will assist the GOT to establish an autonomous municipal development authority (MDA) that will manage loan and grant programs to the municipalities. PEP will assist the MDA to establish criteria for eligible investments and the appropriate mix of financing among loan, grant, and municipal resources;

b. Municipal Financial Management: As a direct corollary to the MDA, representative municipalities will be assisted with measures aimed at enhancing revenues including the installation of computerized cost accounting and tax collection systems.

c. Privatization of Municipal Services: In order to encourage municipalities to contract out for services such as solid waste collection, PEP will assist in the development of model contracting documents, identification of pilot projects and the training of municipal staff in contracting procedures.

<u>2. Financial Markets Development</u>

<u>a. Objective</u>

The objective of the financial markets component of the Project is to increase the availability of capital for the private sector, especially for the purchase of State-owned enterprises and for the expansion of exports. The Project will work towards increasing market forces in the financial sector while reducing the level of government intervention.

Activities will take place at two levels: first, assistance for improvements in the financial markets environment, i.e. the policies, regulations and practices which encourage or inhibit the development of markets and institutions; second, assistance to financial intermediaries willing to develop new services in response to the changing environment. AID assistance will be in the form of research studies and seminars, training, and advisory services.

b. <u>Program</u>

i. <u>Financial Markets Environment/Policy:</u> AID will work with the GOT, interested intermediaries and their representative associations to continue the process of financial markets reform already initiated by the GOT as part of the Structural Adjustment Program. Priority areas include the following:

aa) Information: AID will provide a limited amount of expertise from the American accounting profession to assist the Ministry of Finance, the Conseil Superieur de Comptabilite, and the accounting profession's professional organization, the Conseil de l'Ordre des Experts Comptables de Tunisie, in the ongoing reform of accounting laws, regulations, and standards. Such assistance is anticipated to take place during years one and two of the Project.

bb) Government Debt Management: The Project will assist the Central Bank and the Ministry of Finance in their efforts to set new debt management policies, and to organize a secondary debt market Expert advisors will address the following issues and provide recommendations as needed:

-tax, regulatory and other constraints to the development of more active markets;

-the GOT's optimum debt profile taking into consideration the potential impact on private borrowing;

-estimating trading volumes of Treasury and other securities;

-the role of private financial institutions, including the need for a primary dealer system for Treasury securities;

-the feasibility and suitability of developing secondary markets in other instruments, such as commercial paper;

-in the context of the GOT's move to indirect controls of the money supply and credit expansion, the feasibility and effectiveness of open market operations.

cc) Securities Laws and Regulations· AID will assist the GOT in reviewing current securities laws and regulations and adapting them as needed to encourage the further market development. Among the issues to be addressed are:

-legal and procedural constraints to the establishment of mutual funds, or SICAV's (Societe d'Investisement a Capitale Variable); recommendations for overcoming these constraints;

-whether current listing requirements need to be revised to encourage market growth.

-development of futures market operations.

dd) Taxation of Financial Instruments: AID will assist the GOT in an examination of the remaining fiscal constraints to balanced financial markets development. In particular, the study will examine the impact of differential taxation on various financial instruments and recommend changes, if they are needed.

ee) Convertibility: An initial study that focuses on prerequisites, constraints, and a tentative time schedule is now expected to be funded under the Development Studies Project. PEP will provide follow-on assistance that would more closely examine the specific training and technical assistance requirements for foreign exchange market participants, especially commercial banks.

ff) Other: During the course of project implementation the GOT and AID will identify other issues which need to be studied in order to encourage the development of financial markets.

2. Financial Products/Services Development: As a direct corollary to policy and environment issues to be addressed above, the Project will also provide funding for training and advisory services for financial intermediaries to help them introduce and/or improve the financial services required by an open and competitive economy. The following subjects will receive high priority for training and technical assistance:

-establishment of mutual funds;

-foreign exchange risk management;

-securities issuance and trading;

-export credit insurance (COTUNACE)

Additional priority areas may be identified during the implementation of the Project.

In general, the program will work as follows The Project will sponsor a seminar or series of seminars in cooperation with an existing trade association, such as the Association of Professional Bankers or the Association of Brokers in order to provide an overview of the subject as well as initial training. These seminars would be open to all organizations, public and private, on a first come, first serve partial payment basis (50% cost sharing is anticipated). Following these seminars the Project would then provide in-depth advisory services to one or two private institutions that are both capable of and interested in launching the service on a commercial basis.

Selection of specific financial institutions for technical assistance will be made by the Institutional Contractor according to criteria established by the Financial Markets Committee. The following criteria will be refined during the first meetings of the Committee.

-clients. the financial institution must serve private sector enterprises and/or investors;

-ownership private sector preferred, but public organizations may be eligible if they meet criteria for priority subject areas and serve the private sector. The decision to assist a public organization must be approved by the Financial Markets Committee;

-cost sharing. the financial institution must be willing to pay at least 50% of project costs,

-staffing: the IFI must be committed to assigning appropriately qualified staff to work with the Contractor.

Committee members will be prohibited from taking part in any decision on assistance to any organization in which they have a financial or personal interest.

Participating IFI's will make payments in local currency for their share of project costs directly to the Institutional Contractor, who will use these funds to offset any eligible local contract costs. It is anticipated that the Contractor will invoice AID for the full amount of services, <u>net</u> any payments received from beneficiaries. In order to avoid problems of non-payment by beneficiaries, the Contractor will require that at least 50% of the budgeted costs are paid prior to the commencement of services. Cost sharing percentages and methods of payment will be reviewed periodically and updated during the course of implementation.

With respect to COTUNACE, the Project will support the current management's objectives of improving operations, extending programs, developing new products and expanding coverage of exports. First, AID will fund an expert review of COTUNACE's products, technical functions, and internal procedures. This will be carried out by a team of export credit insurance specialists, with expertise in marketing, computer management, and organization. This review will include a study of how COTUNACE's services are developed and sold to exporters and especially to banks, which are eligible (as with FCIA) to take out policies for their customers Interviews with exporters and banks will be an important part of this review. The goal of this review will be to identify exactly which areas of the company's activities could benefit from medium-term TA funded by the Project.

Based on the findings of the above study, the Project will provide TA over a 2-year period to advise COTUNACE on its products, technical functions, or internal procedures and on implementing the recommended changes. Likely areas for assistance are: marketing; new product development; and internal controls. The TA will include an intensive 4-week effort by at least two experts to lay out an action program, with three 2-week follow-up visits annually.

III. IMPLEMENTATION PLAN

A. OVERVIEW

Overall project management will be the responsibility of the USAID/Tunisia Private Sector Office (PSO), which will be assisted by the Regional Housing and Urban Development Office/Near East/North Africa (RHUDO/NENA) for Decentralization activities.

The Ministry of Foreign Affairs will be the Principal Representative of the Grantee for the purposes of signing the Project Agreement. The Ministry of Plan and Regional Development will be in charge of overall coordination and monitoring of the Project. The Director General for Public Enterprises in the Prime Minister's Office will be the principal GOT counterpart for Privatization Activities. The Ministry of Interior, Directorate of Local Authorities will be the principal counterpart for Decentralization activities. The Central Bank and the Ministry of Finance will be the principal GOT counterparts for financial markets activities.

Three Tunisian/American Project advisory committees, one covering privatization, a second dealing with financial markets and a third for decentralization will play an active role in the development and follow-up of all Project activities. Due to current sensitivities about information on privatization candidates, the Privatization Committee will comprise only representatives of the GOT, the Institutional Contractor, and USAID. The Financial Markets Committee will draw at least 50% of its members from the private sector.

Finally, a single U.S. Institutional Contractor will be responsible for delivering most of the Project's foreign and local technical assistance, the latter through subcontracts with local accounting and financial firms. Buy-ins, IQC's, and AID-direct local contracts will be used to bridge the gap until the Institutional Contractor is in place, as well as for all decentralization activities and evaluations.

B. ROLES AND RESPONSIBILITIES

1. Privatization/Financial Markets

a. Privatization Committee: The Privatization Committee will establish Project priorities, assign implementation responsibilities to committee members or other GOT ministries, review contractor workplans and progress reports, and participate in project evaluations. On the Government of Tunisia side the key members of the Committee will be the Director Generals from the following directorates:

-Public Enterprise/Office of the Prime Minister;
-Participations Department/ Ministry of Finance;
-Enterprises/ Ministry of Plan and Regional Development;
-Investments/ Ministry of National Economy, and;
-Director of Credit/ Central Bank.

Other ministries may participate depending on the particular enterprise to be privatized. The Committee will also include representatives from the USAID Private Sector Office and the Institutional Contractor

More specifically, the Privatization Committee shall be responsible for:

(i) Start-up activities

-- Approve scopes of works for the U.S. Institutional Contract and local short-term contract(s)
-- Participate in the evaluation of proposals for the Institutional Contract and local short-term contract(s)
-- Adopt criteria for public enterprises to be privatized with Project assistance

(ii) Implementation activities

-- Review and approve annual workplans including lists of public enterprises for initial analyses and those to be privatized with Project assistance
-- Review contractor progress reports
-- Review and approve scopes of work for proposed policy studies
-- Participate in Project evaluations

USAID will have final approval over PEs to be privitized with Project assistance, in accordance with the criteria established by the Privatization Committee.

b. Office of the Director General for Public Enterprises (DGEP)

The Office of the Director General for Public Enterprises (DGEP) will serve as the day to day counterpart for the Privatization Component. The DGEP will act as the chair of the Privatization Committee, sit on the evaluation committee for the U.S. Institutional Contractor, prepare the lists of candidate firms for US technical assistance, and assist the Institutional Contractor in coordinating privatization assistance. The DGEP will also be responsible for providing AID with quarterly progress reports on the overall status of privatization activities.

c Financial Markets Committee

A separate committee will be created for the financial markets component of the Project. Like the Privatization Committee, it will establish priorities for financial markets activities, assign counterpart responsibilities, review contractor workplans and progress reports, and participate in Project evaluations. This Committee will include private sector representatives from a cross section of financial intermediaries and at least one private entrepreneur, who will make up at least 50% of the Committee. The GOT representatives will include some of the members of the Privatization Committee, in particular the representatives of the Central Bank and the Ministry of Finance, and others designated by the GOT. AID and the Institutional Contractor will also be represented.

d. Institutional Contractor

All Privatization/Financial Markets activities, with the exception of start-up activities and external evaluations, will be implemented through a single U.S Institutional Contractor who will retain a lead local accounting firm (either through a joint-venture or subcontracting arrangement) to provide in-country project management and other services during the life of the contract. Additional local firms will be subcontracted for discrete activities such as valuations. The Contractor will also provide an expatriate advisor who will visit Tunisia on a regular basis throughout the life of the Project.

The Expatriate Advisor will be a senior privatization/financial markets expert who will provide the GOT and AID with an objective reference point for developing and adopting new strategies for implementing the third phase of Tunisia's privatization program. He/she will also play a key role in the development and implementation of financial markets activities.

The lead Tunisian accounting firm will act as the day to day point of contact between the Institutional Contractor and the two relevant committees. This firm will provide a senior level individual with a financial/investment banking profile and a minimum of 15 years private sector experience. The individual will play a key role in coordinating all in-country activities, including the fielding of local accounting, financial and other expertise required for privatization diagnostics and transactions. This person will also provide substantial input to the Institutional Contractor's IE&C and evaluation activities.

e. Interim Local Advisor

During the initial phase of the Project prior to the arrival of the Institutional Contractor, USAID will contract with a local Tunisian accounting firm to provide expertise, primarily in valuations, for the Privatization Committee.

f. USAID/Tunisia Private Sector Office

Within USAID/Tunis, the Private Sector Office (PSO) will be responsible for overall Project management, and for day to day management of the privatization and financial markets activities. The PSO will play a key role in convening early sessions of the two relevant committees, ensuring that members are informed of Project timetables, programs and the roles they are to play within the Project. The PSO will draft the terms of reference for the US technical assistance contract and interim local contracts and chair the committee established to review proposals. Finally, the PSO will serve as the technical counterpart for the U.S. Institutional Contractor. As such, this office will be responsible for reviewing and approving annual workplans, and monitoring contractor performance. The PSO will also be responsible for managing mid-term and final evaluations of the Project.

2 Decentralization

a. Decentralization/Municipal Development Monitoring Committee (MDMC)

The MDMC will establish Project priorities, assign implementation responsibilities to Committee members or other GOT ministries and public utilities, review and update a Policy Action Plan (PAP), organize annual reviews and participate in project evaluations. The key GOT members of the MDMC will come from the following directorates/ ministries (representatives are Director Generals unless otherwise noted):

-Local Authorities/ Ministry of Interior (DGCPL);
-Municipal Development Authority (CPSCL)/Ministry of Interior;
-Projects/ Ministry of Plan and Regional Development;
-Local Authorities/ Ministry of Finance;
-Urban Rehabilitation and Renewal Agency (ARRU); and
-the President of the National Federation for Tunisian Cities (FNVT).

Other ministries or public utilities dealing with urban infrastructure may also participate in the MDMC meetings.

Specifically, the MDMC shall be responsible for:

-reviewing and updating the policy action plan and related monitoring indicators and schedule;
-reviewing the technical assistance and training plan including activities necessary to implement the policy action plan;
-monitoring implementation of activities in particular privatization activities;
-reviewing and adopting conclusions and recommendations of policy studies;
-participating in annual reviews and project evaluations

b. Office of the Director General for Local Authorities (DGCPL)

The Office of the Director General for Local Authorities (DGCPL) will be the main conterpart for the Decentralization component. The DGCPL will act as the Chair of the MDMC, review progress towards the objectives of Municipal

Development programs, contribute to achievement of these objectives in particular: (i) establishment of the Municipal Development Authority, (ii) improvement of municipal revenues, and (iii) private sector participation in municipal development projects. The DGCPL will also assist participating municipalities in developing privatization activities. In addition, the DGCPL will provide USAID with annual progress reports on the overall status of the Decentralization Component.

c. Regional Housing and Urban Development Office (RHUDO)/NENA

PEP's decentralization activities will be managed by the RHUDO/NENA who will coordinate on a regular basis with the USAID Private Sector Office. Day-to-day management activities will be supervised by a PEP-funded Tunisian PSC.

C. IMPLEMENTATION SCHEDULE

1992

AID/GOT sign PROAG	8/92
AID/GOT prepare & approve RFPs for U.S Institutional Contractor and Interim Tunisian Contractor	9/92
Consultative Committees appointed	10/92
Interim Tunisian Contractor selected	10/92
Privatization Committee meets 1. agrees on working procedures 2. appoints representative for Institutional Contractor evaluation committee	10/92
Financial Markets Committee meets 1. agrees on working procedures 2. approves scope of work for Financial Info study	10/92
AID issues RFP for Institutional Contractor	10/92
AID executes Buy-in for Financial Information Study	11/92
Decentralization Committee meets 1. agrees on working procedures 2. Reviews Policy Action Plan and agrees on priority studies and TA	11/92

1993

AID/Committees evaluate proposals for Institutional Contractor	1/93
AID signs contract with U.S Contractor	4/93
Contractor's Expatriate Advisor arrives for first visit and in cooperation w/Committees develops first annual workplan to include -priority firms for privatizations -priority financial markets studies/TA	5/93
Committees and AID approve annual workplan	6/93
Contractor starts first round of SOE analyses	6/93
Study of past privatizations conducted	8/93

Study of ESOPs conducted	8/93
Privatization Committee reviews SOE analyses and selects next round of privatizations	9/93
Contract with Interim Tunisian Contractor closed out	10/93
Decentralization Committee meets to review and update Policy Action Plan	10/93

1994

Contractor develops second annual workplan	5/94
AID/Committees approve workplan	6/94
Contractor initiates second round of SOE Analyses	6/94
Project's provision of TA for decentralization assumed by new Private Sector Initiatives in Municipal Development Project or other funding mechanism	10/94

1995

Contractor develops third annual workplan	5/95
AID/Committees approve workplan	6/95
AID contracts for mid-term evaluation	6/95

1996

Contractor develops fourth and final annual workplan	5/96
AID/Committees approve workplan	6/96

1997

AID contracts for final evaluation	6/97
Project Assistance Completion Date	9/97

D. PROCUREMENT PLAN

Most Project activities will be implemented through a single U.S Institutional Contractor chosen through full and open competition. During the interim period between Project Agreement signature and the signing of the institutional contract AID will contract for the services of one or more local accounting firm(s) to perform valuations and other analyses of companies to be privatized. During this interim period AID will also "buy-in" to a centrally managed project for financial and accounting expertise. All decentralization activities will be contracted for through IQC's, buy-in's, and monitored by one local PSC. Finally, the two project evaluations will be done through IQC work orders.

Details of planned procurement are as follows:

1. U.S. TA for Privatization/Financial Markets

    a. Type of Contract: AID direct contract

    b. Services to be Procured.

       Technical assistance for planning, execution and evaluation of privatization and financial markets activities, a senior level privatization/ financial markets expert to visit Tunisia on a regular basis; subcontracting with local accounting and financial firms to perform valuations and other preparatory work for privatizations; possible limited commodity procurement.

    c. Estimated Dates of Contract:

       April 1993 - September 1997

    d. Estimated Cost of Contract: $9,117,000

    e. Potential for Minority Contract:

       RFP will require participation and involvement of Gray Amendment contractors, as subcontractors or members of a contractor consortium.

    f. Need for Waiver:

       None are anticipated. U S nationality is antipated for prime contractor.

    g. Contracting Officer: Regional Contracting Officer

    h. AID Method of Financing Direct Reimbursement

2. Interim Local TA for Privatization

a. Type of Contract: AID direct contract(s)

b. Services to be Procured.

Valuation, financial, and other services for privatization program

c. Estimated Date of Contracts:

September 1992 - October 1993

d. Estimated Cost of Contracts: $160,000

e. Potential for Minority Contract:
U.S. contractors will be required to comply with regulations providing for minority sub-contract opportunities

f. Need for Waiver: None anticipated

g. Contracting Officer: USAID Mission Director

h. AID Method of Financing: Direct Reimbursement

3. Financial Information Study

a. Type of Contract· Buy-in

b. Services to be Procured:

Accounting expertise

c. Estimated Date of Contract:

October 1992 - December 1992

d. Estimated Cost of Contract: $203,000

e Potential for Minority Contract:
None anticipated

f. Need for Waiver. None anticipated

g. Contracting Officer: AID/W Contracts Office

h. AID Method of Financing: Direct Reimbursement

4 Technical Assistance for Decentralization

a Type of Contracts: Buy-ins and IQC work orders

b. Services to be Procured:

Technical assistance and studies related to decentralization and privatization of public services

c. Estimated Date of Contracts:

Multiple buy-ins/work orders from 9/92 - 6/94

d. Estimated Cost of Contracts: $350,000

e. Potential for Minority Contract:

U.S contractors will be required to comply with regulations providing for Gray Amendment sub-contract opportunities

f. Need for Waiver: None anticipated

g. Contracting Officer: AID/W Contracts Office

h AID Method of Financing: Direct reimbursement

5. Local Technical Services for Management of Decentralization Activities

a. Type of Contract: USAID/Tunisia PSC

b. Services to be Procured: Project management

c. Estimated Date of Contract:

October 1992 to September 1994

d Estimated Cost of Contract: $50,000

e. Potential for Minority Contract:

Local contract, not applicable

f Need for Waiver: None anticipated

g. Contracting Officer: Mission Director or RCO

h. AID Method of Financing: Direct Reimbursement

6. Technical Services for Audit and Evaluations

a. Type of Contract:
Work Orders under established
Indefinite Quantity Contracts (2-3)

b. Services to be Procured:

Technical assistance for mid-term and final evaluations

c. Estimated Dates of Contracts:

Work Orders to be issued in 1995 and 1997

d. Estimated Cost of Contracts. $120,000

e. Potential for Minority Contract:

Gray Amendment IQC contractors will be given priority consideration

f. Need for Waiver: None anticipated

g Contracting Officer: AID/W Contracts Office

h. A.I.D. Method of Financing: Direct Payment

E. GRAY AMENDMENT

As required by the Federal Acquisition Regulations (FAR), offerors for the major institutional contract to be let under this Project will be required to present minority subcontracting plans. It is anticipated that the successful offeror will subcontract, as required, with Gray Amendment firms.

Priority will be given to Gray Amendment firms for Project evaluations.

IV. COST ESTIMATES AND FINANCIAL PLAN

The Project, estimated to cost a total of $15.900.000 over five years, will be funded by A.I.D., the GOT, and the private sector. A.I.D 's contribution will be a total $10.0 million, of which $1.5 million will be contributed in Fiscal Year 1992 and the remainder over Fiscal Years 1993-1996. GOT contributions will be approximately $4 5 million, while the private sector will fund $1.4 million, excluding the purchase price of SOEs. Tables 1 and 2 are supported by the detailed cost estimates in Annex 7.

A A I D. CONTRIBUTION

A I.D. funds will be used primarily to cover the costs of a U.S. Institutional Contractor who will provide both expatriate and local advisors for privatizations and financial markets activities. During the period between Project signing and execution of the institutional contract, AID will also cover costs of valuations performed under a separate contract(s) with a local accounting firm(s).

The proposed technical assistance contract is budgeted at $9.1 million which includes the costs of roughly 250 person months of technical assistance, overhead and fees.

B NON A.I.D. CONTRIBUTION

The Tunisian contribution to this Project will come from both the Government of Tunisia and the private sector. The GOT's estimated contribution of $4.5 million will cover the following costs project management costs including the costs of the three Project committees and designated project representatives at the Office of the Prime Minister, the Central Bank, and the Ministry of Interior; office space and other in-kind support for expatriate teams, and brokerage fees estimated at 1% of the value of each share offering.

Not specifically included in the Government's required contribution are funds that the GOT is expected to pay out of the Fund for Restructuring Public Enterprises (FREP) for social security obligations, severance payments, and foreign debts. The GOT has requested the World Bank to provide $60,000,000 in loan funds to replenish the FREP for the next five year period.

Private sector financial intermediaries are expected to pay for approximately one-half of the cost of technical assistance and training provided to them under the Project, including air fares. The private sector contribution is expected to total $1.4 million.

C. COST FACTORS

Short-term US TA	$27,330/month
Tunisian TA	$15,985/month
Tunisian PSC	$ 7,000/month
U.S Training/Observation	$ 8,000/person

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TABLE 1
PRIVATE ENTERPRISE PROMOTION PROJECT
SUMMARY COST ESTIMATE AND FINANCIAL PLAN
(000 U S DOLLARS)

	AID			GOT			PRIVATE SECTOR			TOTAL		
	FC	LC	TOTAL	FC	LC	TOTAL	FC	LC	TOTAL	FC	LC	TOTAL
I PRIVATIZATION/FINANCIAL MARKETS	6,122	3,358	9,480		4,389	4,389		1,341	1,341	6,122	9,088	15,210
A VALUATIONS (LOCAL CONTRACTS)		160	160								160	160
B FINANCIAL STUDIES (BUY INS)	203		203							203		203
C U S CONTRACTOR	5,919	3,198	9,117					1,341	1,341	5,919	4,539	10,458
D GOT PRIVATIZATION MANAGEMENT					1,839	1,839					1,839	1,839
E BROKERAGE COSTS					2,400	2,400					2,400	2,400
F GOT FINANCIAL MARKETS MANAGEMENT					150	150					150	150
II DECENTRALIZATION	146	254	400		100	100				146	354	500
III EVALUATION	120		120							120		120
TOTAL	6,388	3,612	10,000		4,489	4,489		1,341	1,341	6,388	9,442	15,830

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TABLE 2
PRIVATE ENTERPRISE PROMOTION PROJECT
SUMMARY BUDGET BY FISCAL YEAR
(U S DOLLARS)

	1993	1994	1995	1996	1997	TOTAL
AID CONTRIBUTION						
I PRIVATIZATION/FINANCIAL MARKETS	1,190,248	2,151,756	2,168,133	2,093,017	1,876,864	9,480,018
A LOCAL CONTRACT VALUATIONS	159,847	0	0	0	0	159,847
B BUY-IN(S) FINANCIAL STUDIES	203,453	0	0	0	0	203,453
C U S CONTRACTOR	826,948	2,151,756	2,168,133	2,093,017	1,876,864	9,116,718
1 0 PRIVATIZATION	445,664	1,081,862	1,056,564	937,853	983,683	4,505,626
2 0 FINANCIAL MARKETS	198,716	730,760	754,051	778,136	495,443	2,957,106
3 0 CONTRACTOR MANAGEMENT	182,569	339,134	357,518	377,028	397,738	1,653,986
II DECENTRALIZATION	175,260	225,211	0	0	0	400,472
III EVALUATION	0	0	57,989	0	61,521	119,510
TOTAL AID	1,365,509	2,376,967	2,226,122	2,093,017	1,938,385	10,000,000
OF WHICH						
FOREIGN COSTS	778,446	1,563,267	1,498,246	1,376,495	1,171,707	6,388,161
LOCAL COSTS	587,063	813,700	727,876	716,521	766,678	3,611,839
GOT CONTRIBUTION						
I PRIVATIZATION/FINANCIAL MARKETS	780,000	902,222	902,222	902,222	902,222	4,388,889
II DECENTRALIZATION	50,000	50,000	0	0	0	100,000
TOTAL GOT	830,000	952,222	902,222	902,222	902,222	4,488,889
PRIVATE SECTOR CONTRIBUTION						
I PRIVATIZATION/FINANCIAL MARKETS	155,401	320,126	329,730	339,622	196,009	1,340,887
TOTAL PROJECT	2,350,910	3,649,316	3,458,074	3,334,861	3,036,616	15,829,777

An inflation rate of 3% has been applied to U.S. technical assistance and 7% to local TA.

D. METHODS OF IMPLEMENTATION AND FINANCING

Method of Implementation	Method of Financing	Approx Amount ($000)
T.A.: A.I.D. Direct Institutional Contract w/ U.S. Firm	Direct Reimbursement	9,117
Interim T.A.: A.I.D. Direct Institutional Contract w/ Local Firm	Direct Reimbursement	160
Financial Information Study: Buy-in	Direct Reimbursement	203
Decentralization Buy-ins	Direct Reimbursement	350
Decentralization PSC	Direct Reimbursement	50
Evaluation & Audits	Direct Payment	120
TOTAL		$ 10,000

E. AUDIT

The USAID/Tunisia project officer will carefully monitor the audit plans during the course of Project implementation and make necessary amendments to the Project budget for additional auditing needs if warranted.

Within the budget for the Institutional Contract, funds are provided for pre-award and annual financial audits of subcontractors receiving funds in excess of $25,000. Performance of the audits should be initiated by the Institutional Contractor using a scope of work approved by the USAID/Tunisia Private Sector Office and the Controller. The Institutional Contractor should have an audit plan which provides for annual visits by the audit firm to each sub-contractor that has received A.I.D. funds of over $25,000 and an annual written audit report on funds usage and internal control adequacy.

Periodic financial audits will be done on the Institutional Contractor by the cognizant federal audit agency and a final close-out audit will be conducted at the end of the Project.

V. MONITORING AND EVALUATION PLAN

A. MONITORING

USAID's Private Sector Office (PSO), with the assistance of RHUDO for Decentralization activities, will be responsible for monitoring Project implementation and the timely reporting and resolution of problems The objectives of the monitoring plan are to assure that:

1) Project inputs arrive in a timely fashion,
2) Continued progress is made towards Project objectives.

The following types of monitoring activities will be undertaken for each Project component:

1. Management Information System. The Institutional Contractor shall develop a management information system with the DGPE and USAID for coordinating and tracking inputs and outputs. On a quarterly basis, the Institutional Contractor and DGPE shall prepare a report on activities completed, in progress and planned to be submitted to the Privatization Committee and USAID.

In addition, the Institutional Contractor and the DGEP will collect baseline data on the 75 public enterprises slated for privatization over the next five years. This data will include information about turn-over, exports, imports, value added, numbers of employees, installed capacity, and, whenever possible, a management appraisal (use of human resource development, technology sourcing, market assessments, quality circles, etc.). The final evaluation will then compare the base-line, with mid-point and final readings to evaluate the impact of (1) the liberalization process and (2) the privatization process on firm-level productivity and competitiveness.

2. Meetings. USAID will participate in regular meetings of the Privatization Committee and the Financial Markets Committee that will take place on at least a semi-annual basis. In addition, USAID will also participate in working level subcommittes as well as meetings of the Inter-Departmental Commission that concern valuations to be funded by AID. In addition, the PSO will meet regularly with the DGEP, the representatives of the U.S. Institutional Contractor, and other recipients of Project assistance (e.g., the Tunis Stock Exchange, COTUNACE, commercial banks, brokers).

3. Contractor Reports. A key source of information for AID monitoring activities are contractor reports. These shall include the quarterly reports discussed in (1), above, annual work plans; analyses of SOE's proposed for privatization, and, privatization plans.

B. EVALUATION

The project plans to conduct two separate evaluations; an external mid-term evaluation, and a final evaluation. The GOT will be invited to participate in both the mid-term and the final evaluation.

1. Mid-Term Evaluation

This evaluation will be conducted by an outside contractor roughly 24 months after the start-up of the institutional contract in order to review Project progress and recommend mid-course modifications that may help to attain Project objectives. Questions to be asked include the following:

What privatization methods have been used and which have been most successful?

What problems, if any, are preventing successful implementation of the Project?

What is the level of Government of Tunisia commitment to the program?

Are the Project committees, Institutional Contractor, and AID performing their functions effectively?

What improvements have been made in process transparency?

What has been the impact to date in terms of income growth, exports, competition, and job creation?

What mid-course modifications are required?

2. Final Evaluation

The final evaluation will concentrate on the Project's overall impact on private sector expansion. Questions to be examined in the final evaluation will include:

What was the impact on privatized firms themselves? Any improvements in quality, productivity, exports, industrial integration, higher ratios of skilled to unskilled labor?

What was the impact on the sector in which a privatization occurred? Was it a positive stimulus to others?

Did the incidence of stock ownership increase? Does it reflect a broader spectrum of investors? Are more private firms going public? Is there less debt financing of new investments?

Has long- and short-term investment capital availability increased for the private sector?

Is there an increased incidence of the private sector providing public services -- and providing them better?

To what extent did teaming US with Tunisian accounting and financial firms result in technology transfer and improved technical capacity?

VI. SUMMARIES OF ANALYSES

A. TECHNICAL ANALYSIS

The Project's Privatization Component capitalizes on the regulatory reforms that have occurred since the start of the Structural Adjustment Program, especially in the financial markets area, while overcoming some of the key weaknesses of past privatizations. It's emphasis on more systematic planning, sales of firms through widely publicized share offerings and employee stock ownership plans, increased transparency, and better feedback and evaluation systems all work to increase the probability that the Government's objective of privatizing 75 enterprises over the next five years will be attained.

The choice of public share offerings as the principal means for the next wave of privatizations is supported by the recent successful offerings of TD 7.5 million in Housing Bank stock (June 1992) and TD 7.0 million in Tunisie Leasing (March 1992). These illustrate the public's potential interest in additional equity issues. The fact that Tunisie Leasing was bought by almost 1000 investors, many of them individuals, indicates that public offerings are an effective method of achieving one of the Project's objectives, i.e. avoiding the concentration of wealth in a few powerful private conglomerates.

The inclusion in the Project of an Information, Education, and Communication Campaign addresses a clear need to document and broadly publicize privatization success stories. Many privatizations have been successful and have resulted in an expansion of jobs and income, but they have not been advertised The Campaign will help to demystify what is going on and why it is to the benefit of Tunisia to continue with and even speed up the process.

Transparency (i.e. of financial reporting) is also one of the early foci of the Project's financial markets activities. The lack of accurate financial information has been an impediment to the development of both the commercial banking and securities industries as it increases the level of risk for lenders and investors, and concommitantly the cost of capital to enterpreneurs.

Because of the importance of securities markets to the privatization program, the Project will also support the development of a sound, active secondary debt market which will benefit the Tunisian financial system in two main ways:

- create greater liquidity in the financial sector. (Improved liquidity is virtually a pre-condition for successful privatizations of significant size, so that underwriters and other investors can shift investments readily between cash and equities.)

- establish a market-based reference price for other interest rates

Finally, technical analyses performed in conjunction with the approval of the Municipal Development Pilot Program (HG 004D) demonstrate that the decentralization of authority to municipalities will result in improvements in the delivery of infrastructure required for private sector growth (Annex 6).

B. ADMINISTRATIVE ANALYSIS

The Project design takes into account a number of factors that will have a direct bearing on successful implementation. Key among these are the following:

1) The limitations on Mission management resulting from the impending reduction in American direct hire staff to six ceilings by the end of September 1992, including the elimination of key staff positions of Controller and Regional Legal Advisor;

2) The need for highly professional foreign expertise in privatization and financial markets on fairly short notice (and the demonstrated inability of central contracts to provide such experts in a timely fashion);

3) The availability of local expertise in accounting and finance, and the opportunity to improve such capabilities through on-the-job experience (i.e. developing share offerings to privatize State-owned firms);

4) The Government of Tunisia's interest in preventing collusion among private sector investors versus the need to involve the private sector in decisions on financial markets development;

5) The importance of not losing momentum in the privatization program while a U.S. institutional contractor is being selected.

6) The fact that the Project's Decentralization Activities complement and support the $15 million Municipal Development Pilot Program (HG 004D) managed by the Regional Housing and Urban Development Office (A detailed Administrative Analysis of the program is included in Annex 6).

As a result, the Mission has chosen to: implement the Project's Privatization and Financial Markets activities through a single U.S. institutional contractor who will maximize the use of local expertise; and to delegate full responsibility for the management of Decentralization Activities to the RHUDO/NENA. During the interim period between Project signing and the first visit of the Contractor's Privatization/Financial Markets Advisor, one or more separate local contractors will provide services in the area of valuation in order not to lose momentum during a critical stage in the privatization program.

The need for separate committees for privatization and financial markets was dictated by the GOT's interest in avoiding public disclosure of the names of privatization candidates prior to the completion of initial studies, versus USAID's interest in maximizing the involvment of representatives from the private sector, especially in financial markets activities. An alternative approach, one committee covering both components plus a GOT/AID committee on privatization, was unacceptable because it implied a special role for the private sector in selecting companies for privatization. In any event the work of the two committees will be closely coordinated as several members of the Privatization Committee will also be members of the Financial Markets Committee.

The two Project committees described above will include key representatives from CAREPP, the Commission on the Reform and Restructuring of Public Enterprises, and the Inter-Departmental Valuation Commission. Together these the commissions make up the core of the GOT's privatization team. CAREPP, established by legislation in 1987, is chaired by the Prime Minister and has been the principal force in all phases of privatization from setting privatization strategies and priorities, initial identification/selection of firms to be sold, and approving the final terms of all sales. Its technical subcommittee, CTAREPP, is chaired by the Director General of Public Enterprises (DGPE), whose office provides full-time technical support for CAREPP.

The Inter-Departmental Valuation Commission plays the lead role for the Government once a decision has been taken to privatize an enterprise. It contracts with local and/or foreign firms to perform financial valuations, sets the initial terms of sales and public offerings, contracts with local brokers to execute sales, and evaluates offers in the case of liquidation. Its chairman is the Director General of the Participations Department at the Ministry of Finance, which has responsibility for managing the State's shareholdings in numerous commercial and industrial enterprises and regulates the accounting profession. The Director General for Public Enterprises and the Director General for Participations will be a member of the Privatization Committee as well as the Financial Markets Committee.

For the implementation of the Financial Markets component the joint private/public committee will ensure that policy and regulatory studies funded by the Project will be action oriented. The proposed balance between representatives of the banking industry and the securities industry will also guaranty that Project activities do not unduly favor one sector at the expense of the other.

C. FINANCIAL ANALYSIS

The Project's financial viability depends on two conditions being met: 1) investors will have sufficient resources to buy out State-owned enterprises, and 2) companies, once privatized, will be profitable.

As mentioned in the technical analysis, several recent successful public share offerings, as well as improvements in the financial markets that will be funded by the Project, indicate that the first condition will be met. For example, in March 1992 an offer of Tunisie Leasing stock (10.5% of the company's stock for a total value of over TD 7 million), was four times oversubscribed; the stock was finally bought by almost 1000 investors. Its price remains today above TD 20, as compared to its TD 17.8 subscription price. In June 1992 the State-owned Housing Bank completed the first step of its privatization with a public share offering of TD 7.5 million. Some 1040 private shareholders (including 280 bank employees and 80 small investment groups) subscribed for the 1.5 million shares at TD 5 per share A second tranche of TD 7.5 million will go on the market in a few weeks.

More generally, the financial market's capacity to absorb future privatizations (at the level projected by CAREPP) and other capital increase operations should not constitute a constraint, if these markets are well managed and supervised. Project technical assistance and training will provide a substantial boost in this regard. With total deposits in the banking system exceeding TD 5 billion, funds from savings accounts alone potentially provide an ample supply: Savings deposited in savings accounts in banks reached TD 1.8 billion on December 31, 1991 with a growth of TD 200-300 million/year over the past three years. Savings accounts in Caisse d'Epargne totaled an additional TD 360 million. These figures show that, by any measure, it should be feasible to "divert" about $100 million/year towards privatization, including the purchase of attractive public stock offerings.

With respect to the second condition for the financial feasibility of the Project, i.e. the viability of each privatized enterprise, the detailed analysis performed prior to an actual offering of shares or assets will tend to assure that only viable enterprises, or blocks of assets, are actually put up for sale. Otherwise, private investors, who will independantly perform their own analyses of the merits of each enterprise and form their own judgments, will not be interested.

Finally, financial analysis performed in conjunction with the Municipal Development Pilot Program demonstrates that municipalities will have adequate resources to pay for infrastructure improvements that will be funded through mechanisms being designed under the PEP Project (Annex 6).

D. SOCIAL ANALYSIS

1. Socio-Cultural Context

With the economic crisis of 1986 and the ensuing adoption of the Structural Adjustment Program, Tunisia began emerging from close to thirty years of state control of almost every facet of the economy. The change of political power in 1987 has served to hasten the transformation from a socialist to market-oriented free enterprise system

Such dramatic changes in the political and economic landscape have challenged individuals from both the private and public sectors to develop the new attitudes, skills and behavior required in a market economy. For those in the public sector the changes have meant giving up the power and prestige of direct control over the economy; for those in the private sector it has meant competing not only with their Tunisian counterparts, but also with the rest of the world.

2. Beneficiaries

The primary beneficiaries will be the entrepreneurs and other investors (including employees) who purchase State-owned firms or who obtain capital through better functioning financial markets. Secondary beneficiaries include other employees of newly privatized or expanded enterprises, and local consumers Ultimately the Tunisian economy as a whole will benefit from increased employment and economic growth generated by new and expanding companies.

Typically, Tunisian enterprises are family owned and managed. The presence of outside investors is limited, although the concept is gaining wider acceptance. With respect to operations and management, several themes predominate: decision making based on personal relationships; a focus on production with less consideration given to customer satisfaction and service; and the absence of long-term planning.

3. Gender Issues

Women represent close to 20% of the total labor force. While the largest percentage of women workers are employed as laborers in the apparel industry, women are also emerging as a significant force in the ranks of entrepreneurs and managers. Indicative of their influence at these levels was the recent formation of "Les Femmes Chefs d'Enterprise" within UTICA, the national trade organization, to further promote the role of women in the economy.

Project activities do not lend themselves to a specific strategy of targetting assistance to women entrepreneurs, managers, or laborers. However, PEP's objective of diversifying the ownership of firms being privatized and expanding the availability of capital to the private sector will have a beneficial impact on all entrepreneurs who are not currently in the mainstream of the economy. Two other major projects expected to be launched by USAID within the coming year, the Management Training for the Private Sector Project and the Agribusiness Promotion Grant will specifically target women as direct recipients of project assistance.

4. Participation

The Project has been designed in close collaboration with officials of the Tunisian Government responsible for the planning and execution of the privatization program as well as those responsible for financial markets reform. The opinions of private sector businesspersons and financial sector representatives have been sought out at every juncture in the design process.

Private sector beneficiaries will participate on the Project committees responsible for financial markets and decentralization activities. At this point in the privatization program the Government is still unwilling to involve the private sector in the planning stage out of fear of collusion among investors and possible labor unrest. However, once privatization candidates are identified and a value has been set by independant appraisers, the Government will widely publicize their availability to potential investors. Furthermore, the Project will fund an Information, Education, and Communication Campaign aimed at increasing understanding and support for the program among the general public and investors.

5. Socio-Cultural Feasibility

Over the past six years the Government of Tunisia has succeeded in convincing many of its citizens that the structural reform program (including privatization, decentralization and financial markets reform) is the only alternative for the future prosperity of the Tunisian economy. Privatization activities are aimed at overcoming remaining resistance from government bureaucrats, labor union leaders and members, and the general public by better publicizing the past successes of the privatization program, broadening ownership to a wider spectrum of investors (including employees), and increasing process transparency.

Project success will also depend on the willingness of the private investors to take on the challenge being offered by the Government, their ability to respond to market signals, and adopt modern management practices and new technologies. To date the private sector has shown that they are willing to respond positively and are trying hard to reorient the direction of their businesses in order to become more competitive.

6. Impact

The potential social impact of the Project is enormous. By creating new private enterprises (through privatizations as well as increasing the availability of capital), expanding existing enterprises, and shifting services to municipalities, the Project will help to decentralize both economic and political power. Share ownership of newly privatized firms will give private citizens a more direct voice in operations and management. The same holds true for employees who may benefit from the Employee Stock Ownership Plans (ESOPs) that have been endorsed by the Government of Tunisia Decentralization activities will give citizens a greater voice in local governance.

7. Issues

The primary issue concerns the continued resolve of the Government and the GOT bureaucracy to pass direct control of the economy to the private sector. Without such commitment the Project will not reach its intended objectives.

E. ECONOMIC ANALYSIS

There are strong grounds to believe that the PEP Project will have a major impact on the economy by increasing the productivity and efficiency of privatized firms. While the initial impact on employment may be negative, previous privatizations have proven that such losses are quickly recouped as improvements in international competitiveness result in expanded sales, output and jobs.

One privatization, even a relatively modest one, would probably justify the entire PEP Project by itself. To illustrate: Public enterprises still account for 25-34% of value added in the economy, or between TD 3-4 billion each year. Their annual investment alone has now reached TD 800 million per year. Estimates suggest 90% of direct public enterprise impact on the economy is accounted for by perhaps 100 firms, most of it by 40-50 firms. The PEP Project will look initially at perhaps 50 firms and in much greater depth at about 20-25 firms.

If 5% of public sector value added and investment is privatized (perhaps 3-10 larger firms), then the Project would result in the transfer to the private sector of TD 150-200 million per year in value added and TD 40 million per year in investment decisions. If efficiency were to increase by 10% as a result of private sector management, efficiency gains would total TD 15-20 million per year on operations and TD 4 million per year on investment decision making versus a total Project investment of approximately $12 million in privatization activities alone.

The Project's financial markets interventions aim to increase the availability of capital while reducing its real cost through technical assistance and training. Taken together with other reform efforts this will translate into an expansion of the private sector through privatization and other investment that will result in expanded income and employment opportunities. It is, however, difficult to estimate the economic returns to the proposed initiatives. Alternatively, one can compare the cost of the Project activities versus other methods of reaching the same objective, increasing capital and reducing its cost.

The classic alternative approach employed by AID has been the establishment of either direct lines of credit or lines of guaranty to financial intermediaries USAID/Tunisia currently employs both approaches, the former using PL480 local currency reflows and the latter with the assistance of the Bureau for Private Enterprise (PRE). Using the approximate figure of $3 million set aside under this Project for the Financial Markets Component, and assuming that a medium sized enterprise requires investment capital of $500,000 (either as a new venture or a privatization), AID would be able to assist only six firms with a direct line of credit to a bank. Employing the line of guaranty approach, and assuming that AID guaranties 50% of the loan as it does under PRE's loan guaranty program, then a total of twelve enterprises could be assisted. By comparison the Government of Tunisia has targeted a total of 75 public enterprises for privatization over the next five years. Looked at from the point of view of the total capital required for the privatization program, it dwarfs the $3 million that AID could provide in direct loans and the $6 million that AID could provide in guaranties.

F. ENVIRONMENTAL ANALYSIS

The Project will provide technical assistance and training for the privatization of State-owned industries, improvements in the efficiency of financial markets, and increased decentralization of public services and infrastructure. As the latter two activities focus on improvements in the management capabilities of financial institutions and municipalities, there will be no significant effects on Tunisia's natural environment. As for privatization activities, USAID will address environmental issues in an initial analysis performed on each State-owned enterprise proposed by the Government of Tunisia for Project assistance, as well as in the more detailed analyses to be done for each selected enterprise

Based on information provided in the Project Identification Document and additional information provided thereafter, the Near East Bureau Environmental Coordinator approved a categorical exclusion from additional environmental analysis based on 22 CFR Part 216.2(2)(c)(2)(ii).

VII. CONDITIONS PRECEDENT AND COVENANTS

A. CONDITIONS PRECEDENT

1. Conditions Precedent to First Disbursement

Except as A.I.D. may otherwise agree in writing, prior to disbursement under the grant or to the issuance by A.I.D. of documentation pursuant to which disbursement will be made, the Government of Tunisia will furnish to A.I D., in form and substance satisfactory to A.I.D.:

(a) A statement of the person holding or acting in the office of the Principal Representative of the Grantee specified in Section 8.2 of the Grant Agreement and of any additional representatives, together with a specimen signature of each person specified in such statement;

(b) A statement of the names of the persons managing the Privatization, Financial Markets, and Decentralization activities for the Grantee.

2. Conditions Precedent to Disbursement for U.S. Technical Assistance Contract

Except as A.I.D. may otherwise agree in writing, prior to disbursement under the grant or the issuance of documentation pursuant to which disbursement will be made to finance the U.S. technical assistance contract, the Government of Tunisia will furnish to A.I.D., in form and substance satisfactory to A.I.D.:

(a) Evidence that a Privatization Committee has been established to carry out the functions described in the Project Agreement, and that it includes participation by the Office of the Prime Minister, the Ministry of Finance, the Central Bank, the Ministry of National Economy, the Ministry of Plan and A.I.D.

(b) Evidence that a Financial Markets Committee has been established to carry out the functions described in the Project Agreement, and that it includes participation by the Central Bank, the Ministry of Finance, and selected members of the Privatization Committee, members of the private financial and business communities in a number at least equal to that of the GOT representatives, and A.I.D

3. Condition Precedent to Disbursement for Decentralization

Except as A.I.D. may otherwise agree in writing, prior to disbursement under the grant or the issuance of documentation pursuant to which disbursement will be made to finance any assistance for the Project's Decentralization activities, the Government of Tunisia will furnish to A.I.D., in form and substance satisfactory to A.I.D.:

a. Evidence that a Decentralization/Municipal Development Monitoring Committee has been established to carry out the functions described in the Project Agreement, and that it includes participation by the Ministry of the Interior, the Ministry of Plan and Regional Development, the Ministry of Finance, the Urban Rehabilitation and Renewal Agency, and the National Federation for Tunisian Cities.

B. COVENANTS

The GOT agrees that, over the life of the Project;

1. It will provide A.I.D. on at least a quarterly basis with information on the progress of the GOT's privatization program. Reports shall provide the names of the entities privatized, the names and nationalities of the purchasers, the value of the assets and shares transferred, the number of employees affected and their disposition, and the method of sale;

2. It will undertake an evaluation of the privatization program to date employing terms of reference acceptable to A.I.D.;

3. It will ensure that information on the progress of the GOT's privatization program will be made available to the general public on an on-going basis;

4. It will ensure that opportunities to purchase State-owned enterprises are widely publicized and that small businesses and individual investors are given adequate opportunity to purchase such enterprises

ANNEX 1
PID APPROVAL CABLE

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ACTION: AID INFO: AMB DCM ECON

664.346
Project Proc

VZCZCTUO954 23-JUL-91 TOR: 06:07
PP RUEHTU CN: 54505
DE RUEHC #9552/01 2031748 CHRG: AID
ZNR UUUUU ZZH DIST: AID
P 221744Z JUL 91 ADD:
FM SECSTATE WASHDC
TO AMEMBASSY TUNIS PRIORITY 6157
BT
UNCLAS SECTION 01 OF 02 STATE 239552

AIDAC

E.O. 12356: N/A
TAGS:
SUBJECT: TUNISIA: PRIVATE ENTERPRISE PROMOTION
(664-0346) GUIDANCE CABLE

1. SUMMARY: THE PROJECT REVIEW COMMITTEE (PRC) MET ON JULY 1, 1991 TO REVIEW SUBJECT PROJECT. THE MISSION WAS REPRESENTED BY PRIVATE SECTOR OFFICE RICHARD ROUSSEAU AND THE PRC WAS CHAIRED BY PDP DEPUTY DIRECTOR SATISH SHAH. THE DAA(NE)/ENE HEREBY APPROVES THE PID AND DELEGATES AUTHORITY TO THE MISSION TO DEVELOP AND APPROVE THE PROJECT PAPER FOR FY 92 OBLIGATION SUBJECT TO GUIDANCE ON ISSUES RAISED DURING THE PRC REVIEW. THE MAIN ISSUE RAISED WAS THE NEED TO NARROW THE PURPOSE AND DEFINE MORE CLEARLY THE LINKAGES BETWEEN THE FOUR PROJECT COMPONENTS. OTHER IMPORTANT ISSUES RAISED INCLUDED THE CYP FUNDING CONSTRAINT AND THE OPTIONS FOR SCALING DOWN THE PROJECT. THESE ISSUES WERE LATER DISCUSSED WITH MISSION DIRECTOR GEORGE CARNER. END SUMMARY.

ACTION 2220
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DIR
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C & R
CHRON RF

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2. PROJECT STRATEGY: THE PURPOSE STATEMENT IS VERY BROAD NAMELY TO PROMOTE PRIVATE SECTOR DEVELOPMENT AND COMPETITIVENESS. AS A CONSEQUENCE, THE PROJECT APPEARS TO LACK A CLEAR DEVELOPMENTAL OBJECTIVE. FOR EXAMPLE, THERE IS AN EXTENSIVE LISTING OF CONSTRAINTS TO PRIVATE SECTOR DEVELOPMENT AND A CORRESPONDING RANGE OF PROJECT ACTIVITIES ARRAYED UNDER FOUR PROJECT COMPONENTS. THE PRC RECOMMENDS NARROWING THE PURPOSE STATEMENT SO AS TO SHARPEN THE PROJECT FOCUS AND MORE CLEARLY DEFINE OBJECTIVES. THE PROJECT PURPOSE MIGHT BE NARROWED TO EMPHASIZE PRODUCTION EFFICIENCY/MARKETING OR IMPROVED INCENTIVE STRUCTURES AND MANAGEMENT PRACTICES ETC. WHICH IN TURN WILL INCREASE EMPLOYMENT OPPORTUNITIES, ENHANCE EXPORT-ORIENTED GROWTH IN SOME OBJECTIVELY MEASURABLE WAY. THIS WILL ALLOW LIMITED PROJECT RESOURCES TO BE CONCENTRATED IN AREAS OF HIGHEST POTENTIAL IMPACT. THE PRC RECOMMENDS THAT THE PROJECT PAPER ARTICULATE MORE CLEARLY THE LINKAGES BETWEEN THE PROJECT COMPONENTS. FOR INSTANCE, ILLUSTRATE HOW THE TRADE AND INVESTMENT COMPONENT INTERFACES WITH PRIVATIZATION. THIS APPROACH MIGHT HELP THE DESIGN TEAM SHARPEN THE FOCUS AND BETTER DEFINE THE RATIONALE FOR THE PROJECT COMPONENTS. THE PP

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SHOULD ALSO IDENTIFY THE PERFORMANCE INDICATORS THAT WOULD MEASURE IMPLEMENTATION PROGRESS AND RELATE THE PROJECT TO THE MISSION OVERALL PROGRAM OBJECTIVES.

4. OYB CONSTRAINTS: GIVEN THE OYB CONSTRAINTS OF DOLLARS THREE MILLION EST FOR FY 91 AND FY 92, THE PRC RECOMMENDS THAT CONSIDERATION BE GIVEN TO A MORE MODEST PROJECT BETTER IN LINE WITH CURRENT OYB, SAY LOP OF DOLLARS SIX TO NINE MILLION. ONE DESIGN OPTION WOULD BE TO FOCUS PROJECT ACTIVITIES ON PRIVATIZATION AND FINANCIAL MARKET DEVELOPMENT AND LEAVE OTHER PROJECT ACTIVITIES TO BE FUNDED UNDER OTHER PROJECTS SUCH AS THE DEVELOPMENT STUDIES PROJECT, IF THAT BECOMES NECESSARY. IF MORE FUNDING BECOMES AVAILABLE, THE PROJECT MAY BE AMENDED TO ADD NEW COMPONENTS OR INCREASE FUNDING FOR ACTIVITIES RETAINED IN THE SCALED-DOWN VERSION OF THE PROJECT. THE PRC BELIEVES THE MISSION IS IN THE BEST POSITION TO DETERMINE A REALISTIC DESIGN APPROACH TO ADDRESS THIS PROBLEM.

5. TRADE AND INVESTMENT: ASSUMING THAT THE PROJECT WILL BE DOWNSIZED, THE DESIGN TEAM NEEDS TO FOCUS ON AREAS THAT PRESENT SOME REAL OPPORTUNITIES FOR TRADE. WHAT MARKET CAN BE IDENTIFIED THAT GIVES TUNISIA A QUOTE COMPETITIVE ADVANTAGE UNQUOTE. HOW CAN THIS COMPONENT HELP BUILD THE COMPETITIVE ADVANTAGE SO THAT TUNISIA MAY

COMPETE IN THE EC OR U.S. MARKET. ALSO, WHAT IS THE ROLE OF PRIVATE INTERMEDIARIES (PRIVATE SERVICE SUPPLIERS). HOW WILL THEIR SERVICES BE UTILIZED IN THIS COMPONENT. THIS COMPONENT SHOULD SUPPORT THE BUSINESS COMMUNITY IN GETTING TOGETHER WITH GOT OFFICIALS TO ENGAGE IN POLICY DIALOGUE AIMED AT IMPROVING INTERNATIONAL COMPETITIVENESS.

6. URBANIZATION: THE PP SHOULD SHOW HOW THIS COMPONENT WOULD INCREASE EMPLOYMENT OR EXPORT-ORIENTED GROWTH THROUGH INVOLVEMENT OF THE PRIVATE SECTOR AND THE DEVELOPMENT OF THE MUNICIPAL FINANCE SECTOR. IN THE CONTEXT OF LEVERAGING GREATER URBAN INVESTMENT THE FINANCIAL SYSTEM SHOULD BE REVIEWED HOLISTICALLY IN ORDER TO IDENTIFY THE APPROPRIATE FINANCIAL NICHE FOR MUNICIPAL INFRASTRUCTURE FINANCE. THIS WILL HELP AVOID A SITUATION WHICH COULD LEAD TO FINANCIAL QUOTE CROWDING OUT UNQUOTE OF PRIVATE BORROWERS FOR DIRECTLY PRODUCTIVE ACTIVITIES. THIS ACTIVITY MIGHT FOCUS ON INNOVATIVE FINANCIAL INSTRUMENTS TO ENCOURAGE GREATER SAVINGS AND, AT THE SAME TIME, CAPTURE A PORTION OF THOSE INCREASED SAVINGS FOR INFRASTRUCTURE DEVELOPMENT NEEDED BY THE

PRIVATE SECTOR. THIS WILL ENTAIL AMONG OTHER THINGS A CAREFUL REVIEW OF THE WAY IN WHICH MUNICIPALITIES OBTAIN LONG TERM FINANCING. AT A SUBSEQUENT MEETING THE MISSION DIRECTOR AGREED THAT THE URBAN COMPONENT WOULD BE BETTER RECAST AS A SEPARATE PROJECT LINKED DIRECTLY TO A HG LOAN. GIVEN CURRENT FUNDING LEVELS IN TUNISIA, THE MISSION DIRECTOR AGREED THAT AT LEAST DOLLARS 300,000 SHOULD BE MADE AVAILABLE UNDER THIS PROJECT TO SUPPORT THE MISSION'S MUNICIPAL COMPONENT OF ITS ASSISTANCE MANAGEMENT PLAN.

7. IN ADDITION TO THE ABOVE ISSUES THE FOLLOWING CONCERNS WERE RAISED FOR MISSION CONSIDERATION:

A) THE PROJECT SHOULD LOOK AT VARIOUS TYPES OF PRIVATIZATION ACTIVITIES CONSISTENT WITH NEW AGENCY GUIDANCE UNDER PI 14. PARTIAL OR GRADUAL PRIVATIZATION OVER TIME MAY BE MORE FEASIBLE TO IMPLEMENT IN THE HOST COUNTRY SETTING AND SHOULD BE SUPPORTED IF IT CLEARLY LEADS TO MORE EFFICIENT MANAGEMENT OF THE FIRMS CONCERNED.

B). GENDER ISSUES SHOULD BE DISCUSSED WITHIN THE CONTEXT OF HOW THE PROJECT WILL CONTRIBUTE TO

REDUCING THE SEVERE UNEMPLOYMENT PROBLEM OF TUNISIA. IN THE MISSION'S AMP ANALYSIS, THE CHRONIC UNEMPLOYMENT FOR MEN WAS ESTIMATED AT A STEADY 15 PERCENT WHILE FOR WOMEN IT WAS RISING ABOVE 20 PERCENT. THUS, WOMEN STAND TO GAIN A GREAT DEAL FROM A PRIVATE SECTOR PROMOTION PROJECT BOTH AS ENTREPRENEURS AND AS EMPLOYEES DEPENDING ON THE CHOICE OF INDUSTRIES TO BE SUPPORTED. CONSTRAINTS AND OPPORTUNITIES FOR EMPLOYMENT GENERATION FOR WOMEN SHOULD BE EXPLICITLY DISCUSSED IN THE ANALYSIS OF BENEFICIARIES FOR THE PROJECT PAPER.

C). THE PP SHOULD LOOK AT GUIDANCE RELATING TO THE GRAY AMENDMENT AND PARTICIPANT TRAINING AT HBCU'S AND DEMONSTRATE HOW IT WILL DEAL WITH THESE REQUIREMENTS.

8. INITIAL ENVIRONMENTAL EXAMINATION: IN LIGHT OF SUPPLEMENTAL INFORMATION PROVIDED BY THE MISSION, THE BUREAU HAS PREPARED A MEMORANDUM RECOMMENDING A CATEGORICAL EXCLUSION BASED ON 22 CFR PART 216.2(2)(I). WE WILL ADVISE THE MISSION SEPTEL ON OTHER ENVIRONMENTAL RECOMMENDATIONS.

9. BASED ON THE PRC RECOMMENDATION, THE DAA (NE)/ENE HEREBY APPROVES THE PID AND DELEGATES TO THE MISSION PP APPROVAL AUTHORITY PURSUANT TO GUIDANCE PROVIDED ABOVE. AID/W REQUESTS MISSION TO SUBMIT A REPORTING CABLE ON THE REVISED PROJECT SUMMARY OUTLINING REFORMULATED ELEMENTS OF THE PROJECT PRIOR TO AUTHORIZATION. EAGLEBURGER
BT
#9552

ANNEX 2
GOVERNMENT OF TUNISIA REQUEST FOR ASSISTANCE

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REPUBLIQUE TUNISIENNE

MINISTERE
DES AFFAIRES ETRANGERES

TUNIS le 3 1 ...

N° 2284

DGAA/DIR AMERIQUES
Z B/R H

MONSIEUR JAMES A GRAHAM
DIRECTEUR DE LA MISSION SPECIALE
AMERICAINE DE COOPERATION
ECONOMIQUE ET TECHNIQUE
EN TUNISIE

OBJET Projet "Private Entreprise Promotion" (P E P)

Monsieur le Directeur,

Me réferant aux negociations tuniso-americaines sur le projet de coopération technique "Private Entreprise Promotion", j'ai l'honneur de vous confirmer l'accord des autorités tunisiennes au sujet de votre proposition relative à l'affectation de 10 millions de dollars à partir du Fonds de Soutien Economique (E S E) pour le financement de ce projet

Je vous remercie pour votre aimable coopération et vous prie d'agreer Monsieur le Directeur les assurances de ma considération distinguée

Le Directeur ...

Azouz ENNIFAR

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ANNEX 3
LOGFRAME

LOGICAL FRAMEWORK
PRIVATE ENTERPRISE PROMOTION (PEP) PROJECT
PROJECT NUMBER (664-0346)

NARRATIVE	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	ASSUMPTIONS
GOAL: *To support the continued emergence of a market-driven, competitive economy*	1. Public/private sector participation in the economy reverses from 60/40 to 40/60 2. Private sector investment increases by 9% 3. Employment and investment expansion	• Industrial value added figures Employment figures • Investment Figures	*Concerning long term value of project* 1. Traditional European markets remain open to Tunisian products 2. Tunisian industry raises quality productivity & increases added value 3. Tunisian industry diversifies mrkts
PURPOSE: *To expand private sector employment and income by privatizing state-owned enterprises, decentralizing government functions, and improving the efficiency of financial markets*	*End of Project Status* 1. Twenty state-owned firms privatized 2. Private sector invests approx. US$100 Million to acquire and upgrade former state-owned enterprises 3. Approx. 3 municipalities are managing 25% or more of their infrastructure investment and using private sector operators to provide basic muni. services	• Government statistics Stock Exchange records	*Affecting purpose-to-goal link* 1. GOT continues to implement the SAP 2. GOT continues to disengage from public enterprises 3. Tunisian firms adopt modern business methods & technologies 4. Quality & productivity increases
OUTPUTS *Privatization* 1. Privatization Program transparency increased 2. Privatization implementation process improved and strengthened 3. "Critical Mass" of Public enterprises offered for public sale or ESOPs	*Magnitude of Outputs necessary & sufficient to achieve purpose* a. 4 seminars and 3 observ. trips conducted in Yrs 1 & 2 of Project b. 6 case studies on previous privatizations developed & publicized (Years 1 & 2) c. Feedback mechanism generating recommendations to improve privatizations d. Response times on public offerings at least 6 weeks long e. 30 strategic analyses of PEs conducted conducted f. 23 PEs readied for privatization	• Minutes of Committee meetings • Contractor reports AND • Studies • Seminar proceedings • Trip reports • Minutes of Committee meetings • Contractor reports • Copies of valuations, marketing strategies, etc.	*Affecting output-to-purpose link* 1. Financial markets increase flow of capital to private investors 2. The private sector invests in shares in privatized firms 3. Foreign investors acquire shares in privatized firms 4. Municipalities use financial mechanism and contract with private sector to provide public services
Financial Markets 1. Reliable financial information increasingly available 2. New financial instruments introduced to channel domestic savings into productive investments 3. Financial intermediaries strengthened 4. More responsiveness to private sector financing needs	g. 4 financial mkt policy studies conducted h. 5 TA missions with financial institutions	• Financial Mkts reforms implemented by GOT to revitalize financial markets • New financial products introduced • More competition within the financial sector	1. Continuous stream of new issues 2. Active secondary market 3. Development of bond markets
Decentralization 1. Financial mechanism for infrastructure upgrading that is accessible by municipalities is established	a. loan applications being received and processed b. 3 municipalities trained to use the financial mechanism		
INPUTS: Activities & Types of resources 1. Hire local Tunisian accounting firms 2. Contract with Institutional Contractor for technical assistance – Strengthen analysis techniques a. Design feedback mechanism b. Develop data base on past priv c. Develop SOW for analyzing PEs – Develop IE&C Program a. Organize seminars b. Organize observation trips c. Develop case studies – Conduct studies – Deliver technical assistance – Conduct Analyses/studies – Prepare Privatization Deals 3. Hire local contractor for RHUDO work 4. Execute IQCs for RHUDO work	<u>Level of Effort</u> 334 ST US/Tu.pm 9100 8 (buy-in) US.pm 283 12 (buy-in) TU.pm 160 Decentralization buy-in 400 Evaluation 120 TOTAL $10,000,000	1. Contractor quarterly reports 2. Project manager records 3. Controller Office reports	*Affecting input-to-output link* • Tun. actg/fin firms participate in teams with US experts • Project Committees convened NLT 9/92 • Project Committees agree on first set of Privatizations NLT 1/93 • Privatization SOW requires process transparency financial packaging & mrktg designed to broaden ownership • A seminar to explain the process of privatization to the general public is held NLT December 1993 • Financial intermediaries request T.A. • That there are 20 PEs that qualify as "going concerns" i.e., are candidates for privatization, not liquidation • The newly created Municipal Develop. Authority assumes its responsibilities • World Bank Municipal Program Loan begins disbursing NLT 12/93

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ANNEX 4
STATUTORY CHECKLIST

5C(2) - ASSISTANCE CHECKLIST

Listed below are statutory criteria applicable to the assistance resources themselves, rather than to the eligibility of a country to receive assistance. This section is divided into three parts. Part A includes criteria applicable to both Development Assistance and Economic Support Fund resources. Part B includes criteria applicable only to Development Assistance resources. Part C includes criteria applicable only to Economic Support Funds.

CROSS REFERENCE: IS COUNTRY CHECKLIST UP TO DATE? — Yes

A. CRITERIA APPLICABLE TO BOTH DEVELOPMENT ASSISTANCE AND ECONOMIC SUPPORT FUNDS

1. Host Country Development Efforts (FAA Sec. 601(a)): Information and conclusions on whether assistance will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.

The project will assi the on-going reform o private sector policy environment and will result in the privatization of stat owned enterprises Th will encourage a,b,d, e.

2. U.S. Private Trade and Investment (FAA Sec. 601(b)): Information and conclusions on how assistance will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

The project will enc the development of t and investment betwe U.S. and Tunisia by expanding the number types of private enterprises

3. Congressional Notification

a. General requirement (FY 1991 Appropriations Act Secs. 523 and 591; FAA Sec. 634A): If money is to be obligated for an activity not previously justified to Congress, or for an amount in excess of amount previously justified to Congress, has Congress been properly notified (unless the notification requirement has been waived because of substantial risk to human health or welfare)?

Congress was notifiec on page 654 or the F C P

b. Notice of new account obligation (FY 1991 Appropriations Act Sec. 514): If funds are being obligated under an appropriation account to which they were not appropriated, has the President consulted with and provided a written justification to the House and Senate Appropriations Committees and has such obligation been subject to regular notification procedures?

N/A

c. Cash transfers and nonproject sector assistance (FY 1991 Appropriations Act Sec. 575(b)(3)): If funds are to be made available in the form of cash transfer or nonproject sector assistance, has the Congressional notice included a detailed description of how the funds will be used, with a discussion of U.S. interests to be served and a description of any economic poolicy reforms to be promoted?

N/A

4. Engineering and Financial Plans (FAA Sec. 611(a)): Prior to an obligation in excess of $500,000, will there be: (a) engineering, financial or other plans necessary to carry out the assistance; and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?

Yes

5. Legislative Action (FAA Sec. 611(a)(2)): If legislative action is required within recipient country with respect to an obligation in excess of $500,000, what is the basis for a reasonable expectation that such action

No legislative actior is required

will be completed in time to permit orderly accomplishment of the purpose of the assistance?

6. Water Resources (FAA Sec. 611(b); FY 1991 Appropriations Act Sec. 501): If project is for water or water-related land resource construction, have benefits and costs been computed to the extent practicable in accordance with the principles, standards, and procedures established pursuant to the Water Resources Planning Act (42 U.S.C. 1962, et seq.)? (See A.I.D. Handbook 3 for guidelines.)

N/A

7. Cash Transfer and Sector Assistance (FY 1991 Appropriations Act Sec. 575(b)): Will cash transfer or nonproject sector assistance be maintained in a separate account and not commingled with other funds (unless such requirements are waived by Congressional notice for nonproject sector assistance)?

N/A

8. Capital Assistance (FAA Sec. 611(e)): If project is capital assistance (e.g., construction), and total U.S. assistance for it will exceed $1 million, has Mission Director certified and Regional Assistant Administrator taken into consideration the country's capability to maintain and utilize the project effectively?

N/A

9. Multiple Country Objectives (FAA Sec. 601(a)): Information and conclusions on whether projects will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture and commerce; and (f) strengthen free labor unions.

The project will as in the ongoing refo of the private sect policy environment will result in the privatization of st owned enterprises This will encourage a,b, d, and e.

10. U.S. Private Trade (FAA Sec. 601(b)): Information and conclusions on how project will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).	The project will encoura the development of trade investment between the and Tunisia by expanding the number and types of private enterprises
11. Local Currencies	
a. Recipient Contributions (FAA Secs. 612(b), 636(h)): Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the U.S. are utilized in lieu of dollars.	The Government of Tunisi the Tunisian private sec will contribute approxim 40% of the total costs o project
b. U.S.-Owned Currency (FAA Sec. 612(d)): Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release?	The US does not own exce foreign currency of Tuni
c. Separate Account (FY 1991 Appropriations Act Sec. 575). If assistance is furnished to a foreign government under arrangements which result in the generation of local currencies:	N/A
(1) Has A.I.D. (a) required that local currencies be deposited in a separate account established by the recipient government, (b) entered into an agreement with that government providing the amount of local currencies to be generated and the terms and conditions under which the currencies so deposited may be utilized, and (c) established by agreement the responsibilities of A.I.D. and that government to monitor and account for deposits into and disbursements from the separate account?	

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(2) Will such local currencies, or an equivalent amount of local currencies, be used only to carry out the purposes of the DA or ESF chapters of the FAA (depending on which chapter is the source of the assistance) or for the administrative requirements of the United States Government?

(3) Has A.I.D. taken all appropriate steps to ensure that the equivalent of local currencies disbursed from the separate account are used for the agreed purposes?

(4) If assistance is terminated to a country, will any unencumbered balances of funds remaining in a separate account be disposed of for purposes agreed to by the recipient government and the United States Government?

12. **Trade Restrictions**

a. **Surplus Commodities** (FY 1991 Appropriations Act Sec. 521(a)): If assistance is for the production of any commodity for export, is the commodity likely to be in surplus on world markets at the time the resulting productive capacity becomes operative, and is such assistance likely to cause substantial injury to U.S. producers of the same, similar or competing commodity? N/A

b. **Textiles (Lautenberg Amendment)** (FY 1991 Appropriations Act Sec. 521(c)): Will the assistance (except for programs in Caribbean Basin Initiative countries under U.S. Tariff Schedule "Section 807," which allows reduced tariffs on articles assembled abroad from U.S.-made components) be used directly to procure feasibility studies, prefeasibility studies, or project profiles of potential investment in, or to assist the establishment of facilities specifically designed for, the manufacture for export to the United States or to third country markets in direct competition with U.S. exports, of No textiles, apparel, footwear, handbags, flat goods (such as wallets or coin purses worn on the person), work gloves or leather wearing apparel?

13. Tropical Forests (FY 1991 Appropriations Act Sec. 533(c)(3)): Will funds be used for any program, project or activity which would (a) result in any significant loss of tropical forests, or (b) involve industrial timber extraction in primary tropical forest areas? No

14. PVO Assistance N/A

a. Auditing and registration (FY 1991 Appropriations Act Sec. 537): If assistance is being made available to a PVO, has that organization provided upon timely request any document, file, or record necessary to the auditing requirements of A.I.D., and is the PVO registered with A.I.D.?

b. Funding sources (FY 1991 Appropriations Act, Title II, under heading "Private and Voluntary Organizations"): If assistance is to be made to a United States PVO (other than a cooperative development organization), does it obtain at least 20 percent of its total annual funding for international activities from sources other than the United States Government?

15. Project Agreement Documentation (State Authorization Sec. 139 (as interpreted by conference report)): Has confirmation of the date of signing of the project agreement, including the amount involved, been cabled to State L/T and A.I.D. LEG within 60 days of the agreement's entry into force with respect to the United States, and has the full text of the agreement been pouched to those same offices? (See Handbook 3, Appendix 6G for agreements covered by this provision). Case-Zablocki Act provisions wi complied with

16. **Metric System** (Omnibus Trade and Competitiveness Act of 1988 Sec. 5164, as interpreted by conference report, amending Metric Conversion Act of 1975 Sec. 2, and as implemented through A.I.D. policy): Does the assistance activity use the metric system of measurement in its procurements, grants, and other business-related activities, except to the extent that such use is impractical or is likely to cause significant inefficiencies or loss of markets to United States firms? Are bulk purchases usually to be made in metric, and are components, subassemblies, and semi-fabricated materials to be specified in metric units when economically available and technically adequate? Will A.I.D. specifications use metric units of measure from the earliest programmatic stages, and from the earliest documentation of the assistance processes (for example, project papers) involving quantifiable measurements (length, area, volume, capacity, mass and weight), through the implementation stage?

Yes

Yes

Yes

17. **Women in Development** (FY 1991 Appropriations Act, Title II, under heading "Women in Development"): Will assistance be designed so that the percentage of women participants will be demonstrably increased?

Yes

18. **Regional and Multilateral Assistance** (FAA Sec. 209): Is assistance more efficiently and effectively provided through regional or multilateral organizations? If so, why is assistance not so provided? Information and conclusions on whether assistance will encourage developing countries to cooperate in regional development programs.

No

Assistance will
directly encour
regional cooper

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19 Abortions (FY 1991 Appropriations Act, Title II, under heading "Population, DA," and Sec. 525):

a Will assistance be made available to any organization or program which, as determined by the President, supports or participates in the management of a program of coercive abortion or involuntary sterilization?

No

b. Will any funds be used to lobby for abortion?

No

20. Cooperatives (FAA Sec. 111): Will assistance help develop cooperatives, especially by technical assistance, to assist rural and urban poor to help themselves toward a better life?

No

21. U.S.-Owned Foreign Currencies

a. Use of currencies (FAA Secs. 612(b), 636(h); FY 1991 Appropriations Act Secs. 507, 509): Describe steps taken to assure that, to the maximum extent possible, foreign currencies owned by the U.S. are utilized in lieu of dollars to meet the cost of contractual and other services.

The US does not own excess foreign curren of Tunisia.

b. Release of currencies (FAA Sec. 612(d)): Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release?

The US does not own e foreign currency of T

22. Procurement

a. Small business (FAA Sec. 602(a)): Are there arrangements to permit U.S. small business to participate equitably in the furnishing of commodities and services financed?

Yes

b. U.S. procurement (FAA Sec. 604(a)): Will all procurement be from the U.S. except as otherwise determined by the President or determined under delegation from him?

Yes

c. Marine insurance (FAA Sec. 604(d)): If the cooperating country discriminates against marine insurance companies authorized to do business in the U.S., will commodities be insured in the United States against marine risk with such a company? N/A

d. Non-U.S. agricultural procurement (FAA Sec. 604(e)): If non-U.S. procurement of agricultural commodity or product thereof is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity? (Exception where commodity financed could not reasonably be procured in U.S.) N/A

e. Construction or engineering services (FAA Sec. 604(g)): Will construction or engineering services be procured from firms of advanced developing countries which are otherwise eligible under Code 941 and which have attained a competitive capability in international markets in one of these areas? (Exception for those countries which receive direct economic assistance under the FAA and permit United States firms to compete for construction or engineering services financed from assistance programs of these countries.) No

f. Cargo preference shipping (FAA Sec. 603)): Is the shipping excluded from compliance with the requirement in section 901(b) of the Merchant Marine Act of 1936, as amended, that at least 50 percent of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed shall be transported on privately owned U.S. flag commercial vessels to the extent such vessels are available at fair and reasonable rates? No

g. Technical assistance (FAA Sec. 621(a)): If technical assistance is financed, will such assistance be furnished by private enterprise on a contract basis to the fullest extent practicable? Will the Yes facilities and resources of other Federal agencies be utilized, when they are particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs?

The use of other Federal agencies is not contemp.a'

h. **U.S. air carriers** (International Air Transportation Fair Competitive Practices Act, 1974): If air transportation of persons or property is financed on grant basis, will U.S. carriers be used to the extent such service is available?

Yes

i. **Termination for convenience of U.S. Government** (FY 1991 Appropriations Act Sec. 504): If the U.S. Government is a party to a contract for procurement, does the contract contain a provision authorizing termination of such contract for the convenience of the United States?

Yes

j. **Consulting services** (FY 1991 Appropriations Act Sec. 524): If assistance is for consulting service through procurement contract pursuant to 5 U.S.C. 3109, are contract expenditures a matter of public record and available for public inspection (unless otherwise provided by law or Executive order)?

Yes

k. **Metric conversion** (Omnibus Trade and Competitiveness Act of 1988, as interpreted by conference report, amending Metric Conversion Act of 1975 Sec. 2, and as implemented through A.I.D. policy): Does the assistance program use the metric system of measurement in its procurements, grants, and other business-related activities, except to the extent that such use is impractical or is likely to cause significant inefficiencies or loss of markets to United States firms?

Yes

Are bulk purchases usually to be made in metric, and are components, subassemblies, and semi-fabricated materials to be specified in metric units when economically available and technically adequate?

Yes

Will A.I.D. specifications use metric units of measure from the earliest programmatic stages, and from the earliest

Yes

documentation of the assistance processes (for example, project papers) involving quantifiable measurements (length, area, volume, capacity, mass and weight), through the implementation stage?

1. Competitive Selection Procedures (FAA Sec. 601(e)): Will the assistance utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise? — Yes

23. Construction

a. Capital project (FAA Sec. 601(d)): If capital (e.g., construction) project, will U.S. engineering and professional services be used? — N/A

b. Construction contract (FAA Sec. 611(c)): If contracts for construction are to be financed, will they be let on a competitive basis to maximum extent practicable? — N/A

c. Large projects, Congressional approval (FAA Sec. 620(k)): If for construction of productive enterprise, will aggregate value of assistance to be furnished by the U.S. not exceed $100 million (except for productive enterprises in Egypt that were described in the Congressional Presentation), or does assistance have the express approval of Congress? — N/A

24. U.S. Audit Rights (FAA Sec. 301(d)): If fund is established solely by U.S. contributions and administered by an international organization, does Comptroller General have audit rights? — N/A

25. Communist Assistance (FAA Sec. 620(h). Do arrangements exist to insure that United States foreign aid is not used in a manner which, contrary to the best interests of the United States, promotes or assists the foreign aid projects or activities of the Communist-bloc countries? — Yes

26. **Narcotics**

a. **Cash reimbursements** (FAA Sec. 483): Will arrangements preclude use of financing to make reimbursements, in the form of cash payments, to persons whose illicit drug crops are eradicated? — Yes

b. **Assistance to narcotics traffickers** (FAA Sec. 487): Will arrangements take "all reasonable steps" to preclude use of financing to or through individuals or entities which we know or have reason to believe have either: (1) been convicted of a violation of any law or regulation of the United States or a foreign country relating to narcotics (or other controlled substances); or (2) been an illicit trafficker in, or otherwise involved in the illicit trafficking of, any such controlled substance? — Yes

27. **Expropriation and Land Reform** (FAA Sec. 620(g)): Will assistance preclude use of financing to compensate owners for expropriated or nationalized property, except to compensate foreign nationals in accordance with a land reform program certified by the President? — Yes

28. **Police and Prisons** (FAA Sec. 660): Will assistance preclude use of financing to provide training, advice, or any financial support for police, prisons, or other law enforcement forces, except for narcotics programs? — Yes

29. **CIA Activities** (FAA Sec. 662): Will assistance preclude use of financing for CIA activities? — Yes

30. **Motor Vehicles** (FAA Sec. 636(i)): Will assistance preclude use of financing for purchase, sale, long-term lease, exchange or guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained? — Yes

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31. **Military Personnel** (FY 1991 Appropriations Act Sec. 503): Will assistance preclude use of financing to pay pensions, annuities, retirement pay, or adjusted service compensation for prior or current military personnel? — Yes

32. **Payment of U.N. Assessments** (FY 1991 Appropriations Act Sec. 505): Will assistance preclude use of financing to pay U.N. assessments, arrearages or dues? — Yes

33. **Multilateral Organization Lending** (FY 1991 Appropriations Act Sec. 506): Will assistance preclude use of financing to carry out provisions of FAA section 209(d) (transfer of FAA funds to multilateral organizations for lending)? — Yes

34. **Export of Nuclear Resources** (FY 1991 Appropriations Act Sec. 510): Will assistance preclude use of financing to finance the export of nuclear equipment, fuel, or technology? — Yes

35. **Repression of Population** (FY 1991 Appropriations Act Sec. 511): Will assistance preclude use of financing for the purpose of aiding the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the Universal Declaration of Human Rights? — Yes

36. **Publicity or Propoganda** (FY 1991 Appropriations Act Sec. 516): Will assistance be used for publicity or propaganda purposes designed to support or defeat legislation pending before Congress, to influence in any way the outcome of a political election in the United States, or for any publicity or propaganda purposes not authorized by Congress? — No

ANNEX 7 5
PRIVATE ENTERPRISE PROMOTION PROJECT
DETAILED BUDGET BY FISCAL YEAR
(U S DOLLARS)

	1993	1994	1995	1996	1997	TOTAL
II DECENTRALIZATION						
A COUNTERPART SALARIES/STUDIES	50,000	50,000	0	0	0	100,000
TOTAL GOT CONTRIBUTION	830,000	952,222	902 222	902,222	902,222	4,488,889
PRIVATE SECTOR CONTRIBUTION						
I PRIVATIZATION/FINANCIAL MARKETS						
A IFI'S						
1 0 COST SHARE (INC AIR FARES)	155,401	320,126	329,730	339,622	196,009	1,340,887
TOTAL P S CONTRIBUTION	155,401	320,126	329,730	339,622	196,009	1,340,887

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ANNEX 7 5
PRIVATE ENTERPRISE PROMOTION PROJECT
DETAILED BUDGET BY FISCAL YEAR
(U S DOLLARS)

	1993	1994	1995	1996	1997	TOTAL
II DECENTRALIZATION						
A LOCAL PSC	24,600	26,322	0	0	0	50,922
B STUDIES	150,660	198,889	0	0	0	349,550
1 0 FOREIGN COSTS	54,660	91,769	0	0	0	146,430
1 1 LOCAL COSTS	96,000	107,120	0	0	0	203,120
DECENTRALIZATION FOREIGN	54,660	91,769	0	0	0	146,430
DECENTRALIZATION LOCAL	120,600	133,442	0	0	0	254,042
TOTAL DECENTRALIZATION	175,260	225,211	0	0	0	400,472
III EVALUATION						
1 0 FOREIGN COSTS	0	0	57,989	0	61,521	119,510
TOTAL AID FOREIGN COSTS	778,446	1,563,267	1,498,246	1,376,495	1,171,707	6,388,161
TOTAL AID LOCAL COSTS	587,063	813,700	727,876	716,521	766,678	3,611,839
TOTAL AID	1,365,509	2,376,967	2,226,122	2,093,017	1,938,385	10,000,000
GOT CONTRIBUTION						
I PRIVATIZATION/FINANCIAL MARKETS						
A PRIVATIZATION PROGRAM MANAGEMENT						
1 0 SALARIES	166,667	166,667	166,667	166,667	166,667	833,333
2 0 PREPARATORY WORK						
- APUREMENT	66,667	83,333	83,333	83,333	83,333	400,000
- INVENTORIES	44,444	50,000	50,000	50,000	50,000	244,444
3 0 LOGISTICS						
- REPORT PREPARATION	50,000	50,000	50,000	50,000	50,000	250,000
- TRANSPORT ETC	22,222	22,222	22,222	22,222	22,222	111,111
SUBTOTAL	350,000	372,222	372,222	372,222	372,222	1,838,889
B BROKERS FEES	400,000	500,000	500,000	500,000	500,000	2,400,000
TOTAL	750,000	872,222	872,222	872,222	872,222	4,238,889
C FINANCIAL MKTS COUNTERPARTS						
1 0 SALARIES	30,000	30,000	30,000	30,000	30,000	150,000
SUBTOTAL GOT FOR PRIV /FM	780,000	902,222	902,222	902,222	902,222	4,388,889

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ANNEX 7 5
PRIVATE ENTERPRISE PROMOTION PROJECT
DETAILED BUDGET BY FISCAL YEAR
(U S DOLLARS)

	1993	1994	1995	1996	1997	TOTAL
3 0 CONTRACTOR MANAGEMENT						
3 1 U S ADVISOR	54,660	84,450	86,984	89,593	92,281	407,969
3 2 LOCAL ADVISOR	95,908	205,244	219,611	234,983	251,432	1,007,178
3 3 HOME OFFICE SUPPORT	32,000	49,440	50,923	52,451	54,024	238,839
SUBTOAL CONTRACTOR MGT FOREIGN	86,660	133,890	137,907	142,044	146,306	646,808
SUBTOAL CONTRACTOR MGT LOCAL	95,908	205,244	219,611	234,983	251,432	1,007,178
SUBTOAL CONTRACTOR MGT	182,569	339,134	357,518	377,028	397,738	1,653,986
CONTRACTOR FOREIGN	520,333	1,471,498	1,440,257	1,376,495	1,110,186	5,918,769
CONTRACTOR LOCAL	306,616	680,258	727,876	716,521	766,678	3,197,950
TOTAL CONTRACTOR	826,948	2,151,756	2,168,133	2,093,017	1,876,864	9,116,718
TOTAL AID PRIV & FM FOREIGN	723,786	1,471,498	1,440,257	1,376,495	1,110,186	6,122,221
TOTAL AID PRIV & FM LOCAL	466,463	680,258	727,876	716,521	766,678	3,357,797
TOTAL AID PRIV & FM	1,190,248	2,151,756	2,168,133	2,093,017	1,876,864	9,480,018

ANNEX 7 5
PRIVATE ENTERPRISE PROMOTION PROJECT
DETAILED BUDGET BY FISCAL YEAR
(U S DOLLARS)

	1993	1994	1995	1996	1997	TOTAL
AID CONTRIBUTION						
1 PRIVATIZATION/FINANCIAL MARKETS						
A VALUATIONS (LOCAL CONTRACTS)	159,847	0	0	0	0	159,847
B FINANCIAL STUDIES (BUY INS)	203,453	0	0	0	0	203,453
C U S CONTRACTOR	826,948	2,151,756	2,168,133	2,093,017	1,876,864	9,116,718
1 0 PRIVATIZATION						
1 1 DIAGNOSTICS	137,820	215,984	225,729	78,665	82,271	740,468
FOREIGN COSTS	86,960	134,353	138,383	47,512	48,937	456,145
LOCAL COSTS	50,860	81,631	87,345	31,153	33,334	284,324
1 2 TRANSACTIONS	259,889	678,806	709,433	741,696	775,696	3,165,521
FOREIGN COSTS	163,981	422,252	434,919	447,967	461,406	1,930,525
LOCAL COSTS	95,908	256,555	274,513	293,729	314,290	1,234,996
1 3 IE&C	0	135,761	66,501	58,746	62,858	323,866
FOREIGN COSTS	0	84,450	11,598	0	0	96,048
LOCAL COSTS	0	51,311	54,903	58,746	62,858	227,818
1 4 FOLLOW-UP	47,954	51,311	54,903	58,746	62,858	275,772
FOREIGN COSTS	0	0	0	0	0	0
LOCAL COSTS	47,954	51,311	54,903	58,746	62,858	275,772
SUBTOTAL PRIV FOREIGN	250,941	641,055	584,901	495,478	510,343	2,482,718
SUBTOTAL PRIV LOCAL	194,723	440,807	471,664	442,374	473,340	2 022,909
SUBTOTAL PRIV	445,664	1,081,862	1,056,564	937,853	983,683	4,505,626
2 0 FINANCIAL MARKETS						
2 1 STUDIES	43,315	90,508	94,591	98,893	103,426	430,732
FOREIGN COSTS	27,330	56,300	57,989	59,729	61,521	262,869
LOCAL COSTS	15,985	34,207	36,602	39,164	41,905	167,863
2 2 U S TA TO IFI'S	273,302	563,002	579,892	597,289	307,604	2,321,090
LESS IFI'S CONTRIBUTIONS	136,651	281,501	289,946	298,645	153,802	1,160,545
NET AID CONTRIBUTION	136,651	281,501	289,946	298,645	153,802	1,160,545
2 3 U S TRAINING FOR IFI'S	37,500	77,250	79,568	81,955	84,413	360,685
LESS IFI'S CONTRIBUTIONS	18,750	38,625	39,784	40,977	42,207	180,343
NET AID CONTRIBUTION	18,750	38,625	39,784	40,977	42,207	180,343
SUBTOTAL FM FOREIGN	182,731	696,553	717,449	738,973	453,538	2,789,243
SUBTOTAL FM LOCAL	15,985	34,207	36,602	39,164	41,905	167,863
SUBTOTAL FM	198,716	730,760	754,051	778,136	495,443	2,957,106

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ANNEX 7 4
PRIVATE ENTERPRISE PROMOTION PROJECT
PRICES PER UNIT

	INFLAT INDEX	COST PER	1993	1994	1995	1996	1997
RATE OF EXCHANGE (TD/$)			0 900	0 900	0 900	0 900	0 900
FOREIGN COST FACTORS							
FOREIGN CONSULTANT	103%	PM	27,330	28,150	28,995	29,864	30,760
HOME OFFICE SUPPORT	103%	PM	16,000	16,480	16,974	17,484	18,008
U S TRAINING	103%	PM	7,500	7,725	7,957	8,195	8,441
LOCAL COST FACTORS							
LOCAL CONSULTANT	107%	PM	15,985	17,104	18,301	19,582	20,953
LOCAL PSC	107%	PM	2,050	2,194	2,347	2,511	2,687
AIR FARES		RT	1,500	1,500	1,500	1,500	1,500
GOT PROJECT MGR SALARIES (TD)		PY	10,000	10,000	10,000	10,000	10,000
(US $ EQUIVALENT)			11,111	11,111	11,111	11,111	11,111
PREPARATORY PRIV WORK							
"APUREMENT" (TD)		CO	15,000	15,000	15,000	15,000	15,000
(US $ EQUIVALENT)			16,667	16,667	16,667	16,667	16,667
INVENTORIES		CO	10,000	10,000	10,000	10,000	10,000
(US $ EQUIVALENT)			11,111	11,111	11,111	11,111	11,111
LOGISTICS							
GOT SUPPORT SALARIES (TD)		PY	3,000	3,000	3,000	3,000	3,000
(US $ EQUIVALENT)			3,333	3,333	3,333	3,333	3,333
TRANSPORT/COMMUNICATION (TD)			20,000	20,000	20,000	20,000	20,000
(US $ EQUIVALENT)			22,222	22,222	22,222	22,222	22,222
BROKERS FEES							
AVG SIZE OF OFFERING ($000)			10 0	10 0	10 0	10 0	10 0
% OF OFFERING			1%	1%	1%	1%	1%
FEE/OFFERING			100,000	100,000	100,000	100,000	100,000
PRIVATE SHARE OF TA/TRNG		%	50%	50%	50%	50%	50%

ANNEX 7 3
PRIVATE ENTERPRISE PROMOTION PROJECT
TUNISIAN TECNICAL ASSISTANCE
ESTIMATED COST PER MONTH

ITEM	UNIT COST UNIT	UNITS/ MONTH	COST/ MONTH
LABOR			
1 SALARY	254 DAY	22	5,598
2 OVERHEAD	100%SALARY		5,598
SUBTOTAL			11,196
3 MISCELLANEOUS EXPENSES			1,100
SUBTOTAL LABOR & EXPENSES			12,296
4 G&A/FEE	30%LABOR & EXPENSES		3,689
TOTAL			15,985

SALARY BASED ON TD 60,000/YEAR, EXCHANGE RATE
OF TD 0 900, AND 262 WORK DAYS
EQUIVALENT BURDENED DAILY RATE (W/O EXPENSES) TD 609

ANNEX 7 2
PRIVATE ENTERPRISE PROMOTION PROJECT
U S SHORT TERM TECNICAL ASSISTANCE
ESTIMATED COST PER MONTH

ITEM	UNIT COST UNIT	UNITS/ MONTH	COST/ MONTH
LABOR			
1 SALARY	319 DAY	22	7,012
2 OVERHEAD	100%SALARY		7,012
SUBTOTAL LABOR AND OH			14,023
EXPENSES			
3 AIRFARE	3,400 TRIP	1	3,400
4 PER DIEM	100 DAY	26	2,600
5 MISCELLANEOUS	1,000 TRIP	1	1,000
SUBTOTAL LABOR, OH & EXPENSES			21,023
6 G&A/FEE	30%LABOR & EXPENSES		6,307
TOTAL			27,330

- SALARY BASED ON 1/1/92 FS 01 RATE OF $83,502 AND 262 WORK DAYS/YEAR
- EQUIVALENT BURDENED DAILY RATE (W/O EXPENSES) $ 924

ANNEX 7 1
PRIVATE ENTERPRISE PROMOTION PROJECT
QUANTITIES

COMPONENT/CONTRACT OUTPUTS/INPUTS	UNIT	1993	1994	1995	1996	1997	TOTAL
GOT CONTRIBUTION							
I PRIVATIZATION/FINANCIAL MARKETS							
A PRIVATIZATION COUNTERPARTS							
1 0 SALARIES	PY	15	15	15	15	15	75
2 0 PREPARATORY WORK							
- APUREMENT	COS	4	5	5	5	5	24
INVENTORIES	COS	4	5	5	5	5	24
3 0 LOGISTICS							
REPORT PREPARATION	PY	15	15	15	15	15	75
- TRANSPORT ETC		LUMP SUM, SEE TABLES BELOW					
B BROKERS FEES	COS	4	5	5	5	5	24
C FINANCIAL MKTS COUNTERPARTS							
1 0 SALARIES	PY	3	3	3	3	3	15

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ANNEX 7 1
PRIVATE ENTERPRISE PROMOTION PROJECT
QUANTITIES

COMPONENT/CONTRACT OUTPUTS/INPUTS	UNIT	1993	1994	1995	1996	1997	TOTAL
2 0 FINANCIAL MARKETS							0
2 1 STUDIES	#	1	2	2	2	2	9
TA/STUDY	PM	2	2	2	2	2	10
FOREIGN	PM	1	1	1	1	1	5
LOCAL	PM	1	1	1	1	1	5
- TOTAL TA	PM	2	4	4	4	4	18
FOREIGN	PM	1	2	2	2	2	9
LOCAL	PM	1	2	2	2	2	9
2 2 TA TO IFI'S	PM	10	20	20	20	10	80
2 3 U S TRAINING FOR IFI'S	PM	5	10	10	10	10	45
3 0 CONTRACTOR MANAGEMENT							
3 1 U S ADVISOR	PM	2	3	3	3	3	14
3 2 LOCAL ADVISOR	PM	6	12	12	12	12	54
3 3 HOME OFFICE SUPPORT	PM	2	3	3	3	3	14
II DECENTRALIZATION							
A PSC	PM	12	12				24
B STUDIES							
1 0 FOREIGN TA	PM	2	3 3				5 3
1 1 LOCAL TA	PM	6	6 5				12 5
IV EVALUATION							
A IQC WORK ORDER	PM			2		2	4

ANNEX 7 1

PRIVATE ENTERPRISE PROMOTION PROJECT

QUANTITIES

COMPONENT/CONTRACT OUTPUTS/INPUTS	UNIT	1993	1994	1995	1996	1997	TOTAL
AID CONTRIBUTION							
I PRIVATIZATION/FINANCIAL MARKETS							
A VALUATIONS (LOCAL CONTRACTS)	PM	10					
B FINANCIAL STUDIES (BUY-INS)	PM	7					
C U S CONTRACTOR							
1 0 PRIVATIZATION							
1 1 DIAGNOSTICS	#	10	15	15	5	5	50
- TA/DIAGNOSTIC	PD	14	14	14	14	14	70
FOREIGN	PD	7	7	7	7	7	35
LOCAL	PD	7	7	7	7	7	35
- TOTAL TA	PD	140	210	210	70	70	700
FOREIGN	PD	70	105	105	35	35	350
LOCAL	PD	70	105	105	35	35	350
- TOTAL TA	PM	6	10	10	3	3	32
FOREIGN	PM	3	5	5	2	2	16
LOCAL	PM	3	5	5	2	2	16
1 2 TRANSACTIONS	#	2	5	5	5	5	22
TA/TRANSACTION	PM	6	6	6	6	6	30
FOREIGN	PM	3	3	3	3	3	15
LOCAL	PM	3	3	3	3	3	15
							0
TOTAL TA	PM	12	30	30	30	30	132
FOREIGN	PM	6	15	15	15	15	66
LOCAL	PM	6	15	15	15	15	66
1 3 INFORMATION, EDUCATION, & COMMUNICATION							
- TOTAL TA	PM	0	6	3	3	3	15
FOREIGN	PM	0	3	0	0	0	3
LOCAL	PM	0	3	3	3	3	12
1 4 FOLLOW-UP							
- TOTAL TA	PM	3	3	3	3	3	15
FOREIGN	PM	0	0	0	0	0	0
LOCAL	PM	3	3	3	3	3	15

ANNEX 7

DETAILED BUDGET

HG-004D PROGRAM
NOTIONAL TECHNICAL ASSISTANCE PLAN AND FINANCING

ACTIVITIES (benchmark reference No.)	SOURCE OF FUNDS ($) USAID DSP	PEP	RHUDO	GOT
Implementation of the municipal awareness program: Seminar, etc... (3.C2)		30,000		10,000
T.A. for implementation of municipal/private sector partnership projects (3.D1)		50,000		
Workshop on private provision of municipal services (3.D1)		20,000		10,000
Implementation of privatization activities in a RSM (3.D1)		50,000		
A MUNICIPAL DEVELOPMENT "OBSERVATOIRE"				
Setting-up of Observatoire and related data base (4.A1)			19,000	
Preparation and annual evaluation of the Program Benchmark Schedule (3 interventions at $30,000)		90,000		
MISCELLANEOUS				
Implementation PSC - 24 months		50,000		
TOTAL	450,000	410,000	39,000	245,000

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HG-004D PROGRAM
NOTIONAL TECHNICAL ASSISTANCE PLAN AND FINANCING

ACTIVITIES (Benchmark reference No.)	SOURCE OF FUNDS ($)			
	USAID			GOT
	DSP	PEP	RHUDO	
Study on new municipal system of analytical/cost accounting (2.B2)		20,000		
Implementation of new cost accounting system in a RSM (2.B2)		15,000		25,000
Preparation of a Municipal Training Strategy (2.B3)			5,000	
Preparation of a Training Action Plan for municipalities (2.B3)	60,000			
Implementation of the training plan in a representative sample of municipalities - RSM (2.B4)			10,000	60,000
III- PRIVATE SECTOR INVOLVEMENT AND PRIVATIZATION				
A series of Policy studies on the provision and financing of urban infrastructure and services including cost recovery study plus a public seminar to discuss policy implications (3.A1)	250,000			
Preparation of a five-year municipal investment program (3.B1)				10,000
Preparation of feasibility based PIC's (3.B2)				30,000
Analysis report on privatization activities in Tunisian Municipalities (3.D1)		20,000		
Preparation of a municipal awareness program on private sector participation in municipal projects (3.C1)		20,000		10,000

July 31, 1992

HG-004D PROGRAM
NOTIONAL TECHNICAL ASSISTANCE PLAN AND FINANCING

ACTIVITIES (benchmark reference No.)	SOURCE OF FUNDS ($)			
	USAID			GOT
	DSP	PEP	RHUDO	
I- ESTABLISHMENT OF CPSCL				
1- CPSCL Development Plan including Training Plan (1.A5)		20,000		
2- Implementation of CPSCL Training Activities (1.A6)			5,000	5,00
3- Financial Consultants to assist and review policies for the recently established CPSCL (1.B)		25,000		
4- Policy analysis on methods of facilitating the provision by Private Banks of direct loans to municipalities (1.C1)	40,000			
5- Preparation and dissemination of standard forms and checklists for municipal project identification (1.D1)				5,00
6- Policy Analysis for CPSCL Alternative Financing Models (1.E1)	50,000			
II- MUNICIPAL MANAGEMENT AND FINANCE				
1- Policy study on Local Tax Reform (2.A2)	40,000			10,00
2- Preparation and Implementation of a Property Tax Management Program (2.A1)				30,0
3- Policy study of the system of Central-Local budget and grant allocations (2.B1)	10,000			40,0

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3 <u>ONAS</u> (National Sanitation Office)

The Office National d'Assainissement (ONAS) was created in 1974. It is charged with the operation, maintenance, renewal and extension of the sewer systems in urban areas throughout the country, as delimited by decrees. ONAS has a regionalized organizational structure with operational centers in Tunis, Nabeul, Sousse and Sfax covering respectively the Greater Tunis area, the North, the Center and the South The current tendency is towards increased decentralization and deconcentration. With a staff of 2020 agents ONAS operates a network of some 4380 kms, 24 sewer treatment stations and 183 pumping stations serving 365,000 users in 56 municipalities, and some 420 hotels. During its 16 years of existance ONAS has invested a total of 290 million TD or about $320 million. Current levels of investment approach $60 million per year. ONAS relies heavily on Government contribution (60%) and foreign borrowing to finance its investment (28%). Despite sustained user rate increases (8 increases since the creation of the ONAS). ONAS has only been financing about 12% of its investment program from user charges. Revenues from user charges currently are only 50% of the total operating charges. Other revenues to offset operating charges come from the Fond Commun, a National Fund for financing municipal budgets (19%), and compensation revenues 17%. The compensation revenues are raised as a levy of 40 millimes per m3 of drinkable water and is paid by the state. In 1989 ONAS made TD 3.6 million deficit and is exected to had a TD 3.4 million deficit in 1990. According to current projection ONAS will have a surplus of TD 2.9 million in its operating account in 1991 that will result from new user charges adjustments.

F. <u>ENVIRONMENTAL ANALYSIS</u>

An extensive environmental analysis was accomplished as part of the design process for HG-004B. It reviewed Tunisian policies and procedures with regard to wastewater collection, treatment, disposal and re-use, as well as storm and surface water drainage and disposal. In addition, local road and sidewalk standards were reviewed in relation to the sites and services sub-program

The results of this environmental analysis showed that the procedures and technology in place in Tunisia were both appropriate and acceptable. Similar practices will be applied to projects to be financed under this Housing Guaranty supplement. Both ONAS and the participating municipalities will take full responsibility to assure that all environmental standards are maintained. A major benefit of this particular program is that sewers requiring rehabilitation will come under full ONAS operation and maintenance services for the first time.

With respect to their capacity to implement this program, the municipalities in the greater Tunis area are better positioned than most. In general, they are better staffed and they have the further advantage of being able to access professional assistance from the District of Tunis or from ARRU.

While there are clearly small municipalities without the "threshold" capacity to participate in the program, in general the project will follow a practice of self-selection. Technical assistance will be available on an as-needed basis from ARRU and municipal technical staffs should have little difficulty in providing the overall direction. They will contract with the private sector firms to design, construct, and supervise these relatively straight forward projects. In fact, the program should provide an opportunity to both use and enhance their skills.

2. ARRU (Urban Rehabilitation and Renewal Agency)

L'Agence de Rehabilitation et de Renovation Urbaine (ARRU) was created in 1981. It is chartered as a public industrial and commercial enterprise with a considerable degree of financial and decision autonomy. The ARRU is charged with upgrading below standard housing sites, extending services for neighborhoods not so equipped and renovating or building new housing. ARRU does not have its own investment budget. It usually operates as a principal on behalf of municipalities or ministries. Its operating budget is provided by the state and accordingly it does not charge for the services it extends Finally ARRU acts mainly as a Coordinator (maitre d'ouvrage délégué). It contracts all works and studies to private and public firms and does not have any in house production capacity.

Since its creation ARRU has accumulated a broad experience with urban upgrading and rehabilitation project. It assumed the implementation responsibilities for overseeing the IBRD 3rd and 4th urban projects totalling $47 million in rehabilitation components. This is in addition to other projects financed by the state and by the municipalities through the Caisse de Soutien aux projets des Collectivités locales (CPSCL), the Fonds National de Développement municipal, and the FNAH (the centrally managed fund financed by a property tax add-on).

In addition to overseeing the preparation and the implementation of urban renewal and rehabilitation projects ARRU also acts as agent of the state and the municipalities for the identification of urban projects and provides, treasury permitting, technical assistance to municipalities for the identification of urban projects. In this capacity ARRU recently completed two such activities encompassing more than $100 million of investment in over 100 neighborhoods.

situation is explained by the discrepancy between staff skills and the real needs of local Governments. The laws limiting the number of professional staff employed by each municipality and the supervisory authorities' control over recruitment discourage the recruitment of highly qualified staff in favor of the unskilled. Most municipalities do not have enough technical and administrative staff, and in many cases have fewer than the number permitted by law.

The regulations governing recruitment are not the only cause of the inadequacy of municipal staff. Qualified administrative and technical staff are not attracted to municipal positions because they do not offer the same benefits, in terms of promotion and bonuses for example, as do posts in the central Government. In addition, the institutional weakness of municipalities in terms of operational autonomy and relationships with other institutions creates an environment unlikely to attract high-caliber technical and administrative personnel.

Since 1985, however, municipalities are gradually introducing more rational management techniques. Computerization for example, has enabled a number of municipalities to improve the execution of day-to-day management and administrative activities, and in some cases, to substantially improve the collection of property taxes.

As municipalities take a more active role in the development of the areas under their jurisdiction, this process of modernizing management methods and improving the skills of municipal staff will continue. A major focus on hiring better qualified employees is needed, with one of the first steps being a revision of the rules that currently apply to municipal staff. Municipal employees should enjoy the same promotion opportunities and benefits as other public sector employees. Staff training and retraining programs should be organized for municipal staff.

The recently completed Urban Implications Study provides a prototypical organizational chart and staffing pattern for cities in the 20-50,000 population range (the municipality of Ben Arous for example, is slightly larger). The typical technical division, with responsibility for managing city property and infrastructure, as well as for overseeing local public works project, should have a workforce of 71, of which 5 would be senior and trained personnel.

2 Women in Development

USAID/Tunisia believes that the most effective way to assist women is by "mainstreaming" them in the development process. Therefore, the use of gender analysis, in order to "(1) achieve a more comprehensive understanding of the issue or issues being studied; (2) contribute more effectively to ensuring equal access by males and females; and, (3) monitor the effectiveness of gender-disaggregated program impacts," is a first step in understanding differences between men and women in society Based then on firm data, projects can include any specific components necessary to further Agency WID objectives.

The proposed HG 004D project promotes the delivery of urban infrastructure on a self sustaining basis. In support of the Mission's WID approach, RHUDO/NENA will collect gender-disaggregated data on program beneficiairies.

At a different level, the project also seeks to improve municipal capacity to plan, manage and maintain urban infrastructure. Hence, RHUDO/NENA will also, when assessing the technical assistance requirements of the municipalities involved, seek to incorporate Women in Development principles. Particular emphasis will be given to seeing that the development impacts of their municipal works are neutral or positive on females.

E. ADMINISTRATIVE ANALYSIS

1. Municipalities

Despite the fact that the GOT has officially adopted a policy of decentralization since the mid-1980's, the role of municipalities in Tunisia is still quite weak. Direct municipal responsibilities currently include only the provision of such services as building permits, maintaining local roads, street lighting and open space, some sewage maintenance and refuse collection. Administrative, technical, financial and planning functions are shared or subject to supervision by national-level entities, as are such activities as water supply/distribution and major road, sewer and land development projects. With the recent municipal elections and tentative steps toward greater decentralization at the governorate level, municipalities are destined to play a more important role in the future development of the country.

The general level of municipal management capacity remains relatively low in terms of both human resources and management tools. Despite very high staffing costs, municipalities are generally short of human resources. This paradoxical

During the last two decades, the public sector produced a very large number of housing units Because projects were designed and implemented quickly and the choice of sites not always ideal, many of these projects present difficult infrastructure problems today. The initial benefit to municipalities of having public sector housing projects has now turned into a burden and source of difficulties.

The upgrading of infrastructure in public sector housing projects therefore, has been proposed as a starting point for this program These projects have varying degrees of problems with the major ones involving inadequate or deficient sewers, stormwater drainage and roads

The proposed Housing Guaranty program is aimed at improving living conditions in these and other eligible low income neighborhoods. It will fund activities to upgrade sanitation networks to ONAS standards and improve storm water drainage and road networks to the point where the appropriate entities will take over their maintenance. This program is only part of the Tunisian Government's broader policy of upgrading substandard urban neighborhoods. Its implementation is expected to have a positive social impact by bringing about improvements that meet the expressed needs of the population.

Major benefits from this program will include improved sanitary and health conditions in a number of low income neighborhoods. Housing Guaranty guidelines require that this program be targeted to urban neighborhoods where resident household incomes are below the established median. One of the initial activities in identifying eligible projects will be to verify that household incomes correspond to AID criteria.

1. Information on Public Sector Housing Projects Proposed for Upgrading

   A household survey of some 32 public sector housing sites was carried out in the Fall of 1984 in order to obtain information about population characteristics and the kinds of infrastructure problems experienced within these neighborhoods. Data were collected on household size, occupation of the head of household, household income and expenditure, problems with housing, and willingness to pay for planned improvements. The surveys were, however, conducted with uneven quality. For this reason, their results are not extremely precise, and should be considered only in terms of establishing initial guidelines for the program.

Because municipal tax effort is weak, only about 50% of taxes owed are collected This leaves considerable room for improvement Prior AID experience with municipal finance in Tunisia has shown that municipal tax collection can be increased significantly at relatively minor cost. Technical assistance will be provided in conjunction with the HG-004D program to improve tax collection performance in participating municipalities.

To briefly summarize, overall growth in Tunisia's economy has resumed, government budget accounts have stabilized, the role of the public sector has decreased by selling off state enterprises to the private sector, and private sector investment has subsequently been expanding. The inflation rate remains moderate and relative price stability has been maintained.

D. SOCIAL SOUNDNESS ANALYSIS

The design of this supplementary Housing Guaranty program takes into account a variety of basic socio-economic factors related to urban conditions in Tunisia. These factors include:

- disparities in access to urban shelter services and maintenance, particularly in public sector housing projects and low income neighborhoods

- limited capacities of municipalities to provide a satisfactory level of urban services to their populations.

- greater demand for urban shelter services by the poor and increasing pressure on municipalities to respond to these demands;

In 1989, Tunisia's population of 7.9 million inhabitants was already highly urbanized with 60% of the residents living in urban areas. Urban growth rates were 3.0% per annum compared to an overall growth rate of 1.9% according to INS per annum. Roughly 83% of Tunisia's GDP was produced in urban areas.

Urban growth has been particularly important in the District of Tunis and along the coast from Bizerte to Sfax. Larger cities are growing at a faster rate than the national population, essentially because migrants continue to seek employment and other opportunities in these areas. With this growth has come increased demand for public services and infrastructure, shelter and utilities, and related environmental problems caused by inadequate sewage and solid waste, disposal and management services.

C ECONOMIC AND DEBT RISK ANALYSIS

Tunisia's economic situation and progress in line with structural adjustment is discussed at length in USAID/Tunis' Assistance Management Plan According to this document, structural adjustment reforms are working and Tunisia is on the move. Economic growth has resumed, with the balance of payments and government budget accounts now stablilized Exports are up by 35 percent and private investment has expanded by 20 percent in the last year Progress has been made in changing factor prices to encourage greater labor use, and in developing incentive systems to favor tradeable goods. The role of the public sector in the economy has decreased, the inflation rate of 6.5% is moderate, relative price stability has been maintained and when exogenous factors are considered, reasonable growth has taken place.

Nonetheless, there are still considerable problems to be faced. Drought in three of the last four years, heavy rains and flooding this year and an epidemic of hoof and mouth disease have all taken an economic toll. While structural adjustment remains on track, there have been slippages in implementing some of the necessary reforms this past year. As actions required to maintain the pace of structural adjustment become more difficult, further schedule delays may occur. Despite these problems, Tunisia's overall progress in implementing their structural adjustment program during the 1986-89 period is considered to have been quite good.

A debt risk analysis was carried out in conjunction with a recent Housing Guaranty borrowing (HG-004B auctioned July 1990). This analysis showed that although total debt had increased, short-term debt is minimal and the average interest rate for medium and long term debt had declined. The World Bank was quoted to the effect that Tunisia's credit rating remains high and continues to be one of the best in Africa. The IMF also reported that Tunisia has consistently met debt service payments at the original due dates. In addition, Tunisia is not negotiating with either the Paris or London Clubs and has not rescheduled debt, nor does it anticipate doing so. It is current on HG and other commercial and official debt and is operating under a WB/IMF supported structural adjustment program which has been successful to date. Based on all the relevant factors, the recently completed debt risk analysis concluded by stating that Tunisia is an acceptable candidate for further US assistance under the Housing Guaranty Program.

The debt carrying capacity of municipalities in Tunisia is also quite good. In the absence of the proposed program the debt service ratios of three Ben Arous municipalities over the next ten years varies from a low of 1.6 percent to a one year high of 8.9 percent of recurrent revenues.

population. Since its creation ONAS has invested 290 million TD or approximatly $320 million. The financing of these investments has been as follows:

- 60% state financing
- 28% foreign borrowing
- 10% self financing
- 2% beneficiary participation and other sources

ONAS has adjusted its tariffs eight times since its creation, the last of which took place in October 1989. The tariff adjustments are designed to reduce ONAS financial dependency on the state and to allow it to contribute a more substantial part of its investment needs.

The sites to be rehabilitated under the proposed program taken individually or as a whole constitute a very small proportion of ONAS users. The average neighborhood contains about 1000 users or about 0.3% of ONAS's total users. Furthermore, the rehabilitation works to be undertaken under the proposed program will positively affect the ONAS maintenance and operational budgets, the rehabilitated network being easier and cheaper to operate and maintain than at present.

(f) Cash Flow of the Program and HG Disbursements

The detailed Project Cash Flow Analysis is summarized below. This Cash Flow Analysis assumes a $6 million HG advance. This advance will be liquidated against funding commitments to municipalities. Subsequent disbursements will be necessary begining in year three. They will be calculated on the basis of the actual disbursements made, projected cash needs and the status of policy dialogue with the GOT. HG funds will be depleted by the end of the fifth year. Thereafter resources raised by the GOT will be necessary for the continuation of the program. The total amount of funds required for the continuation is TD 8.3 million or about $9.5 million, spread over a period of 7 years. The cash flow turns positive in the thirteenth year and the system can be sustained without any additional capitalization. By the end of the fifteenth year the portfolio or total infrastructure upgrading investments will be 72 million TD or $80 million.

The total yearly investments by municipalities is about 40 million TD of which 30 million TD is self financed and 10 million TD through borrowing The current level of borrowing for capital investment is quite low, and could safely be increased without jeopardizing financial stability

(ii) Debt Service Burden Resulting from a Typical Infrastructure Improvement Project.

The technical analysis conducted for the preparation of this Project Paper showed that the cost of a typical project will be around 1.24 million TD ($1.364 million). In the absence of any Central Government cost sharing, it is anticipated that the municipality will have to pay 80% of this cost or 992,000 TD ($1.09 million) and that beneficiaries will pay 20% or 220,000 TD ($240,000). Based on an interest rate of 10.5% and a maturity of 15 years, the debt service for the municipality contribution to the cost of the project is 134,000 TD ($148,000.) The proportion of this to the current revenues of a sample of 3 municipalities in the Greater Tunis area (Ben Arous, Megrine and Rades) varies between 11% and 13%.

In the case of Meghrine, the most indebted of the three municipalities, the ratio of debt service to current revenues without any improvement in tax collection, would increase from 4.6% to 15.6%. While this is still below the generally accepted ratio of 20%, it would represent a daunting three and one-half fold increase in debt service. As such, it should prove to be an important test of the central policy question, the degree to which municipalities seek and are able to assume control over their finances and provision of services. One should note that the debt service resulting from a loan made under the proposed program could be offset by an increase in revenues of about $4.64 per capita which amounts to a 13% increase over current levels.

(e) <u>Cost Recovery and ONAS Tariff Schedules</u>

ONAS was created in 1974. It is charged with the operation, maintenance renewal and extention of sewer systems in urban areas delimited by decrees. Currently ONAS operates a network of 4380 kms, 24 sewer treatment stations and 180 pumping stations and manages a portfolio of 365,000 users, equivalent to 63% of the urban upgrading a number of potentially eligible public housing sites under this program indicates that total costs average close to 1101 TD and that the direct contribution by beneficiaries therefore would be about 220 TD. These figures may be slightly higher for eligible neighborhoods in which no infrastructure currently exists.

(d) Municipalities

It is assumed that municipalities will be able to bear roughly 80% of the cost of a typical infrastructure improvement project. They will repay this debt primarily through improved tax collection. In the Municipality of Tunis, for example, a tax collection improvement campaign was undertaken in 1986 that resulted in doubling the total municipal tax receipts from property assessments A similar experience occured in Kairouan, where the introduction and use of a simple computer program for the management of property taxes led to a 65% increase in revenues.

On the average, only around 50% of the property taxes that are owed are in fact paid, which leaves considerable room for improvement. Experience in Tunisia has shown that these improvements can be made at relatively modest cost. Significant possibilities seem to exist, therefore, to improve municipal taxation and for municipalities to participate successfully in the program.

(i) Municipal Debt Carrying Capacity

The debt service of all municipalities in Tunisia is estimated at 6.8% of their recurrent revenue receipts. A general rule of thumb is that a municipality remains on a sound financial footing so long as its debt service does not exceed 20% of recurrent revenues.

A review of three Ben Arous municipalities for example, showed that debt service ratios over the next ten years, will be as low as 1.6% in Rades, from 3.2% to 4.6% in Meghrine, and varying from a low of 1.6% to a one year high of 8.9% in Ben Arous city.

assumed that municipalities will be able to repay approximately 80% of the loan through these improvements in tax collection.

2. Cost of Program

Detailed cost estimates for the rehabilitation and/or completion of infrastructure in public housing sites have been carried out as part of the HG 004D Project Paper preparation The cost per household or housing unit, varies from 360 TD to 4715 TD with an average of around 1100 TD

The GOT will undertake detailed financial analysis on a project by project basis. Affordability to beneficiaries and the ability of municipalities to service their loans will be among the key criteria for project selection.

3. Cash Flows and Affordability

(a) Municipal Development Authority (CPSCL)

The CPSCL will manage the proposed line of credit to fund municipal infrastructure. Although a detailed projection has not been made of the staffing requirements to manage this program, a 1.5% interest commission is considered adequate to cover its management costs.

(b) Tunisian Government

The Tunisian Government will have the use of the foreign exchange resulting from the Housing Guaranty loan and will therefore assume the full debt service of this loan. The Housing Guaranty loan is equivalent to 0.23% of the total Tunisian debt portfolio of $6.5 billion and the resulting debt service will be a similar proportion of the total debt service burden of the country.

(c) Direct Beneficiaries of the Program

Direct beneficiaries of this program will be households living in low income housing areas that meet program eligibility criteria for infrastructure improvement. Although the proportion of improvement costs to be paid directly by the beneficiaries is likely to vary somewhat between municipalities and projects, it is anticipated that direct project beneficiaries will contribute payments of approximately 20% of the total cost of rehabilitating their neighborhoods.

The exact method and formula to be used in making these payments will be based on the application of existing property taxes. Analysis of projected costs for

The need for upgrading varies from one low income neighborhood to another The objective is to raise the level of infrastructure to an acceptable level without going beyond that which is commonly found throughout the city.

In order to evaluate infrastructure problems in projects of the Societe Nationale Immobiliere de Tunisie (SNIT) and determine the cost of upgrading low income neighborhoods, socioeconomic studies were carried out in 1985 for a sample of 32 public housing sites in the Governorates of Tunis, Ariana and Ben Arous.

These projects included 18,420 housing units and housed roughly 104,000 inhabitants. Most of these projects were executed during the mid-1970's. According to this socioeconomic survey, the most significant problems are caused by deficiencies in sewer and storm water drainage networks. Among the sites, sixteen, comprising 10,600 housing units and a population of 64,000, were studied in detail with engineering drawings and bid documents prepared.

The sites included in this sample give a good indication of the costs of upgrading current infrastructure deficiencies. Site works as proposed in the bid documents are estimated to cost a total of TD 11.6 million at 1990 prices. A breakdown of these costs indicates that: 36% are for sewers, 10% for connections, 32% for storm water drainage, and 22% for roads.

B. FINANCIAL ANALYSIS

The proposed $15.0 million in Housing Guaranty funds will provide the necessary working capital to initiate and sustain an urban infrastructure upgrading and maintenance program of some $3 million per year. This will be adequate to improve the living conditions of some 1500 low income families on an annual basis.

1. Loan Mechanism

The Government of Tunisia will borrow the Housing Guaranty funds and directly assume repayment of this loan and the foreign exchange risk. It will lend the dinar equivalent of these funds to municipalities interested in rehabilitating and completing urban infrastructure in low income neighborhoods.

A 10.5% annual interest rate and 15 year maturity have been used for the purpose of this financial analysis. Participating municipalities will reimburse loans using two sources of revenue: a) contributions from beneficiaries directly served by the infrastructure improvements; and, b) revenues from improvements in the overall collection of property related taxes by the municipality. Although they have not been included in this analysis, the central government may provide funds for cost-sharing purposes. It is

ANNEX 6
PEP SUMMARY PROJECT ANALYSES
DECENTRALIZATION

The PEP Project will provide technical assistance that will help create a financing mechanism for infrastructure upgrading which can be accessed directly by municipalities, as well as help municipalities create the financial and technical capacity to better utilize the private sector in improving and operating basic services throughout the city. To do this, the PEP Project's Decentralization Component will provide the technical assistance that is critical to the implementation of the last phase of the Tunisia Low-Cost Shelter Project (Project Number 664-HG-004/D). The project analyses which supported the approval of the HG Project Supplement (August 29, 1990) relevant to the design of the PEP project, are summarized below.

A <u>TECHNICAL ANALYSIS</u>

In order to address Tunisia's housing stock deficit that prevailed in the years immediately after Independence, as well as to provide housing that was adapted to the needs of the people and their financial capacities at the time, housing agencies and low income families in informal settlements sought to build quickly and cheaply. Emphasis was placed on elements of the housing unit itself, without adequate consideration that housing is also a consumer of land and infrastructure.

Low income families economized as much as possible on the quality of infrastructure and site layout, allowing a maximum proportion of total housing costs to be devoted to the unit itself. In addition, housing suppliers were primarily specialized in housing construction and did not know very much about the provision of infrastructure.

In order to economize on the land input, the choice of sites was often based on lowest price. As a result, many of the sites were located in areas having serious problems, for example flood zones and low lying areas, or areas located at excessive distances from trunk line infrastructure.

In addition, housing was frequently built with only a minimum of infrastructure (e.g. compacted dirt roads, pit latrines, and the like). In time, these infrastructure systems proved inadequate, poorly adapted to the sites and their inhabitants and became the source of serious and considerable sanitation problems.

In locations where the level of infrastructure was adequately planned and designed, there were still problems in the quality of materials and execution of on-site work. These situations have been aggravated even further by the lack of adequate maintenance of road and sewer networks.

Perhaps more fundamentally, staffing and management are often unsatisfactory In April 1990 the World Bank observed that the authorities have kept bank salaries artificially low, and recommended more attention be paid to attracting well qualified personnel and rewarding good performance. An inter-bank symposium organized by a local economics revue concluded that the capacity of middle and upper management is weak and training generally inadequate.

Until these problems have been addressed more satisfactorily, the authorities will probably be reticent to remove some of the barriers that have insulated the banks from real competition in many areas.

In the public banking sector, the World Bank has extended a major loan to restructure the Government-controlled Société Tunisienne de Banque, the second largest bank in Tunisia. The Bank will encourage similar restructuring and reform at a few other large (Government-owned) banks, but not at the privately owned banks.

At STB, World Bank loan proceeds have been used to hire external consultants to help management revise the basic chart of accounts, introduce management information systems and other computer systems, bring branch network procedures into line with new head office procedures, identify non-performing loans, and introduce other management changes. The project is scheduled to take at least two years.

Although most private banks in Tunisia are sounder than the large Government-owned ones, they are under-capitalized by international standards. Donor assistance in setting management priorities and achieving key internal reforms is needed to accelerate the reform process and assist in making them truly competitive.

credit insurance is particularly important. Where such insurance is available on a timely basis at a reasonable price, it enables an exporter to offer competitive financing terms while avoiding excessive "foreign" credit risk. Without it, the exporter must choose between uncompetitive terms - e.g., insisting on a confirmed letter of credit - and what often is the excessive risk of dealing with foreign buyers with whom he may have little experience and lacks the ability to judge the credit risk.

Export credit insurance is not an issue for foreign firms who sell to their home-country affiliates, nor for sub-contractors who deal with importers on a long term basis. It is particularly critical for Tunisian-owned export firms expanding into new markets and seeking new clients.

This explains the prevalence of export credit insurance programs in all major exporting countries. (Eximbank and FCIA in the US, COFACE in France, ECGD in the UK, are the best known.) A similar program exists in Tunisia, but it is young and not yet well developed.

COTUNACE[2], established in 1984, is owned 60% by the GOT, 40% by banks and insurance companies. It currently offers Tunisian exporters six commercial risk products, generally with 80% coverage. COTUNACE has a small capital base, which in turn restricts the business it may prudently write. This also obliges the company to reinsure much of its business, which in turn cuts into its profitability and slows its growth. COTUNACE's shareholders have apparently agreed to a 150% capital increase, to take effect over the next year, which will alleviate this problem somewhat.

Tunisian exporters may also obtain political risk coverage up to 90% through a separate guarantee fund managed by COTUNACE but funded entirely by the GOT. (This fund is not part of COTUNACE's balance sheet.) This guarantee fund is less than half the size needed to assure sound risk coverage ratios.

COTUNACE estimates it insures less than 15% of Tunisia's exports and reaches less than half the eligible exporters at all. It has no branch offices outside Tunis. The new Chairman is in the early stages of planning a thorough review and improvement of the company's operations: products, procedures, technical functions, as well as the balance sheet.

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2 Compagnie Tunisienne pour l'Assurance du Commerce Extérieur.

In brief, COTUNACE, now 6 years old, is a critical institution in the effort to develop a fully performing export credit system, the utility of a competitive export credit program has been amply demonstrated in many countries. In that connection, some of Tunsia's competitors benefit from better established programs, COTUNACE's relatively low level of export insurance activity represents an additional competitive handicap the Tunisian exporter must face.

Even with a capital increase, COTUNACE does not have adequate financial resources to fund on a timely basis all the improvements it needs to provide a truly competitive export credit insurance service.

Although many of COTUNACE's products and procedures are modelled after the French and German programs, none of those organizations currently offers technical assistance. AID has previously contributed to the establishment of the policy risk guarantee fund (DT 1.7 million from PL 480 funds) and provided some limited TA to the organization in the form of overseas exposure tours for management.

The PEP project assistance will support the current management's objectives of improving operations, extending programs, developing new products and expanding coverage of exports.

5. <u>Technical Assistance and Training for Financial Intermediaries</u>

The commercial banking sector constitutes the lion's share of the Tunisian financial system but, regrettably, is financially weak, uncompetitive, and needs greater management depth. Improvement of the banking system is an important component of the World Bank's structural adjustment loans, and the Bank is strongly encouraging the Tunisian Central Bank to strengthen its bank supervision and control.

With individual exceptions, commercial banks in Tunisia typically face a number of major problems, despite astonishing reported profit growth (1990 net interest margin up 26% on average over 1989, net profits up 41%, etc.). Most important, World Bank and other analysts believe a great many Tunisian banks have not made adequate loan loss provisions, and in some cases management is not confident of the quality of their loan portfolios.

The likely low quality of some assets casts doubt on the quality of reported profits, and even on the solvency of some banks, which typically have low capital adequacy ratios. In many banks, internal accounting and internal controls are primitive. In a few cases, even external audits may be of low quality.

respects by regulatory and tax restrictions. World Bank EFRL conditions require removal of some of these restrictions, other changes may be needed as well

Development of mutual funds appears particularly useful for smaller, inexperienced investors in an underdeveloped stock and bond market investment climate. AID therefore will assist in clearing away remaining regulatory underbrush in order to make this type of collective investment vehicle more feasible and more attractive.

There will be a direct benefit as well in facilitating the success of the forthcoming privatizations since mutual funds will be a useful vehicle for attracting funds from the Tunisian public for the next round of privatizations. Indeed, without the presence of SICAVs and other institutional investors in the market, it may be difficult for the Bourse, in its undeveloped state, to handle the magnitude of the privatizations planned. Relatively modest US advice and TA would greatly assist the authorities and the investment community to achieve this goal.

In 1988 Tunisia's securities legislation was amended significantly, providing additional tax incentives for investment funds.[1] To date, however, only one open-ended mutual fund has been established, and this for debt securities only. One obstacle to their creation, especially funds of the type and size that would be useful in financing privatizations, appears to be a requirement for a three year waiting period before qualifying for listing on the Bourse. Given the other prudential regulations governing mutual funds, this may well be unnecessary.

Finance Ministry officials, among others, have indicated that they recognize that current legal requirements and tax regulations hamper unnecessarily the creation of broadly based mutual funds. They need additional assistance, however, if they are to make sufficient progress on a timely basis before the next round of privatizations. US TA could help break this significant regulatory logjam as well as help promote the concept of collective investment funds as desirable investment media.

4. <u>Export Credit Insurance Promotion</u>

Analysis performed during the design of the Management Training for the Private Sector Project points out clearly the importance of increasing exports and the difficulty exporters have in entering new markets abroad. In such a competitive environment, export

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1 Tunisian law has established two types of funds: closed-end (SICAFs) and open-end (SICAVs). See pp. 43ff and 65ff of the Financial Sector Assessment for details.

effects. First, it tends to reduce the amount of funds available for longer term lending and investment. Second, it means that Tunisia lacks a market-determined interest rate that serves as a "reference rate" for the rest of the financial system.

As a condition of World Bank lending, the Tunisian authorities have progressively reduced many of the restrictive features of the debt pricing, maturity, and asset allocation regulations. Starting in January 1992 the Government began issuing all debt at "market" rates, mostly through the weekly Treasury auctions. This change will also result in the elimination of all subsidized debt within ten years, as the Government must adopt a plan for retiring all outstanding bons d'équipement.

Even with these reforms, obstacles to secondary debt market trading and market develoment will exist. In this context the Central Bank seeks outside assistance in setting new debt management policies, and particularly in organizing a secondary debt market. It will be important that the Treasury structure new debt issues so as to minimize cost to the budget and maintain a suitable maturity profile, but without "rigging" the Treasury auction.

Development of a sound, active secondary debt market will benefit the Tunisian financial system in two main ways:

- create greater liquidity in the financial sector. (Improved liquidity is virtually a pre-condition for successful privatizations of significant size, so that underwriters and other investors can shift investments readily between cash and equities.)

- establish a market-based reference price for other interest rates.

- lengthen maturity of bond markets to medium and long term.

In addition, it will permit the monetary authorities to add open market operations to their tools of monetary control. Decreased reliance on reserve requirements and discount rate changes would result. This in turn would make it easier to avoid credit "crunches" in periods of rapidly rising money supply and credit growth.

3. Mutual Fund Regulatory Analysis

The Bourse remains virtually moribund, notwithstanding significant reforms during the last three years, some of which were implemented with technical assistance under the predecessor project to PEP. Likewise, with little stock market activity, open-end mutual funds (SICAVs) have not developed, in something of a chicken-and-egg dilemma. Further, the structure of SICAVs appears flawed in some standards (i.e., State enterprises will be required to adopt a modified form of commercial accounting standards).

As suggested above, the GOT's motive behind this reform is simple. the next round of privatizations, which will start in 1992, will involve the sale of going-concern enterprises, not partial asset sales as in the past, and will generally be done through the Bourse. Without reliable accounts for those enterprises (and for other quoted companies), the privatization sales effort will not be credible.

The accountants' own professional organization (the COECT) has published accounting principles and auditing standards for some industries, but they carry little legal weight. A main purpose in reviving the Conseil Supérieur is to establish the legal requirement to follow certain of those standards and require promulgation of additional standards. The COECT is cooperating enthusiastically with the re-animated CSC, its members chairing one of the working parties and volunteering readily to participate in lengthy (3 days non-stop) unremunerated working party sessions.

Part of the CSC's mandate is to take into account relevant international accounting standards. In that connection, the Participations Department (with specific approval of the Finance Minister) welcomes cooperation with US accounting specialists. (The other key Government office in the privatization process, the Secretariat to the Prime Minister, has concurred that a narrowly focussed effort would bring major benefits, and that US TA would be appropriate.) The precise nature of that cooperation will be worked out in the initial consultation between professional US specialists, the Ministry, and the CSC.

This activity directly complements the PEP project's privatization activity component. In particular, it can be used to help lay the groundwork for subsequent involvement of Tunisian accounting firms in valuation of large enterprises being privatized and preparation of the offering prospectus.

2. Secondary Debt Market Development

The Government currently obliges Tunisian banks (and insurance companies) to hold significant amounts of Government debt priced below market. These mandatory asset allocation policies penalize bank earnings and tend to "crowd out" private borrowers. More fundamentally, by subsidizing a large part of the Government's debt, they distort the entire range of interest rates and, by extension, other pricing throughout Tunisian financial markets.

There is no real secondary trading of Treasury debt (although a few banks now resell new Treasury issues to customers). Virtually all market participants purchase Treasury and other debt intending to hold it to maturity. This situation has at least two unfortunate

Traditionally, Tunisian businessmen have not favored financial disclosure in any form, and have deliberately avoided the generation, let alone the circulation, of accurate financial statements. Public sector commercial corporations, as well, have had limited incentives to publish accurate financial information.

Among the specific detrimental effects of this situation is its impact on activity at the Bourse. The lack of reliable financial information affects both the supply of and the demand for securities traded on the exchange. Because a company can obtain bank loans without submitting audited statements, the Stock Exchange's disclosure requirements are a strong disincentive for listing, since needed financing can be obtained more easily from the banks. Despite the fact that listed companies are subject to strict disclosure regulations, investors remain for the most part unwilling to invest in outside companies partly because they distrust published financial information. This deeply ingrained attitude restricts activity on the Tunis Stock Exchange.

In order for the next round of privatizations to succeed, this problem will have to be addressed urgently. Otherwise, prospective Tunisian and foreign investors will shy away from investments in all but the best-known enterprises. Worse, without reasonably reliable financial information, the risk of inappropriate bids - too low or too high - is increased, with harmful effects on the entire privatization program.

The GOT, of course, seeks maximum financial and political success for the next set of privatizations. Equally important for the longer term, they hope the quality of financial information provided on these companies will be models for the rest of Tunisian business. Finally, as most of the privatizations will go through the Bourse, the GOT also intends for this process to stimulate the Bourse. They are well aware that more reliable financial information is critical to all three of these goals.

To address this problem PEP will support a technical assistance activity in this area, to support privatization efforts through the Bourse by facilitating policy change being initiated by the "Participations" department in the Finance Ministry and executed by Tunisia's highest level accounting council (Conseil Superieur de Comptabilite, CSC). Although it is not designed as a general purpose activity to help improve the quality of financial information throughout the economy, improve the qualifications of accountants and auditors throughout Tunisia, etc., the proposed activity, if successful, will have an important demonstration effect.

The CSC has established four subcommittees to address: the basic accounting law, which would become obligatory; accounting standards; detailed accounting law for specific sectors including banks, insurance, and agriculture; public enterprise accounting

There are two Pension Funds in Tunisia· The CNRPS for Government and public sector employees (500,000 members) with total resources in excess of TD 250 million; the private pension fund CNSS which operates similarly to the CNRPS and has assets in excess of TD 300 million. Although there are no legal or regulatory limits on the type of investments made by the funds, they have so far played a minimal role in the securities market, concentrating their holdings on government bonds purchased at issue and held until maturity. This situation is expected to change in the future with the expected development of an active capital market, and adequate training and "sensitization" of these institutions.

B. Financial Markets Development

Project activities focus on increasing the availability of capital for private sector investors, especially for the prospective purchasers of state-owned enterprises and exporters. The Project focuses on improving the transparency of financial information, developing primary and secondary debt and equities markets, strengthening the management and operation of financial intermediaries, especially private ones, and improving export credit insurance programs. In selecting specific activities for this project, the mission has set the following general criteria against which a proposed activity can be measured:

-- expanding market forces in the financial sector;

-- increasing the role of private financial intermediaries;

-- aiding privatization and export promotion.

The following is an analysis of the priority areas included in the Project and the relevance to the improved functioning of financial markets:

1. Improving Financial Information

The lack of standardized and reliable financial information in Tunisia is one of the most pervasive constraints to the development of the financial sector. This problem results from a number of factors. While the country does have an association of chartered accountants, the Conseil de l'Ordre des Experts Comptables de Tunisie, who are well-trained in internationally accepted accounting principles and audit standards, there is no incentive for companies to apply these standards. There are no established charts of accounts (plans comptables) for various industries; corporations and government institutions do not have adequate internal audit systems; and members of the chartered accountants association do not uniformly apply any one set of accounting principles and audit standards.

more cooperative attitude following positive experiences of employee participation (Sogitex group, le Comfort), and the generally improved labor climate in enterprises which have been privatized

-An increasing awareness from all potential "actors" (banks, financial intermediaries, institutional investors, the press, the university...etc.) of the importance and catalytic role of the Privatization Program for Tunisia's development, i.e. opening of the economy, higher professional standards of management and accounting, and the expansion and increased sophistication of its capital market

3. An Adequate Absorption Capacity By Financial Markets

Despite recent ups and downs on the stock exchange, the recent stock offering of Tunisie Leasing (March 1992) illustrates the public's potential interest in such operations. The offer, for 10.5% of the company's stock (a total value of over TD 7 million), was four times oversubscribed; the stock was finally bought by almost 1000 investors. Its price remains today above TD 20, as compared to its TD 17.8 subscription price.

More generally, the financial market's capacity to absorb future privatizations (at the level projected by CAREPP) and other capital increase operations should not constitute a constraint, *if* of course these markets are well managed and supervised. With total deposits in the banking system exceeding TD 5 billion, funds from savings accounts alone potentially provide an ample supply. Savings deposited in savings accounts in banks reached TD 1.8 billion on December 31, 1991 with a growth of TD 200-300 million/year over the past three years. Savings accounts in "Caisse d'Epargne" totaled an additional TD 360 million. These figures show that, by any measure, it should be feasible to "divert" about $100 million/year towards privatization, including the purchase of attractive public stock offerings.

The size and role of institutional investors is little developed in Tunisia. There are ten insurance companies of which STAR, a Government owned company, accounts for over 40% of premiums in the market for which total insurance premiums received exceeded $190 million dinar in 1991. Until recently there has been little incentive (and expertise) in arbitrage of portfolio investments and most investments have been tied to Government and Bank obligatory papers. However, several insurance companies are indicating their interest in actively participating in the development, expansion, and stabilization of the financial markets, particularly for stock issues. Discussions with the President of the Association of Insurance Companies indicates that, under "attractive" conditions, the insurance industry could easily channel over $20 million/year into stock offerings.

-Broadening of target investors (local and foreign) to avoid concentration of economic power;
-Closer involvement of employee groups and labor unions in the process.

While there are pros and cons concerning the (sensitive) issue of transparency, the lack of historic information is a clear detriment to the privatization process: while many privatizations have been successful they have not been "advertised", success stories need to be documented and broadly publicized.

b. Structural Obstacles

These obstacles have been outlined in previous studies; many will be addressed by the PEP program and by the World Bank supported reform program. They include:

-The natural tendency of Tunisian entrepreneurs for secrecy of operations/financial information.
-The essentially family nature of most Tunisian businesses and their aversion/distrust of outside investors. This situation is further complicated by the penal orientation of the present Commerce Code--presently being reviewed for broad reform.
-Historical setbacks of many small and medium investors in the 1960s and '70s who were (often) "required" to take minority participations in companies, to see themselves forced to later sell at a loss. The recent up and down variation of the stock market (end 1991 to mid-'92) undermined the image of the Bourse and underlined the instability and inherent risks of the stock market.
-The general lack of reliable operational and financial information is a deterrent to business analysis/valuation and results in de-facto discounting in the purchase price offered by would-be investors.

c. Static Financial Markets

Despite many recent good reforms of institutions, regulations and fiscal incentives, financial markets have remained static. Only fifteen company stocks are listed on the stock exchange. Of these, nine are for well established banks which contribute the bulk of the stock trading volume; annual trading is still at a low TD 70-90 million. There is a lack of "independent" financial intermediaries (only two out of seventeen stock brokers) with strong capitalization that could play real active marketing, market making, and investor education roles. Institutional investors have played no active role in financial markets The investing public is still little aware (and partly skeptical) of stock market possibilities Overall this situation points to the need to "jump start" the stock market, i.e. break a vicious circle· practically no stock issues (except for banks) and consequently limited trading volume and low investor appeal.

2. Strengths

a. An Increasingly Attractive Legal and Regulatory Framework

Since 1987 a number of reforms have been enacted--and more are being prepared under World Bank guidance--to remove impediments to private enterprise, liberalize banking, and develop financial markets while eliminating market distortions. Among the measures already taken or soon to be implemented one can note:

-Continuous liberalization of banking since 1987, with freeing of interest rates, reduction of portfolio requirements for the banking system, gradual phasing out of Government "Bons d'Equipement" replaced by Treasury Bills at attractive rates...etc., all measures that create new competition in the financial sector and widen the array of financial instruments available

-Reform and strengthening of the Bourse; the improvement and streamlining of numerous stock exchange procedures and regulations, providing BVM with the minimum tools to coordinate, regulate, and foster financial markets in a modern and professional manner

-Recent tax reforms that reduce incentives for corporations to use debt over equity financing (i.e. share subscription can be deducted from earnings for tax purposes up to 35%) as well as provide incentives to investors in company stocks (i.e. dividends and capital gains are no longer taxable)

-Recent regulations (December 1991) which reduced portfolio requirements of insurance companies (down to 35%) opening the way for these companies (and more generally institutional investors) to actively participate in the financial markets.

2. An Increasingly Positive Climate For Privatizations, Reflecting:

-The realization, based on Tunisia's (as well as worldwide) experience, that privatizations do bring substantial economic benefits to enterprises, entrepreneurs, the investing public at large, and the employees. Tunisian labor unions today exhibit a

ANNEX 5
TECHNICAL ANALYSIS

A. Privatization

The Project design capitalizes on the regulatory reforms that have occurred since the start of the Structural Adjustment Program, especially in the financial markets area, while overcoming some of the key weaknesses of past privatizations. It's emphasis on more systemmatic planning, sales of firms through widely publicized share offerings and employee stock ownership plans, increased transparency, and better feedback and evaluation systems all work to increase the probability that the Government's objective of privatizing 75 enterprises over the next five years will be attained. The followowing is a review of the weaknesses that must be overcome through the Project and other complementary efforts, and the strengths that the Project design takes advantage of:

1. Weaknesses:

a. Shortcomings of Past Privatizations

The most often heard criticisms of past privatizations and of the current privatization process include:

-Assets (or shares) have been sold too cheaply or with too many advantageous conditions.
-Conversely, there were too many requirements attached by CAREPP (i.e. debt transfer, maintaining personnel levels...etc.) which made the offer unattractive or financially burdened operations after privatization.
-Privatizations have created more power concentration by transferring a public "monopoly" to a private "monopoly."
-The process lacks transparency; the short advance notice prevents potential "actors" from getting involved. The lack of open information possibly benefits "insiders" or well connected businessmen with access to information or decision makers.
-Employees and labor unions are not (or insufficiently) associated with the process, creating confrontational reactions.
-The privatization process has slowed markedly during 1991 and 1992. One does not know the Government's present plan and objectives for future privatizations.

While authorities disagree on many of these statements they recognize needs for improvement of future privatizations in a number of key areas:

-Democratization of stock ownership (through public share offerings in particular);

b Local currencies: Will all local currencies that may be generated with funds provided as a cash transfer to such a country also be deposited in a special account, and has A.I.D. entered into an agreement with that government setting forth the amount of the local currencies to be generated, the terms and conditions under which they are to be used, and the responsibilities of A.I.D. and that government to monitor and account for deposits and disbursements?

c. U.S. Government use of local currencies: Will all such local currencies also be used in accordance with FAA Section 609, which requires such local currencies to be made available to the U.S. government as the U.S. determines necessary for the requirements of the U.S. Government, and which requires the remainder to be used for programs agreed to by the U.S. Government to carry out the purposes for which new funds authorized by the FAA would themselves be available?

d. Congressional notice: Has Congress received prior notification providing in detail how the funds will be used, including the U.S. interests that will be served by the assistance, and, as appropriate, the economic policy reforms that will be promoted by the cash transfer assistance?

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C CRITERIA APPLICABLE TO ECONOMIC SUPPORT FUNDS ONLY

1. **Economic and Political Stability** (FAA Sec. 531(a)): Will this assistance promote economic and political stability? To the maximum extent feasible, is this assistance consistent with the policy directions, purposes, and programs of Part I of the FAA? Yes Yes

2. **Military Purposes** (FAA Sec. 531(e)): Will this assistance be used for military or paramilitary purposes? No

3. **Commodity Grants/Separate Accounts** (FAA Sec. 609): If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made? (For FY 1991, this provision is superseded by the separate account requirements of FY 1991 Appropriations Act Sec. 575(a), see Sec. 575(a)(5).) N/A

4. **Generation and Use of Local Currencies** (FAA Sec. 531(d)): Will ESF funds made available for commodity import programs or other program assistance be used to generate local currencies? If so, will at least 50 percent of such local currencies be available to support activities consistent with the objectives of FAA sections 103 through 106? (For FY 1991, this provision is superseded by the separate account requirements of FY 1991 Appropriations Act Sec. 575(a), see Sec. 575(a)(5).) No

5. **Cash Transfer Requirements** (FY 1991 Appropriations Act, Title II, under heading "Economic Support Fund," and Sec. 575(b)). If assistance is in the form of a cash transfer: N/A

a. **Separate account:** Are all such cash payments to be maintained by the country in a separate account and not to be commingled with any other funds?

37. **Marine Insurance** (FY 1991 Appropriations Act Sec 563): Will any A I D. contract and solicitation, and subcontract entered into under such contract, include a clause requiring that U.S. marine insurance companies have a fair opportunity to bid for marine insurance when such insurance is necessary or appropriate? Yes

38. **Exchange for Prohibited Act** (FY 1991 Appropriations Act Sec. 569): Will any assistance be provided to any foreign government (including any instrumentality or agency thereof), foreign person, or United States person in exchange for that foreign government or person undertaking any action which is, if carried out by the United States Government, a United States official or employee, expressly prohibited by a provision of United States law? No