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SETTING TUNISIA ON AN AMBITIOUS PATHWAY FOR A SUSTAINABLE ENERGY FUTURE

ESMAP support complemented the World Bank's $151 million Energy Sector Improvement Project to support Tunisia's goal to transition to a secure, viable, and sustainable energy future. This transition is being achieved by holistically addressing key energy issues with the removal of energy subsidies at the center, accompanied by improving the performance of energy sector companies, accelerating the development of renewable energy, and establishing a regulatory agency to enhance accountability and transparency. ESMAP's Energy Subsidy Reform Assessment Framework (ESRAF) played a key role in supporting Tunisia's subsidy reform by helping the government consider social protection, poverty, public awareness, and how people and businesses would be impacted and protected.

A NEED TO DIVERSIFY ENERGY SOURCES, IMPROVE UTILITY'S PERFORMANCE, AND PHASE OUT SUBSIDIES

The condition of Tunisia's electricity sector has been steadily declining in recent years. At the start of this engagement in 2017, the sector was confronted with several challenges: dependence on imported gas for electricity production threatened Tunisia's energy security and macroeconomic stability; distortive subsidies discouraged energy efficiency; and the national electricity and gas company, Société Tunisienne de l'Electricité et du Gaz (STEG), was facing deteriorating commercial and financial performance.

The government set a goal to diversify its energy sources away from imported hydrocarbons and provide cleaner and less expensive electricity to the Tunisian people and businesses with an ambitious target to achieve 30 percent renewables by 2030. In parallel, the government wanted to gradually phase out subsidies in a way that was least disruptive to the economy, socially sustainable, and politically feasible.

Like in many developing countries, Tunisia subsidized all energy products to different extents. The cost of products depends on the fluctuations of international oil prices and the exchange rate, but domestic prices are controlled and adjusted only occasionally. Liquefied petroleum gas (LPG) for households was the most subsidized at 60–70 percent, depending on international prices. This fuel discount acted as an important cushion for lower income households and ensured energy access for all, especially those without access to piped natural gas, who relied upon LPG for cooking and heating. Other products were subsidized to a lesser extent, but the tariff adjustments were ad hoc and did not reflect cost fluctuations.

The structure put a significant burden on the federal budget, as the total energy subsidy bill was estimated at 2.5 percent of GDP in 2018 (of which one-third went to LPG, 45 percent to electricity and gas, and the rest to transport fuels), while the government lacked the ability to target the most needy consumers. Tunisia was determined to reform the system.

SUPPORTING TUNISIA TO ADDRESS KEY CHALLENGES FACING ITS ELECTRICITY SECTOR

To support Tunisia's renewable energy targets, the World Bank's $151 million Energy Sector Improvement Project approved in June 2019 is funding efforts by STEG to strengthen the country's electricity transmission network to integrate domestically produced renewable energy. The project's goals included reducing the reliance on imported fossil fuel and generation costs, hence, enhancing energy security and setting the electricity sector on a path toward financial sustainability.

The project also helped STEG improve its commercial performance on a par with well-performing utilities globally.

This activity is aligned with the government's long-term vision to transition to a secure, viable, and sustainable energy future with an ambitious renewable energy plan. The Energy Sector Improvement Project is part of the Bank's wider engagement, where policy dialogue, technical assistance, advisory services, and lending complement one another to address some of the critical development challenges facing Tunisia.

ESMAP'S INVOLVEMENT TO HOLISTICALLY TACKLE ENERGY REFORM

To inform and complement the World Bank lending project and support the government's efforts to improve the performance and financial viability of the energy sector, ESMAP provided a $1.85 million grant in FY 2018–22 to finance analytical work to help the government implement the subsidy reform roadmap that ESMAP's technical assistance helped draft in FY 2018.

The ESMAP-funded analytical work helped the government design a holistic reform that tackled subsidies while addressing political economy concerns. The main outputs included:

- Monitoring the energy costs and tariff reform
- Calculating the fiscal impact of subsidy reform and of different tariff increase scenarios
- Assessing the macroeconomic impact of energy subsidy reform
- Assessing the impact of energy subsidy reform on firms and households, as well as options for mitigation measures
- A political economy analysis of stakeholders' interest and public opinion on the sector
- Communications support to build social consensus around the reform
- A technical and commercial performance diagnostic and improvement action plan for STEG
- A strategy for LPG subsidy reform
- A study tour for the inter-ministerial task force to learn about the LPG subsidy reform experience in India
- A hedging strategy to manage oil import prices

AN INTER-MINISTERIAL TASK FORCE ALLOWED FOR A COORDINATED RESPONSE

Based on a recommendation of the ESMAP-funded assistance, an inter-ministerial task force on energy subsidy reform was set up in FY2018 to tackle the multi-faceted nature of the reform with representatives from STEG, the Ministry of Energy (later integrated into the Ministry of Industry and Small and Medium Enterprises), Ministry of Finance, and Ministry of Social Affairs under the coordination of the Minister of Grand Reforms. This was the first time there was a coordinated effort to discuss this complex and intersectoral issue, which helped create a mutual understanding of the comprehensive strategy required. The task force was active in reviewing and contributing to the analytics and provided recommendations to the prime minister on tariff increases during FY2019.

CREATING A COMMERCIAL PERFORMANCE IMPROVEMENT ACTION PLAN FOR TUNISIA'S ELECTRICITY AND GAS COMPANY

ESMAP's grant supported the preparation of a diagnostic and performance improvement plan for STEG—incorporated into the design of the Bank lending project—to assess the progress of the 2016–20 performance contract between STEG and the Ministry of Energy and recommend actions for the next performance contract.

During the plan's development, STEG staff in all relevant departments formed an interdepartmental team to review the diagnostic and discuss the improvement plan, which was delivered in March 2019 with ESMAP support. The plan will serve as the basis for the next performance contract and STEG's investment plan and is expected to improve STEG's performance, thus, reducing the need for subsidies.

> This project is a significant investment in support of transforming the energy sector into a more environmentally friendly, energetically efficient and economically sustainable one.
>
> *Tony Verheijen, World Bank Tunisia Country Manager*

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APPLYING ESMAP'S ENERGY SUBSIDY REFORM ASSESSMENT FRAMEWORK

In addition to funding, ESMAP provided technical assistance by applying its Energy Subsidy Reform Assessment Framework (ESRAF). ESRAF is a comprehensive analytical toolkit and assessment framework that can be tailored to a country's specific situation to quantify energy subsidies, understand their impact, and evaluate the enabling environment for reform. It is a product of ESMAP's Energy Subsidy Reform Facility (ESRF), which has supported more than 70 energy subsidy reform efforts in World Bank client countries since 2014. The framework focuses on addressing energy subsidy issues that go beyond calculating the gap left behind by the removed subsidy Instead, it looks holistically at the impact it will have on poverty and social protection, and how best to support the population.

The framework includes 10 different aspects of analysis for a comprehensive approach to subsidy reform. Based on discussions with the government, excluding items 4 and 8 below, each of the other elements was applied in Tunisia:

1. Quantify subsidies
2. Assess fiscal impact
3. Analyze quantitative impact on households
4. *Analyze qualitative impact on households*
5. Assess readiness of social safety nets to mitigate the impact
6. Identify the impact on firms
7. Model macroeconomic impact
8. *Assess local environmental externalities of subsidies*
9. Understand the political economy of reform
10. Design communication campaigns

The use of ESRAF helped Tunisia implement a comprehensive tariff reform accompanied by mitigation measures to minimize the impact, as well as consultations to mobilize support for reform. For electricity, for example, support to the poor was done through the tariff structure. Smaller consumers would have smaller increases, and larger consumers have higher increases to reduce the impact on households. In parallel, the analyses carried out within the framework led the way for policy dialogue with the Ministry of Social Affairs on how to expand the existing social safety net to protect poorer customers. It also led to more policies allowing firms to invest in self generation of renewable energy to mitigate price increases. These impact assessments and dialogues were conducted jointly by the World Bank's energy, poverty, social protection, and macroeconomic teams. The understanding of these impacts, in turn, allowed the government to design a strategy to consult with stakeholders and communicate with the public about the rationale for the reform. For example, the analytical outputs, based on the framework above, provided the government with the needed information for its dialogue with external stakeholders, including the Tunisian General Labour Union and the Tunisian Union of Industry, Trade and Handicrafts.

HOW THE "OUR ENERGY" COMMUNICATIONS CAMPAIGN BUILT CONSENSUS ON ENERGY SECURITY BEING A SHARED RESPONSIBILITY

World Bank studies carried out in Tunisia in 2018 showed that 75 percent of the population incorrectly believed that Tunisia was rich in oil and was unaware that energy subsidies had been in place that accounted for reduced energy prices—only 15 percent of respondents knew that the cost of producing electricity and gas is higher than the price at which it was sold.

ESMAP funds helped design and kick start a national communications campaign supported by the World Bank and launched by the Tunisian Government in October 2019 to accompany the reform effort. It was determined to be the most direct channel to reach the public to create awareness of the process and build trust in the government that removing the subsidies would be beneficial and that the savings would be well used for other services. It included a website, Facebook page, a promotional video for TV and YouTube, promotional radio recordings, press release, and capacity building (media training for the government spokespeople of the campaign).

The name chosen for the campaign was TAKETNA طاقتنا, meaning "Our Energy," invoking the theme that the country's energy security is a shared responsibility. The campaign started by clarifying the facts: why Tunisia needed to import energy resources, why

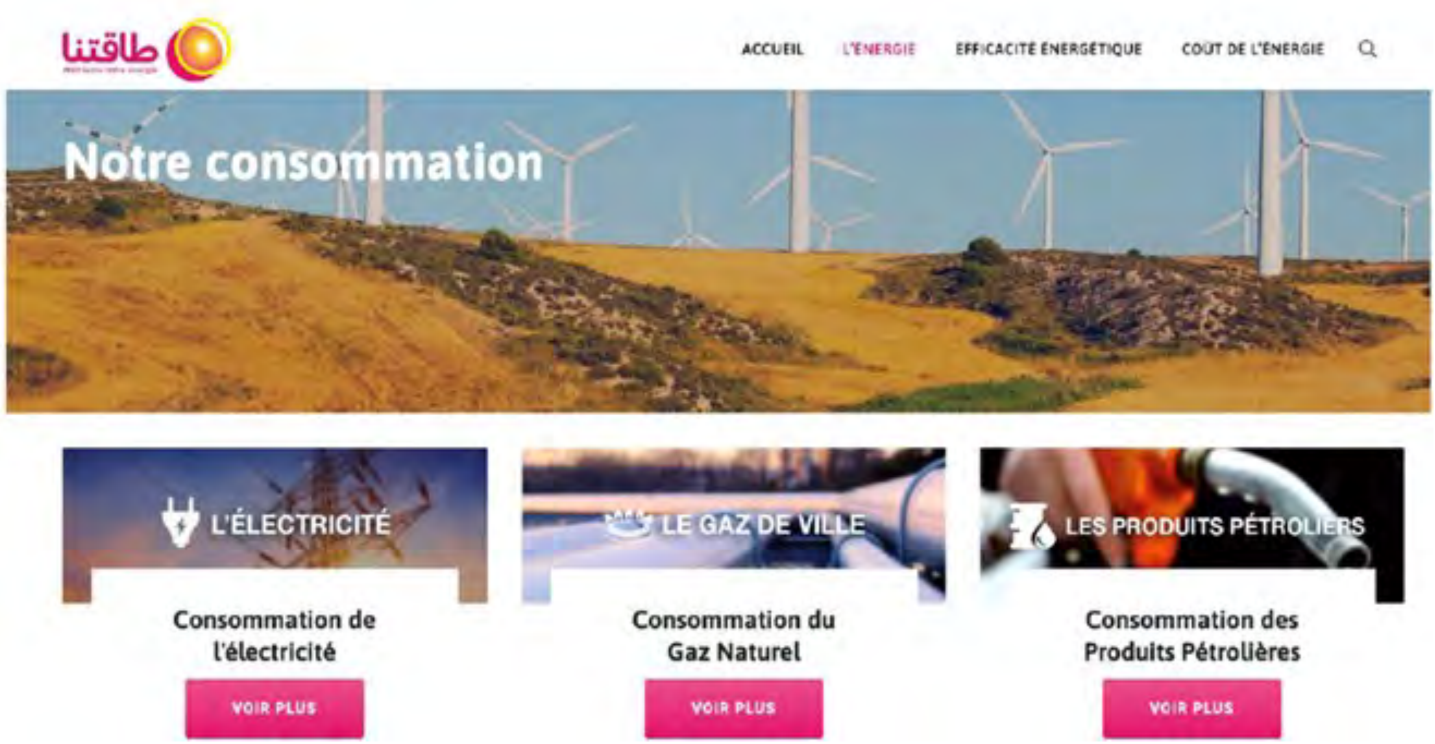

Image Source: ©World Bank

they were subsidized, and the cost of the opportunity.

The well-received promotional video, which starred Wael Toukabri—a highly regarded media figure in Tunisia, created awareness of the energy situation and presented a number of solutions. It was posted on YouTube and broadcast on TV and radio for two weeks.

The campaign continued to release posters mainly on Facebook, the most popular social media platform in Tunisia with more than 7 million active accounts.

The website hosted by the government played a central role in the campaign and serves as the primary source of information. The content was developed to be informative and easy to understand. The website and Facebook posts present easily understandable numbers on the basic facts of the sector (how much the country imports, how much each product costs, and how much subsidy is paid).

INTER-MINISTERIAL TASK FORCE STUDY TOUR ON THE INDIAN EXPERIENCE OF LPG SUBSIDY REFORM

In September 2019, a high-level delegation with representatives from several Tunisian ministries, with support from the World Bank team, traveled to India for a productive South-South knowledge exchange on LPG subsidy reform.

The Tunisian delegation was interested in learning ways to build a database of potential beneficiaries of a cash transfer program as compensation for a tariff increase and determine simple exclusion/inclusion and targeting criteria for targeted social safety net beneficiaries.

The lessons learned from the Indian experience helped create an understanding of how to proceed with an LPG subsidy reform with a clear outlook on the necessary policy, compensation system, and communication changes needed for a successful implementation. Seeing how another country succeeded with many of the changes helped boost the Tunisia team's confidence to plan their own reform strategy. The draft strategy for LPG subsidy reform elaborating the design of the cash transfer mechanism was validated by the inter-ministerial taskforce in November 2019.

IMPLEMENTING THE REFORM AND ROADMAP

In order to reform energy subsidies, the government has implemented a series of tariff increases for transport fuels, electricity, and natural gas in 2018 and 2019, expanded the database of the two safety net programs to cover 31 percent of the population to serve as channels for compensation against tariff increases, and issued implementing decrees to facilitate firms' self-generation to help them cope with increased electricity tariffs. ESMAP's technical assistance also allowed for the preparation of an assessment of the impact of energy subsidy reform on firms. Options for mitigation measures were presented to the Minister of Industry and Small and Medium Enterprises in September 2019 and validated by the National Agency for Energy Management in March 2020, which prepared an action plan to implement the recommendations.

To manage the costs of energy, a hedging strategy to manage oil price fluctuation was adopted by the government in January 2020. It also implemented a hedging transaction in 2019 in line with the hedging strategy (with the support of the World Bank's Treasury Department.)

Under STEG's performance improvement plan, the commercial action plan has been implemented under the project mentioned above. As part of the STEG commercial performance improvement action plan implementation, collection rates of the utility among private customers increased to 97 percent in FY2020 (from 92 percent in FY2018). In addition to improving collection rates, STEG has recruited more technicians and field staff to detect fraud, reduce losses, and improve customer service. The government has also concluded negotiations on projects of 500 MW solar photovoltaic with the private sector, helping to advance the country's renewable energy agenda.

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LOOKING FORWARD

As of April 2021, two of the technical assistance's three objectives had been completed: energy subsidy reform and performance improvement by STEG. The project's closing has been extended to 2022 to allow for sufficient time to complete the third objective—setting up a regulatory authority for the electricity and gas sector.

Although some aspects of the energy subsidy reform have been put on hold due to the COVID-19 pandemic, technical dialogue has restarted and the nature of the policy work will play an important part in Tunisia's economic recovery. The World Bank is in dialogue with the Prime Minister's Office on options to further reform subsidies to energy products, including more systematic application of the automatic indexation mechanism for petroleum products, design of an indexation for electricity and gas, and gradual removal of LPG subsidies, accompanied by targeted cash transfers and strategic communications.

ESMAP MISSION

The **Energy Sector Management Assistance Program** (ESMAP) is a partnership between the World Bank and 19 partners to help low- and middle-income countries reduce poverty and boost growth through sustainable energy solutions. ESMAP's analytical and advisory services are fully integrated within the World Bank's country financing and policy dialogue in the energy sector. Through the World Bank Group (WBG), ESMAP works to accelerate the energy transition required to achieve Sustainable Development Goal 7 (SDG7) to ensure access to affordable, reliable, sustainable, and modern energy for all. It helps to shape WBG strategies and programs to achieve the WBG Climate Action Plan targets.

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1818 H Street, NW Washington DC 20433 www.esmap.org esmap@worldbank.org