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# Tunisia's Lost Five Decades:

# Government Chronic Failures and Need for Action

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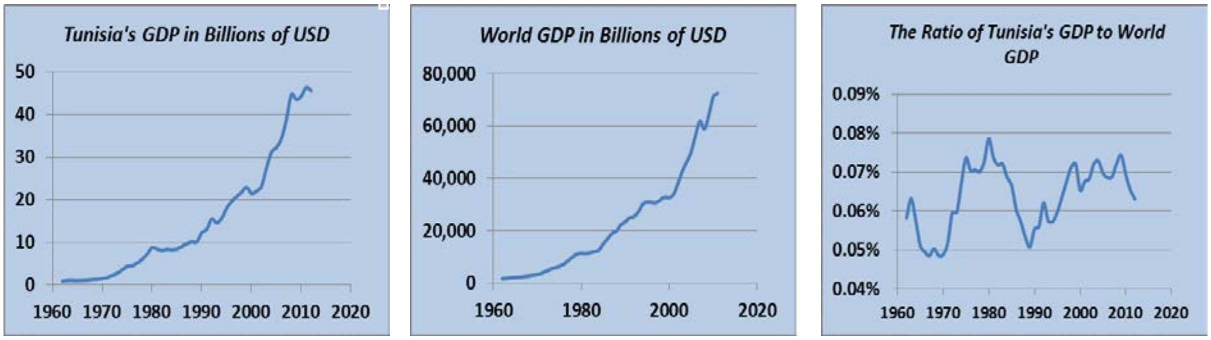
This article studies Tunisia's economic performance in the world stage during the last 50 years. I describe various historical weaknesses and provide policy recommendations in order to alleviate hurdles, break the cycle of chronic mediocrity, and insure the brighter future I believe we are capable of achieving as a nation. I show that Tunisia's share of world GDP has not changed in the last 50 years, leading to what I refer to as "the Lost Five Decades." The Tunisian dinar (TND) has been continuously devaluating during this period reducing the purchasing power of every Tunisian. I explain how to achieve the critical goal of a stable and strong currency through policies that attract foreign direct investments and insure trade surpluses. Such outcomes would bring in much needed reserves that help further manage and support the TND. Along the way, I rely on the success stories of Singapore, South Korea, and Indonesia's economies as reference points to compare Tunisia's performance and as guidance for hopefully a much brighter future.

The United States enjoys an exorbitant privilege because of the dollar's reserve status and the de facto world currency (over 60% of world trade is conducted in USD). First, a high demand for the dollar allows the US treasury to issue debt more cheaply. Even more beneficial, recent years show that the US through its quantitative easing program can print huge sums of dollars to support its deficits, while keeping inflation under full control. Through the strength of its currency and its reserve status, the United States can buy anything it desires from the world at basically no cost, except the tiny cost of the paper used to print dollars. China, on the other hand, has gained political influence and has become a major player on world stage, through high growth (a larger stake of world GDP) and stable currency (pegging its currency to the dollar). China's share of world's gross domestic products (GDP) gained from 1.73% in 1993 to 11.36% as of the end of 2012. This gain gave China enormous influence and a status of a major world power.

A simple measure of a national GDP to world GDP goes a long way in determining status in the world stage. Size basically leads to influence. This measure has two components: domestic GDP level and strength of currency. The product of Tunisian gross domestic products and the value of the Tunisian dinar in terms of US dollars equals to the value of the Tunisian GDP in dollar terms. A high GDP growth that is associated with an even higher currency devaluation lead to a lower purchasing power and a weaker position in the world stage. I first study Tunisia's share of world GDP during the last five decades. Then, I provide the reasons that lead to the underperformance and list various policies that I recommend going forward.

Graph I shows Tunisia's GDP in billions of US dollars (USD), the world GDP in billions of USD, the ratio of Tunisia's GDP to world GDP, for the last 50 years. The annual GDP data is provided by the World Bank and extends from 1962 until the end of 2012. Few years after Tunisia's independence, Tunisia's share of the world economy was approximately 0.06%. Fifty years later, the country's economy continues to represent around 0.06% of the world economy. Sadly enough, today our economy's share is even lower than the 0.08% level we achieved back in 1981. In my opinion, Tunisia has experienced "The Lost Five Decades!"

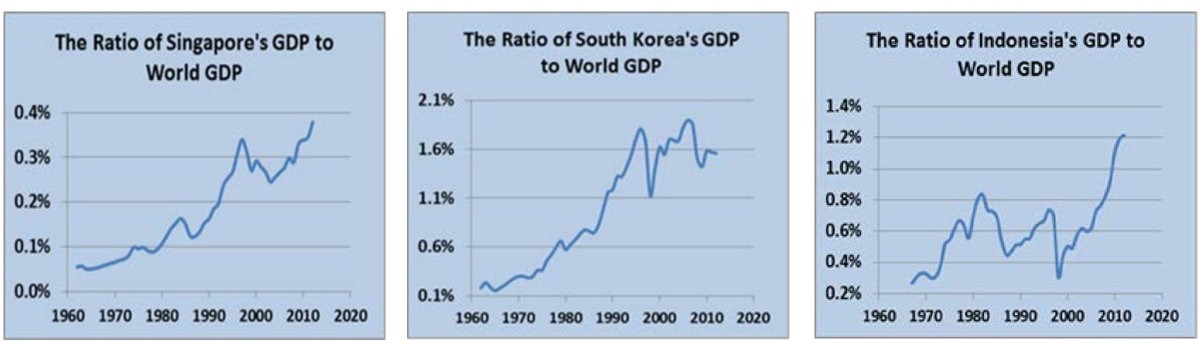
**Graph I: Tunisia's "Lost Five Decades"**




In this section, I compare Tunisia's performance to Singapore, South Korea, and Indonesia. I pick these three countries due to their success stories and because they are more comparable to Tunisia. The BRIC countries, which represent Brazil, Russia, India, and China, might have achieved even more success in recent years. However, they are too large in terms of population and area to be compared to Tunisia. In addition, countries such as Russia and Brazil have significant natural resources such as mineral resources and oil products. Similar to Tunisia, Singapore and South Korea lack the natural resources. Indonesia is a Muslim country and thus can be arguably closer to Tunisia in terms of religion and culture.

Singapore, South Korea, and Indonesia are great examples of countries that have been able to climb the ladder and raise their status in the world stage. Singapore, with half of Tunisia's population, had a lower ratio of GDP to world GDP in 1962 than Tunisia. However, its share of world GDP is more than 6 times Tunisia's share as of the end of 2012 (see Graph II). South Korea's share climbed from 0.18% to 1.56% of world GDP between 1962 and 2012. Indonesia quadrupled its stake of world GDP in the last 15 years. The Tunisian government has a lot to learn

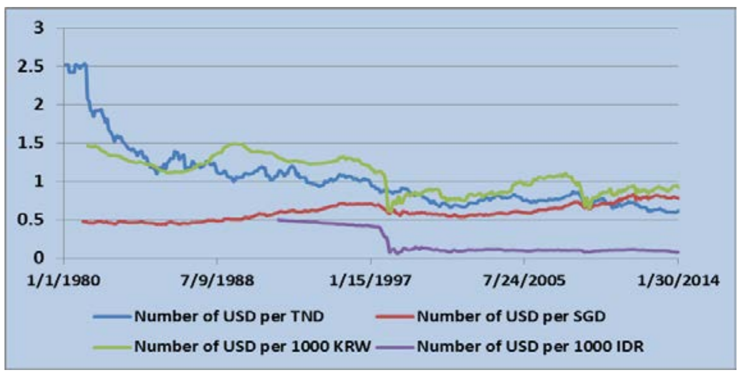
**Graph II: Great Examples to Follow**




from the policies implemented by Singapore, South Korea, and Indonesia's governments. As I will show later, these three countries have been able to achieve their success stories through strong and stable currencies, strong international trade surpluses, and disciplined fiscal policies. On all these three interconnected dimensions, the Tunisian government has failed drastically.

Supporting a strong and stable currency is critical for the success of an economy, given the current international monetary system. Over the long term, a strong Tunisian dinar increases the purchasing power and the well being of every Tunisian and ultimately raises our stake and our position in the global stage. During recessionary periods, allowing the dinar to devalue can be helpful. A weaker dinar makes Tunisian products cheaper abroad and thus helps the competitiveness of our export industries. This temporary increase in competitiveness would encourage export companies to hire more employees to meet the increased demand for the cheaper domestic products and thus support growth and provide a temporary relief. However, a policy of devaluation should only be used during difficult recessionary periods. An export industry should be strengthened by innovation and creation of more competitive products, not by artificially making products cheaper through a continuously devaluation of currency. Devaluation of a currency as the only mean of increasing competitiveness of the domestic

**Graph III: Currency Performance and Stability**

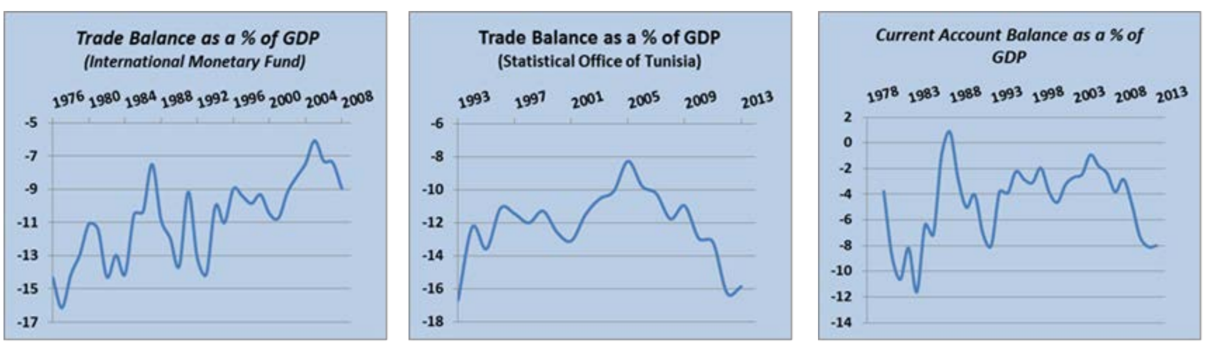



industries is a dangerous policy that does not solve the root problem. Graph III shows how the Tunisian Dinar (TND) has been on a continuous steady decline since the 1980’s. In 1980, 2.5 USD were needed to buy 1 TND, now it only takes 0.6 USD to buy 1 TND. Contrary to this, the plot shows the Singapore dollar (SGD) has been very stable since at least the 1980’s. The Singapore government has been very successful at managing and pegging the SGD to the USD, allowing for very little fluctuation. This policy protects the purchasing power of Singaporeans in the world and builds international investors’ confidence, who face very little currency risk investing in Singapore. Such confidence leads to increased foreign direct investments (FDI). The resulted capital inflows further strengthen the currency and raise the amount of reserves the government is able to accumulate in order to support and manage the currency. South Korea and Indonesia have also relied on managed floating currency regimes. Graph III shows that their currencies are often stable and are only allowed or forced to devalue during significant economic shocks such as the 1997 Asian’s financial crisis that started in Thailand and quickly spread across the region due to contagion.

Avoiding the dangers of chronic currency weakness and instability requires the right set of policies. First, a transparent and stable business environment is required to encourage domestic entrepreneurship and attract foreign investments. The historical widespread corruption and administrative bureaucracies in Tunisia can no longer be tolerated. Strong laws have to be in place to prosecute and punish corruption. Furthermore, strong monitoring of government employees and the right incentives must be set in place to deal with bureaucracy that hinders and discourages entrepreneurs and investors.

Furthermore, a strong trade balance, which is the difference between exports and imports, is crucial to support a strong currency. Exports bring in foreign reserves, while imports spend them. Maintaining a high level of reserves allow the government to support the currency by buying dinars in the open market when there is downward pressure. The ability to support a currency through a high level of reserves, gives foreign investors needed confidence to invest in Tunisia since it reduces currency risk and protects their investments from devaluation. Based on the numbers reported by the International Monetary Fund (IMF) as shown in graph IV, the Tunisian Trade balance, is chronically negative. The deficit ranged between -16% and -6% of GDP during the 1976 to 2008 period. The IMF stopped reporting these numbers as of 2008. The middle plot in graph IV shows the deficit numbers reported by the Statistical Office of Tunisia. The trade balance was approximately -16% of GDP as of 1993, improving to -8% in 2005, and then dropping sharply toward -16% as of the end of 2013. The third plot shows the current account balance, which is the sum of trade balance, factor income (earnings on foreign

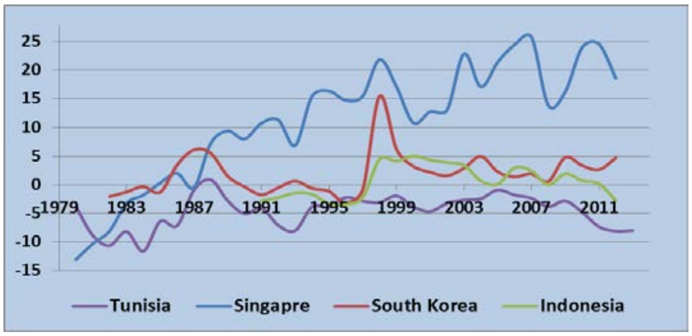
**Graph IV: Tunisia's Never Ending Cycle of Trade and Current Account Deficits**




investments minus payments made to foreign investors) and cash transfers. The Current account deficit is slightly lower than the trade deficit mainly due to the cash transfers by the million or so Tunisians that work abroad. Graph V shows that Tunisia's current account balance has been much weaker than that of Singapore, South Korea, and Indonesia since at least 1980. Singapore had by far the strongest current account balance, followed by South Korea, then Indonesia.

Setting in place the right policies that insure a trade surplus is a must in order to achieve a stable and strong currency. Exports help growth by encouraging new production and investments and help bring much needed currency reserves, which allow the central bank to support and manage the TND. The Tunisian governments needs to create programs that provide incentives to diversify exports, reduce dependence on sales of raw materials and promote knowledge-based high-tech industries. Export subsidies such as tax reliefs for exporters, direct payments, low cost loans, tariffs that protect local industry, export marketing, and investment assistance schemes, as well as targeting capital exports and

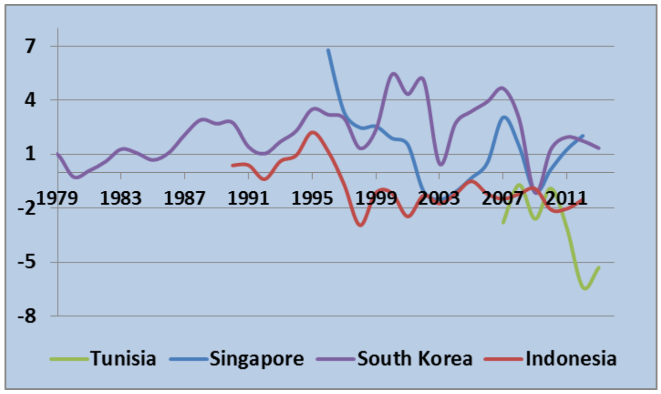
**Graph V: Current Accounts as a % of GDP**




support for technology development through research grants are some of the few policies that need to be undertaken and expanded. Furthermore, imports have to be restricted until a domestic industry is developed. Tunisian companies cannot compete at this stage with cheap Chinese and Indian basic products, cheap electronics from South Korea, and more competitive high tech products from Europe. Opening the Tunisian market to foreign competition destroys our existing infant industries and provides no space for new industries to develop.

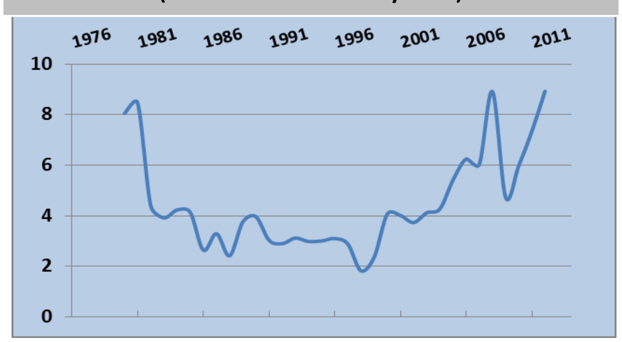
Based on data from Bloomberg, Graph VI shows budged balances as a percentage of GDP for Tunisia, Singapore, South Korea, and Indonesia. The data for Tunisia is only available since 2007. Again, Tunisia falls behind our comparable countries in this measure. Moreover, Tunisia's budget deficit increases to dangerous levels in 2002 and 2003. The Tunisian government has to practice sound fiscal policy. Clear rules have to be in place to control government spending. Moreover, Spending has to be countercyclical in nature, where budget deficits are only allowed during recessionary periods. During recessions, government spending can help speed up the rate of growth in the economy. Strong rules

**Graph VI: Budget Balance as a % of GDP**




have to be in place to stop wasteful spending that relies on debt. Most importantly, the government needs to reduce and work toward eliminating all debt from international organizations such as the International Monetary Funds (IMF), the European Investment Bank (EIB), and the European Bank for Reconstruction and Development (EBRD) no matter what. Through their loans to Tunisia, these organizations yield great power to influence projects and policies that benefit their European and American shareholders rather than the development of Tunisia. These organizations provide loans under strong conditions that I believe hurt the domestic industry. They require Tunisia to open its market to foreign goods that benefit foreign companies, remove any export subsidies and protection of infant industries. Infant industries are more likely incapable to compete against large global firms and as a result end up dying out. Such policies lead to further dependence on imports and the continuous deterioration of the balance of trade, which ultimately leads to an even weaker Dinar. A complete free trade policy is as dangerous as isolationism or full protectionism. Providing some level of temporary protection to the domestic infant industries in order to have the time to build a competitive advantage without the constant threat of annihilation by more powerful foreign entities is a necessary requirement for the development of the nation.

**Graph VII: Oil Imports as a % of GDP**
**(International Monetary Fund)**



Last, Tunisia needs to find a way to reduce its dependence on oil in order to reduce imports and improve its balance of trade. Since 1980, Tunisia has spent between 2% and 8% of its GDP per year for oil imports (see graph VII). First, the volatility of oil imports needs to be curbed by sound hedging techniques. It is shocking to see how sensitive our imports are to oil price movements. Between 2008 and 2012, oil imports fluctuated drastically between 4% and 8% of GDP. Such huge fluctuation hurts the government ability to budge properly and can easily be avoided by hedging oil needs through future or option markets. It is encouraging to see recent solar energy production projects that are being developed. However, such projects are relying on European companies. Tunisian youth have the education and intelligence to learn such technologies and build our home-built solar energy industry. We need to stop relying on foreign companies and rely on our own youth to develop new technologies. That way the entire benefits of such projects would stay in Tunisia and help Tunisians. Politicians would argue that we don't have the resources to develop such expensive technology ourselves. I would disagree and state we simply need to prioritize better and focus all what we have toward value added technologies and products that would welcome Tunisia to the information age. Our Youth have sacrificed to get rid of decades of dictatorships and to earn a free future. It is time to honor that sacrifice and build a foundation for future stability and prosperity.

**Data References:**

| Country | Variable | Bloomberg Ticker | Original Source |
|---|---|---|---|
| World | Gross Domestic Products | WGDPWRLD Index | World Bank |
| Tunisia | Currency Spot | TND Curncy | Bloomberg BGN |
| Tunisia | Current accounts as a % of GDP | ICA%TUN Index | International Monetary Fund |
| Tunisia | Government Budge balance | UBALTUNI Index | International Monetary Fund |
| Tunisia | Gross Domestic Products | WGDPTUNI Index | World Bank |
| Tunisia | Trade Balance | TNTBAL Index | Statistical Office of Tunisia |
| Tunisia | Value of Oil Imports | VAOITUN Index | International Monetary Fund |
| South Korea | Currency Spot | KRW Curncy | Bloomberg BGN |
| South Korea | Current accounts as a % of GDP | EHCAKRY Index | Bloomberg Indices |
| South Korea | Government Budge balance | EHBBKRY Index | Bloomberg Indices |
| South Korea | Gross Domestic Products | WGDPKORE Index | World Bank |
| Singapore | Currency Spot | SGD Curncy | Bloomberg BGN |
| Singapore | Current accounts as a % of GDP | EHCASGY Index | Bloomberg Indices |
| Singapore | Government Budge balance | EHBBSG Index | Bloomberg Indices |
| Singapore | Gross Domestic Products | WGDPSING Index | World Bank |
| Indonesia | Currency Spot | IDR Curncy | Bloomberg BGN |
| Indonesia | Current accounts as a % of GDP | EHCAID Index | Bloomberg Indices |
| Indonesia | Government Budge balance | EHBBIDY Index | Bloomberg Indices |
| Indonesia | Gross Domestic Products | WGDPINDO Index | World Bank |