RESTRICTED

Report No. P-943

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT AND RECOMMENDATION OF THE PRESIDENT TO THE EXECUTIVE DIRECTORS ON A PROPOSED LOAN TO BANQUE NATIONALE DE TUNISIE WITH THE GUARANTEE OF THE REPUBLIC OF TUNISIA AND A PROPOSED CREDIT TO THE REPUBLIC OF TUNISIA FOR AN AGRICULTURAL CREDIT PROJECT

May 18, 1971

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT AND RECOMMENDATION OF THE PRESIDENT TO THE EXECUTIVE DIRECTORS ON A PROPOSED LOAN TO BANQUE NATIONALE DE TUNISIE WITH THE GUARANTEE OF THE REPUBLIC OF TUNISIA AND A PROPOSED CREDIT TO THE REPUBLIC OF TUNISIA FOR AN AGRICULTURAL CREDIT PROJECT

1. I submit the following report and recommendation on a proposed loan and a proposed credit totalling an amount in various currencies equivalent to $8.0 million for an agricultural credit project. The loan of $5.0 million would be made to Banque Nationale de Tunisie (BNT) with the guarantee of the Republic of Tunisia. The credit of $3.0 million would be made to the Republic of Tunisia and its proceeds relent to BNT.

PART I - HISTORICAL

2. The proposed loan and credit would be the Bank Group's second operation in Tunisia's agricultural sector. In 1967, the Bank and IDA financed the Cooperative Farm Project (Loan No. 484-TUN; Credit No. 99-TUN) which, after changes in Tunisia's agricultural policies affecting the character of the project, had to be revised. In late 1969, the Government asked for Bank Group assistance in the private agricultural sector. This project was prepared with help from the FAO/IBRD Cooperative Program and appraised in June/July 1970.

3. Negotiations for the proposed loan and credit were held in Washington from March 25 to 31, 1971. The Tunisian delegation was headed by Mr. Ghenima, President and Managing Director of BNT, and included Mr. M'rad, Ministry of Planning, Mr. Ben Khedher, Ministry of Agriculture, Mr. Chatti, President and Managing Director of Societe Tunisienne d'Industrie Laitiere (STIL), Mr. Hamda, BNT, and Mr. Badra from the Tunisian Embassy in Washington.

4. My Report and Recommendation dated May 17, 1971 on a proposed loan to Tunisia for a highway project (P-942) includes a summary statement of loans and credits to Tunisia at April 30, 1971 and comments on certain problems encountered on projects previously financed.

PART II - DESCRIPTION OF THE PROPOSED LOAN AND CREDIT

5. BANK LOAN

Borrower:	Banque Nationale de Tunisie (BNT)
Guarantor:	Republic of Tunisia
Purpose:	To be used by BNT for making loans to help finance development of cereal and dairy farming, and of date-palm plantations.
Amount:	The equivalent in various currencies of $5.0 million.
Amortization:	In 15 years including a 5-year period of grace, through semi-annual installments beginning September 15, 1976 and ending March 15, 1986.
Interest Rate:	7-1/4 percent per annum.
Commitment Charge	3/4 of 1 percent per annum.
Estimated Economic Return on the Project:	22 percent

IDA CREDIT

Borrower:	Republic of Tunisia
Beneficiary:	Banque Nationale de Tunisie (BNT)
Purpose:	The same as for the Bank loan.
Amount:	The equivalent in various currencies of $3.0 million.
Amortization:	In 50 years including a 10-year period of grace, through semi-annual installments of 1/2 of 1 percent from September 15, 1981 through March 15, 1991 and 1-1/2 percent from September 15, 1991 through March 15, 2021.
Service charge:	3/4 of 1 percent per annum.
Relending terms:	15 years including a 5-year grace period, at an interest rate of 1 percent per annum.

PART III - THE PROJECT

6. An appraisal report entitled "Agricultural Credit Project - Tunisia" (No. PA-79a) is attached.

7. Measured in constant 1966 prices, the contribution of Tunisia's agricultural production to GDP has, despite a high level of investment, dropped from a one-time high in 1965 of almost $200 million to some $150 million in 1970, or little more than the 1960 production level. This disappointing performance can be explained by a number of reasons. Bad weather and the heavy floods in fall 1969 depressed production. The program of organizing agricultural cooperatives increasingly led to misallocation of resources and reduced productivity. Private farmers benefitted little from public investment programs, and when finally threatened with loss of their land to cooperatives, liquidated a large part of their livestock and equipment.

8. The Government is beginning to redefine agricultural policies. While this will take some time, immediate measures are required to increase productivity in order to contain rising food imports. The Government has decided to give immediate assistance to the modern agricultural sector which would be most responsive, by introducing a program which is expected to lead to considerable import savings on cereal and dairy products and to yield valuable foreign exchange from date exports. The project whose total cost amount to $15 million would be part of this program.

9. The major part of the project (61 percent) will be for the mechanization of grain farming in northern Tunisia. Credit facilities would be opened to farmers for purchasing wheel and crawler tractors, combines and related agricultural machinery. BNT would, simultaneously, provide from its own sources short-term credit for financing inputs like high yielding seeds and fertilizers.

10. Fourteen percent of the funds available under the project would go into development of dairy farming in northern Tunisia and would help rebuild livestock herds which farmers liquidated in 1969 after the transformation of all arable land into cooperatives had been announced. Investment for this subproject would comprise the purchase of livestock, installation of groundwater pumps for small-scale irrigated fodder production, improvement and modernization of barns and mechanical equipment.

11. About 22 percent of project funds would be earmarked for date plantations in southern Tunisia. New oases would be created in the desert on water from artesian aquifers. This would require drilling of bore-holes up to 600 meters deep, installation of pumps where underground pressure would not be sufficient, irrigation and drainage equipment, land and soil preparation, planting of date palms and wind breaks, and ancillary installations. This sub-project would be carried out by Societe Tunisienne de l'Industrie Laitiere (STIL), a company with no direct State participation which has already gained considerable experience in oasis development.

12. The remaining 3 percent of project funds would finance supporting services to improve BNT's project appraisal section, the technical staff of STIL's plantation management and the public dairy farm extension service.

13. Banque Nationale de Tunisie (BNT) would be the Borrower of the $5 million Bank loan. The IDA credit of $3.0 million would be made to the Republic of Tunisia and re-lent to BNT on the terms and conditions of the Bank loan except that the interest rate would be 1 percent.

14. BNT is the second largest Tunisian commercial bank, and engages mainly in agricultural credit. The Government holds 25 percent of its capital, other public bodies 60 percent, and 15 percent is held privately. The institution is well managed and its staff competent. A fairly high present financial engagement vis-a-vis Societe Tunisienne d'Industrie Laitiere (STIL) which will be the sub-borrower for the date-palm sub-project, has now been adequately secured and will be gradually reduced under a covenant of the Loan Agreement.

15. BNT would make project sub-loans at 8 percent annual interest. Grace and repayment periods would correspond to requirements of sub-projects and would be longest for the date-palm sub-project where the total repayment period would be 15 years. Interest rates for agricultural credit in Tunisia are presently around 4 percent. The increase to 8 percent for project sub-loans would mean an important change in the present low interest policy and would lead to better resource allocation. To moderate the impact of the interest rate increase the Government would temporarily pay farmers a direct subsidy towards investment cost. This subsidy would not exceed the equivalent of 2 percent annual interest so that farmers would pay a minimum effective rate on sub-loans of 6 percent per annum. The same condition would apply if farmers eligible for project sub-loans would apply for loans from other funds administered by BNT. In the meantime, agricultural subsidies as well as the system of high agricultural taxation are expected to be reviewed as part of an overhaul of agricultural policies which the Government is now undertaking.

16. At the request of the Government, it was agreed that the Government re-lend the IDA funds to BNT at 1 percent. The average cost of Bank/IDA funds (4.9%) and of BNT's own resources (4%) would then result in a blended cost of 4.7% giving BNT an overall margin on project operations of 3.3%. This margin would be adequate to cover project overheads, including administrative expenses and provisions for bad debts, and would help in establishing adequate reserves for BNT.

17. At present BNT's liquidity position is strained because of large advances made to cooperatives amounting to D 5.6 million, which have not yet been repaid. These loans had been granted under a Government guarantee and the Government has now agreed to repay in five equal installments an amount of D 2.6 million owed by cooperatives which were dissolved in the wake of the 1969 policy changes. Already in the agreements amending Loan Agreement No. 484 and Credit Agreement No. 99 dated November 23, 1970, it

had accepted to reschedule D 3.0 million owed by cooperatives which were maintained on State lands after 1969. These debts will be repaid over five years partly by the Government and partly by these cooperatives.

18. Most of the goods and services needed for the project would, not be suitable for bulk procurement, and would, therefore, be bought through existing commercial channels. Supplies are adequate, prices competitive and servicing facilities available. Drilling contracts under the date-palm development sub-project would be awarded after international competitive bidding except for four impending operations to be completed before August 1971 where application of international bidding procedures would delay groundwater development and cause the loss of a planting season.

19. Financial rates of return on the project would be high. For the grain farming sub-project, they would vary from 21 to 25 percent according to farm sizes, reach 26 percent for the dairy farm sub-project and 14 percent for the date development. The overall economic return on the project is estimated at 22 percent.

20. The Bank/IDA contribution would meet the foreign exchange expenditure amounting to 53 percent of project cost. 17 percent would be provided by BNT, and farmers would contribute the remaining 30 percent. Bank/IDA would disburse 75 percent on each sub-loan made by BNT which would correspond to the 53 percent overall foreign exchange component.

PART IV - LEGAL INSTRUMENTS AND AUTHORITY

21. The draft Loan Agreement between the Bank and Banque Nationale de Tunisie, the draft Guarantee Agreement between the Republic of Tunisia and the Bank, the draft Development Credit Agreement between the Republic of Tunisia and the Association, the Report of the Committee provided for in Article III, Section 4 (iii) of the Bank's Articles of Agreement, the Recommendation of the Committee provided for in Article V, Section 1 (d) of the Articles of Agreement of the Association, the text of a Resolution approving the proposed Loan and the text of a Resolution approving the proposed Development Credit are being distributed to the Executive Directors separately.

22. The draft Loan, Guarantee and Development Credit Agreements conform substantially to the pattern of agreements for agricultural credit projects. I would call your attention to the following features:

(i) Both the Loan and Development Credit Agreements have identical provisions with respect to the allocation of the proceeds of the total financing to be provided by the Bank and the Association for the Project (Schedule 2 of both Agreements);

(ii) The Loan will not be disbursed until the amount of the Development Credit has been fully withdrawn or committed (aforementioned Schedule 2).

23. The Loan, Guarantee and Credit Agreements will be subject to ratification.

24. I am satisfied that the proposed loan and credit would comply with the Articles of Agreement of the Bank and of the Association.

PART V - THE ECONOMY

25. A brief statement on the Tunisian economy was included in my Report and Recommendation on a proposed loan to Tunisia referred to in paragraph 4 above. A basic data sheet is attached.

PART VI - RECOMMENDATION

26. I recommend that the Executive Directors approve the proposed loan and the credit.

Robert S. McNamara
President

Attachments
May 18, 1971

TUNISIA

BASIC DATA

Area	164,000 square kilometers 63,380 square miles	
Population (mid-1970 estimate)	5.1 million	
Annual Rate of Growth (1965-1970)	2.8 percent	
Density	31.0 per km^2	
Gross Domestic Product (1970) 1/	D 565.1 million	
Per Capita (1970) 1/	US$ 211	
Annual Rate of Growth (1965-1970) 2/	0.6 percent per capita	

Industrial Origin of GDP (1966 prices)	Annual Growth 1965-1970 (%) 2/	Percent Shares 1970
Agriculture	-3.9	14.9
Mining, Water and Power	18.6	8.9
Manufacturing	5.1	15.3
Construction and Public Works	2.0	8.7
Transport and Communications	1.3	8.3
Services	2.7	25.5
Government Wages and Salaries	7.4	18.4
GDP at Factor Cost	3.4	100.0
Expenditure on GDP (Current Prices)		
Private Consumption	3.9	63.8
Public Consumption	10.6	19.9
Gross Investment	1.2	22.2
Exports on Goods and NFS	8.7	22.7
less: Imports of Goods and NFS	2.2	-28.6
Expenditure on GDP	5.9	100.0
Gross Domestic Savings	9.8	16.3
Resource Gap as % of Investment (1970)	26.8	

Money, Credit and Prices	Annual Growth 1965-1970 (%)	End-1970 (D. million)
Money Supply	9.0	198.8
Time and Saving Deposits	11.7	56.0
Bank Credit to Government, Net	2.9	91.1
Bank Credit to non-Government Sectors	12.5	271.6
Consumer Price Index (1962 = 100)	2.9	134.7
Wholesale Price Index (1962 = 100)	3.1	148.0

General Government Operations	Annual Growth 1965-1970 (%)	1970 (D. million)
Current Revenue	9.8	196.1
Current Expenditure	11.2	173.8
Current surplus		22.3
Gross Fixed Capital Formation	-0.7	45.7
Other Capital Expenditure	6.8	24.9
Overall Deficit	2.2	48.3
Domestic Financing, Net	-22.0	3.0
External Financing, Net	6.6	45.3

Balance of Payments		
Exports of Goods and Services	-10.2	171.4
Imports of Goods and Services	4.2	229.4
Current Account Deficit		-58.0
Net Public Capital		50.8
Net Private Capital		14.2
Change in Reserves		-7.0
Net Foreign Assets (end-1970)	-0.6	

External Debt	1970
Public Debt outstanding at Year's End ($ million)	760.0
Debt Service Ratio (%)	22

IMF Position (US$ million)	December 31, 1970
Quota	35.0
Drawings outstanding	19.5

Bank/IDA Position (US$ million)	
Bank loans (less cancellations)	70.1
Repayments	2.3
Total loans outstanding	67.8
IDA credits (less cancellations)	40.0
Total Bank/IDA	107.8
of which disbursed	44.4
undisbursed	63.4

Rate of exchange: 1 US$ = 0.525 Dinar (D)

1/ At current factor cost and at the official rate of exchange.

2/ 1970 compared to 3-year averages centered on 1965 to remove the effect of exceptionally good weather on agriculture in 1965.

May 18, 1971