

focusing their attention on strategies to achieve higher and more persistent growth rates (7-8 percent) compared to the past five year average rate of 5 percent p.a., as a means of addressing the employment issue.

4. Stabilization and structural adjustment: 1987-89. Along with stabilization measures the on-going structural adjustment program was initiated in 1986/1987 with the aim of orienting the economy outward and relying increasingly on the private sector. The Bank has supported this program with a series of adjustment loans and the IMF with a Stand-by and an Extended Arrangement, both of which were successfully concluded. The authorities recognized that the future of Tunisia, with its small domestic market and diminishing oil earnings, would depend on its export performance and that, tourism apart, little of the domestic economy could compete internationally. Although the "off-shore" sector had caused exports to grow fast, it did not stimulate efficiency and innovation in the economy as exports normally do, because it used almost no domestic inputs, beyond labor and non-tradable goods and services. Other potential inputs are mostly not yet competitive internationally.

5. From the start the adjustment process had a wide span. The requirements of prior authorizations for investment and bank loans were dropped and a medium term program of liberalization of trade and prices was begun; interest rates on bank loans were largely freed; antiquated and distortionary taxes were replaced by a VAT on production and wholesale (except foodstuffs and agriculture) and the corporate income tax rate was reduced to a maximum rate of 35 percent; and a number of agricultural prices, including producer prices of cereals, were aligned with international market prices. A privatization program was started and the State began to withdraw from a number of activities, notably in agriculture.

6. These measures were quickly accompanied by a robust economic performance. Despite droughts in 1988 and 1989, GDP growth remained positive, whereas previously droughts had normally caused GDP to fall. The average annual growth for the period was 3.5 percent. In 1980-86 it had been 3.8 percent. Especially successful was the export performance; non-oil exports grew at an annual average of 14.7 percent in volume, as compared to 5.4 percent in 1980-86. The deficit on current account of the balance of payments fell, as a consequence of this and of stringent demand management, to an average of 1.1 percent of GDP, as compared to 7.9 percent for 1980-86, while the budget deficit fell to 3.5 percent as compared to 8.6 percent.