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MEMORANDUM AND RECOMMENDATION
OF THE
PRESIDENT OF THE
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
TO THE
EXECUTIVE DIRECTORS
ON A
PROPOSED LOAN
IN AN AMOUNT EQUIVALENT TO US\$58.0 MILLION
TO THE REPUBLIC OF TUNISIA
FOR A
FIFTH URBAN PROJECT

APRIL 30, 1989

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CURRENCY EQUIVALENTS

The exchange rate for the Tunisian Dinar is floating.
The rates used in this report are the ones
officially quoted as of April 13, 1989.

1 Tunisian Dinar (TD) = US\$ 1.07
1 US Dollar (US\$) = TD 0.94

WEIGHTS AND MEASURES

Metric System

ABBREVIATIONS AND ACRONYMS

AFH	- Agence Foncière d'Habitation (Land Development Agency)
BH	- Banque de l'Habitat (Housing Bank)
CNEL	- Caisse Nationale d'Epargne-Logement (Savings and Loans Fund)
CPF	- Conservation de la Propriété Foncière (Land Registry)
FOPROLOS	- Fonds Social pour la Promotion du Logement des Salariés (Workers Housing Fund)
MEH	- Ministère de l'Equipement et de l'Habitat (Ministry of Equipment and Housing)
OTC	- Office de la Topographie et Cartographie (Office of Topography and Cartography)
SNIT	- Société Nationale Immobilière de Tunisie (Real Estate Company)

FISCAL YEAR

January 1 - December 31

REPUBLIC OF TUNISIA
FIFTH URBAN PROJECT
Loan and Project Summary

Borrower: Republic of Tunisia

Beneficiaries: Housing Bank (BH), Ministries of Public Works and Housing and Justice

Amount: US\$58 million

Terms: 17 years including 5 years of grace, at the standard variable interest rate.

Financing Plan:

	<u>US\$ Million</u>
IBRD	58.0
US AID	15.0
BH	68.0
Housing Loans' Beneficiaries	54.0
Bilateral Aid/Government	3.2
Other Public Agencies	<u>1.8</u>
Total	<u>200.0</u>

On-lending Arrangements:

The Government would onlend the funds for the housing credit line to BH at a rate equal to at least the greater of (i) the Bank rate plus 0.5%, and (ii) the money market rate offered by the Tunisian Central Bank to the banks. Other project elements would be financed by budgetary grants to the ministries and agencies concerned. The line of credit would be used according to the following terms:

<u>Types of Loan</u>	<u>Interest Rate</u>	<u>Maturity</u>	<u>Grace Period</u>
Land Development and Construction loans)) at least average cost of funds plus 2-point spread) up to 3 yrs.) up to 2 yrs.
Mortgages)			

Economic Rate of Return: not applicable

Staff Appraisal Report: No. 7621-TUN

Map: No. IBRD 18707

**MEMORANDUM AND RECOMMENDATION OF THE PRESIDENT
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TO THE EXECUTIVE DIRECTORS
ON A PROPOSED LOAN
TO THE REPUBLIC OF TUNISIA
FOR A
FIFTH URBAN PROJECT**

1. The following memorandum and recommendation on a proposed loan to Tunisia for US\$58 million to finance a Fifth Urban Project is submitted for approval. The proposed loan would be for 17 years including a five-year grace period with interest at the Bank's standard variable interest rate.

Background

2. **Sector Issues.** Tunisia is already highly urbanized and urbanization is expected to continue at a fast pace. Of the total population of 7 million, 4 million live in urban areas, 2.5 million being concentrated in Tunis and three other coastal cities, in which most non-agricultural economic activities are also located. By the year 2000, more than 7 million people will be living in cities. Current demand for housing is estimated at 45,000 units per year. This demand and the demand for serviced land and infrastructure will grow rapidly. Housing constitutes about 20% of all investments. Until now, Tunisia has been successful in avoiding many of the worst features of rapid urbanization; slums and homelessness are relatively uncommon, as indicated by low average occupancy rates of 5.3 inhabitants (or 1.03 household) per dwelling. Moreover, basic utility services have improved considerably over recent years in most urban areas.

3. But the ability to meet future needs, even to preserve the achievements, is jeopardized by shortcomings in the regulatory framework, standards and institutions, as well as by a lack of appropriate financing. Until recently, urban housing and development were officially almost the exclusive domain of the State. In keeping with the broad economic liberalization in progress in Tunisia, regulations have been modified to permit more private activity, but they remain in many other respects ill-suited to the country's conditions, as do the standards governing urban housing and infrastructure. The sector institutions also need to be overhauled to meet the needs of the emerging private activity in the sector, and to function effectively in the liberalized financial sector.

4. Much of urban housing development has slipped into the informal sector, where official standards are disregarded and utility services are often difficult to obtain. Where official standards are applied, urban housing densities are low and the cost of services correspondingly high. A severe long-term problem of land registration has emerged; ownership is assured by the Torrens system of registering rights in a land book kept by the State, but only 50% of land in use has been registered. At the present rate, registration of all plots could take decades to complete. The problem affects rural land equally and, because of its consequences for the land information system, prevents efficient land management by hampering land-use control, establishment of boundaries, collection of taxes, and implementation of projects. The authorities are especially concerned by their inability to regulate the competition between housing and agriculture for land adjacent to towns.

5. The housing sector also lacks adequate financing. The former housing finance agency (CNEL), which financed low-income housing through a contractual saving scheme, experienced difficulties because of rigid regulations concerning savings and lending products, and the inability of the State system to supply housing, resulting in withdrawals by depositors. The desire for housing is a powerful incentive for household savings in Tunisia, whereas long-term lending for housing by the deposit and investment banks remains very limited. These difficulties associated with securing collateral and the inability to make long-term mortgage loans, have led to the Government's decision to transform CNEL into a full-fledged housing bank so that the new institution can operate with greater flexibility in the liberalized financial sector.

6. Recent Actions. In July 1988, the Government adopted a new housing policy. Its principal features are to: (a) increase the supply of land for housing by increasing densities, reserving sites, reorienting the public land development agency towards low-income households, and facilitating subdivision by private developers; (b) increase the supply of appropriate financing for land development and housing by restructuring the existing housing savings institution and removing restrictions on active participation by the banking and insurance sector; and (c) reclaim leadership in the management of urban development by defining an active policy to oversee and direct growth, setting up a land-use data base, revising outdated building and infrastructure standards, and updating the urban planning regulations. In March 1989, the Parliament passed a law authorizing the establishment of the new Housing Bank (Banque de l'Habitat [BH]), which was accomplished on April 28 at its shareholders' meeting.

Project Objectives

7. The principal objectives of the project are to: (a) increase the supply of affordable low- and medium-income housing programs through increased mobilization of domestic savings and rationalization of resource allocation; this would be done by supporting the new Housing Bank to fulfill its role as a financial institution; (b) increase the share of the formal private sector in land and housing development, and in surveying activities; and (c) initiate the modernization of the land information management system by simplifying the procedures for land registration and exchange.

Project Description

8. To support the necessary institutional and policy changes, the project would finance the following three components: (a) housing finance, which includes the transformation of CNEL into a housing bank, BH, with such necessary accompanying measures as training and technical assistance, as well as a line of credit to the new bank of US\$51 million; the line of credit would be available for land development, housing construction, acquisition, extension, and rehabilitation; (b) institutional strengthening of the Ministry of Housing to help implement and monitor Government's new housing policy adopted in June 1988, including a new regulatory framework facilitating private land and construction development, and restructuring of its parastatals SNIT (housing company) and AFH (land developer); and (c) land information management including the modernization of land registration and the production of base topographical maps.

Rationale for Bank Involvement

9. This project is a logical evolution of the Bank's involvement in the urban and financial sectors in Tunisia. Following continuous dialogue between Bank missions and the Government, the latter has moved towards reforming the housing sector. The proposed project is the first Bank operation in Tunisia to address critical issues in housing finance and the regulatory framework, in addition to continuing support to housing development. It comes at a time when the Government has decided to implement changes to allow the private sector to play a greater role in the provision of low-cost housing. The Government's decision to transform CNEL into a housing bank, BH, which will compete with other financial institutions in the full range of banking activities, is a big step towards building a universal banking system. Although other banks would remain free to lend for housing, the transformed CNEL would retain a competitive advantage because of its specialization and experience. The project would thus complement the financial sector reform supported by the Bank under the Structural Adjustment Loan approved in June 1988. The project would also initiate action in the area of land management, which the Government and the Bank have increasingly identified as a major constraint to the implementation of many projects. Land management policies will be followed up under forthcoming operations such as the proposed Second Agricultural Sector Adjustment Project and the Municipal Development Project. Given the complexity and sensitivity of land management, the Bank can contribute the experience gained in other countries and assist the Government in its effort to overcome existing institutional constraints to a more efficient utilization of land.

Lending Arrangements

10. The funds would be borrowed by the Government, which would onlend part of them to BH at the current Bank interest rate plus at least 0.5% or the money market rate offered by the Central Bank, and which reflects the supply and demand conditions in the inter-bank money market, whichever is higher. The proposed line of credit to BH would assist it over a two-year period in refinancing a share of its land development, combined construction-cum-mortgage loans for low-cost housing, including individual construction loans. Maturities of land development and construction loans would be up to three years; those of mortgages and individual construction loans would reach 20 years. The average lending rate of these subloans would assure a two-point spread over the total weighted average cost of resources^{1/}. BH would ensure that the total amount of all construction loans and mortgages for a particular subproject financed from the Bank loan would not exceed the total investment cost of that project (exclusive of land). BH would rely on borrowings and diversified savings instruments to fund its loans, in contrast with CNEL, which relied exclusively on contractual savings. It would thus be able to raise a much wider spectrum of resources, both locally and abroad.

Agreed Actions

11. During loan negotiations, assurances were obtained that: (a) the Government would onlend US\$51 million to BH on terms and conditions acceptable to the Bank; (b) BH's financial accounts would be audited annually by an independent

1/ Currently, the mortgage loan rate is 8.25% and the construction loan rate is 11.3%, compared with an inflation rate of about 7%.

auditor satisfactory to the Bank; (c) a system, satisfactory to the Bank, regulating real estate and land development activities would be introduced by December 1990; (d) an action plan detailing further studies and technical assistance would be prepared and provided by BH to the Bank by December 31, 1989; (e) a review meeting between MEH and Bank representatives would be held once a year to assess progress made in streamlining the regulatory system controlling urban planning activities and in the implementation of SNIT and AFH contrat-programmes; (f) an action plan (including a contrat-programme for OTC) would be agreed for the proposed institutional changes for the modernization of land registration; and (g) a review meeting between the Ministry of Plan and Finance and Bank representatives would be held once a year to assess progress made in the implementation of the action plan for institutional changes for the land management component, and to agree on necessary adjustments.

Justification, Benefits and Risks

12. (a) Housing. The project would endow the housing sector, which accounts for one-fifth of the annual investments made in Tunisia, with an autonomous and healthy financial institution able to contribute to the sector's financing requirements. The new institution would rely on the State budget only for subsidizing housing finance targeted to low-income groups. The project would thus assist the Government in fostering the "creditization" of the housing sector, with a view to eventually reduce the share of informal investments. The latter objective, which is a consequence of a more effective housing policy, would be achieved only in the medium-to-long term, and would be expected to be supported by further Bank projects. The main risks of this component are those inherent in any institutional restructuring. The project involves a new institution, BH, whose future effectiveness is uncertain despite all the built-in safeguards and whose institution-building efforts may be delayed by inherent resistance to change by its staff. The effects of the in-depth changes in strategies, procedures, and staff skill mix to be introduced in the three public agencies, may take longer than planned due to the extent of the retraining needed. To minimize these risks, a statement of general policy, a document of procedures, and an organization chart satisfactory to the Bank have been developed by BH, and a comprehensive technical assistance package has been included in the project.

13. (b) Land Information Management. Project benefits would come from improved security of tenure (legal aspect of cadastre) and improved knowledge of spatial development (topographical plans). The expansion of systematic and accurate mapping of urban areas would allow priority investment programs to be planned and executed more rapidly, and city planning to be more effective. More specifically, the main benefits are the following: (i) speedier land transactions to achieve more efficient land use; (ii) expanded use of credit based on land as collateral to finance investments; and (iii) better land consolidation and land redistribution, which are essential conditions for improving the productivity of land. The main risk is related to the ability of the institutions' management and staff to implement rapidly the necessary organizational changes leading to possible delays in the expected increase of private sector involvement and in the improved overall efficiency in financial intermediation.

Recommendation

14. I am satisfied that the proposed project would comply with the Articles of Agreement of the Bank and recommend that the Executive Directors approve the proposed loan.

**Barber Conable
President**

**Attachments
Washington, D.C. _____**

REPUBLIC OF TUNISIA

FIFTH URBAN PROJECT

Estimated Project Costs and Project Financing
(US\$ Millions)

Estimated Project Costs

PROJECTS COMPONENTS	LOCAL	FOREIGN	TOTAL	AS % OF TOTAL
	US \$ million			
A. HOUSING PROGRAMS	121.0	66.0	187.0	94 %
B. INSTITUTIONAL STRENGTHENING *	1.5	3.4	4.9	2 %
C. LAND INFORMATION MANAGEMENT *	2.4	5.7	8.1	4 %
TOTAL	124.9	75.1	200.0	100%

* including price and physical contingencies
US/DT (04/13/88): 1.07

Project Financing

PROJECT COMPONENTS	TOTAL COSTS	LOCAL FINANCING				FOREIGN EXCHANGE FINANCING		
		GOVERN- -MENT	Other Public Agencies	B.H.	Housing Loans Beneficiaries	I.B.R.D. URBAN V PROJECT	USAID	Other Bilateral Aid *
A. HOUSING PROGRAMS	187.0			67.0	54.0	51.0	15.0	
B. INSTITUTIONAL STRENGTHENING **	4.9	0.3	0.2	1.0	-	1.3		2.1 *
C. LAND INFORMATION MANAGEMENT**	8.1	0.8	1.6			5.7		
TOTAL PROJECT (US \$)	200.0	1.1	1.8	68.0	54.0	58.0	15.0	2.1

\$ US / DT (04/13/88) 1.07

* under discussion with bilateral aid; if not materialized, from Government.
** including price and physical contingencies

REPUBLIC OF TUNISIA

FIFTH URBAN PROJECT

Procurement and Disbursement

Procurement

Based on the experience under the Fourth Urban Project of 1986, and other Bank lines of credit in Tunisia, the line of credit to BH would refinance civil works and acquisition of housing units constructed under the project. No contract is expected to be suitable for international competitive bidding. Public developers would be subjected to Government procurement practices for public works. Private developers tend to execute construction works either by themselves or through a variety of small contractors.

The technical assistance components include the implementation of several studies and associated surveys. Contracts for which Bank financing is requested would be awarded according to Bank guidelines to qualified local and foreign consulting firms.

Topographical, cartographic, and computer material and equipment would be procured through ICB in accordance with the Bank guidelines. However, a wide variety of small items of specialized equipment with individual amounts not exceeding US\$150,000 and up to an aggregate total of US\$1.5 million may be procured through shopping on the basis of evaluation and comparison of bid invited from a list of at least three qualified suppliers eligible under Bank procurement guidelines.

Disbursement Schedule

<u>IBRD Fiscal Year</u> <u>US\$ million</u>	<u>Fiscal Year</u>						
	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>
Annual	2.3	7.6	14.5	13.3	10.4	8.2	1.7
Cumulative	2.3	9.9	24.4	37.7	48.1	56.3	58.0

Schedule C

REPUBLIC OF TUNISIA

FIFTH URBAN PROJECT

Timetable of Key Processing Events

- | | |
|---------------------------------------|---|
| (A) Time taken to prepare: | About two years |
| (B) Prepared by: | Government |
| (C) Bank's first preparation mission: | January 1987 |
| (D) Appraisal mission departure: | October 17, 1988 |
| (E) Negotiations: | March 1989 |
| (F) Planned Date of Effectiveness: | December 1989 |
| (G) List of Relevant PCRs and PPARs: | First Urban Project - PCR Nr.5013
Second Urban Project - PCR Nr.6750 |

THE STATUS OF BANK GROUP OPERATIONS IN TUNISIA

A. STATEMENT OF BANK LOANS AND IDA CREDITS

(As of March 31, 1989)

Loan or Credit Number	Year	Borrower	Purpose	US\$ Million Amount (Less Cancellations)		
				Bank	IDA	Undisbursed
Forty-seven Loans and Ten Credits Fully Disbursed				780.11	75.16	
1797	1980	Office des Ports Nationaux	Third Port	35.20		1.23
1961	1981	Republic of Tunisia	Fourth Education	21.00		6.09
1969	1981	Republic of Tunisia	Small-Scale Industry Development	30.00		3.74
1997	1981	Republic of Tunisia	Northwest Rural Development	17.54		2.09
2005	1981	Republic of Tunisia	Health and Population	8.50		2.76
2052	1981	Republic of Tunisia	Grain Distribution and Storage	33.40		1.01
2108	1982	Republic of Tunisia	Fifth Highway (Rural Roads)	35.50		7.75
2157	1982	Republic of Tunisia	Irrigation Development	15.30		2.14
2223	1983	Republic of Tunisia	Urban Development III	25.00		16.02
2230	1983	Republic of Tunisia	Education V	27.00		15.59
2234	1983	Republic of Tunisia	Central Tunisia Irrigation	13.70		5.08
2255	1983	Republic of Tunisia	Urban Sewerage III	34.00		20.54
2289	1983	Republic of Tunisia	Sfax Flood Protection	22.30		.29
2346	1984	Republic of Tunisia	Mining Technical Assistance	7.80		2.31
2368	1984	Republic of Tunisia	Seventh Water Supply	50.00		27.54
2429	1984	Republic of Tunisia	Second Urban Transport	33.00		19.74
2455	1984	Société Tunisienne de l'Electricité et du Gaz	Fourth Power	21.52		6.25
2502	1985	Republic of Tunisia	Northwest Agricultural Production	8.80		7.49
2522	1985	Republic of Tunisia	Export Industries	32.50		20.06
2554	1985	Republic of Tunisia	Second Electrical and Mechanical Industries	32.50		22.84
2573	1985	Republic of Tunisia	Irrigation Management Improvement	22.00		16.52
2605	1985	Republic of Tunisia	Gabes Irrigation	21.70		12.57
2735	1986	Republic of Tunisia	Energy Conservation	4.00		3.87
2736	1986	Republic of Tunisia	Fourth Urban Development	30.20		24.26
2754	1986	Republic of Tunisia	Agricultural Sector Adjustment	150.00		42.37
2781	1987	Republic of Tunisia	Industrial & Trade Policy Adjust.	150.00		50.11
2865	1987	BNT	BNT IV	30.00		21.86
2870	1987	Republic of Tunisia	Agriculture	20.00		17.93
2896	1987	Republic of Tunisia	Highways Maintenance & Rehabilitation	63.00		62.99
2911	1988	Republic of Tunisia	Second Small & Medium Scale Ind. Development	28.00		28.00
2962	1988	Republic of Tunisia	SAL I	150.00		150.00
3023	1989	Republic of Tunisia	Petroleum Exploration /a	5.50		5.50
TOTAL				1,963.00	75.16	626.54
Of which has been repaid				481.52	13.06	
Total Now Outstanding				1,481.48	62.10	
Amount Sold				34.82		
of which has been repaid				26.93	7.89	
Total now held by Bank and IDA				1,473.59	62.10	
Total Undisbursed						626.54

/a Not yet effective.

B. STATEMENT OF IFC INVESTMENTS IN TUNISIA

(as of March 31, 1989)

Fiscal Year	Obligor	Type of Business	Amount of US\$ Million		
			Loan	Equity	Total
1962	NPK Engrais	Fertilizers	2.00	1.50	3.50
1966/70/78	Société Nationale d'Investissement (now BDET)	Dev. Finance Co.		2.30	2.30
1969	COFIT Tourism (now BNGT)	Dev. Finance Co.	8.00	2.2	10.20
1973	Société Touristique et Hôtelière RYM SA	Tourism	1.60	0.3	1.90
1974	Industries Chimiques du Fluor	Chemicals		0.6	0.60
1975	Société d'Etudes et de Développement de Sousse-Nord	Tourism	2.50	0.6	3.10
1985/86	Société Tunisienne de Leasing	Leasing Co.	3.40	0.5	3.90
1985	Société Minière de Spath Fluor et de Barytine (Fluobar)	Mining Co.		0.3	0.30
1986	Société Industrielle des Textiles (SITEX)	Textiles and Fibers	5.0	3.2	8.20
1987	Adwya S.A.	Pharmaceuticals	2.0	0.3	2.30
1987	Rozzi Edilizzia Industrializzata (REIT S.A.)	Prefabricated Panels	1.3	0.4	1.70
1987	COMETE Engineering	Engineering Services	-	0.04	0.04
1988	Société des Industries Textiles Réunies S.A. (SITER)	Textiles & Fibers	<u>2.35</u>	<u>2.14</u>	<u>4.49</u>
Total Gross Commitments			28.45	14.38	42.83
Less cancellations, Terminations, Repayments and Sales			<u>15.21</u>	<u>2.80</u>	<u>18.01</u>
Total Commitments Held by IFC			<u>13.24</u>	<u>11.58</u>	<u>24.82</u>
of which Undisbursed			<u>6.11</u>	<u>.20</u>	<u>6.31</u>

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from IFC/04/14/89

ALGERIA

LIBYA

TUNISIA

- National Capital
- Governorate Capitals
- Paved Roads
- Railways
- ⚓ Ports
- ✈ Airports
- Salt Lakes
- - - Governorate Boundaries
- - - International Boundaries



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