BANQUE CENTRALE DE TUNISIE

GENERAL DIRECTORATE OF STUDIES AND RESEARCH

UNEVEN GROWTH PROSPECTS

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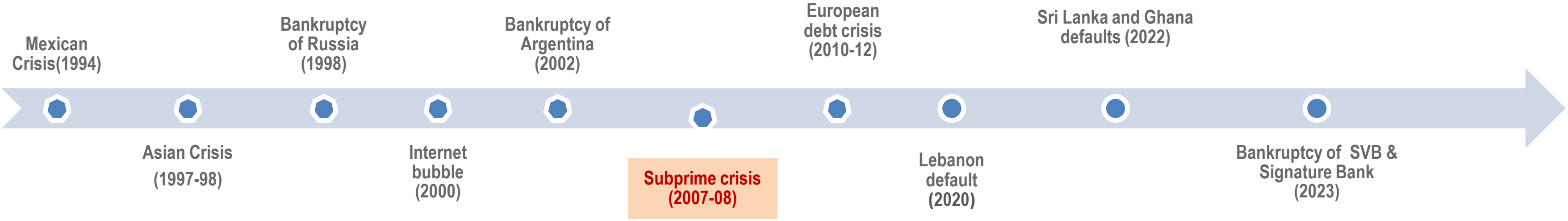
HISTORICAL OVERVIEW AND CURRENT CONTEXT

DATING OF RECENT CRISES



CURRENT CONTEXT: INCREASE IN THE FRAGILITY OF EMERGING MARKETS

1. High level of international energy and food prices;
2. End of an accommodating cycle of monetary policies;
3. Growing macroeconomic imbalances and particularly a widening of the twin deficits and a sharp increase of debt levels of several middle and low incomes countries;
4. Alarming increase in the debt levels of emerging countries in relation to the frequency of shocks such as the COVID crisis, the Ukraine war, climate changes, political transitions …
5. Difficult and more costly access of middle and low incomes countries to financial market and bilateral finance.

Types and Main Causes of Financial Crisis

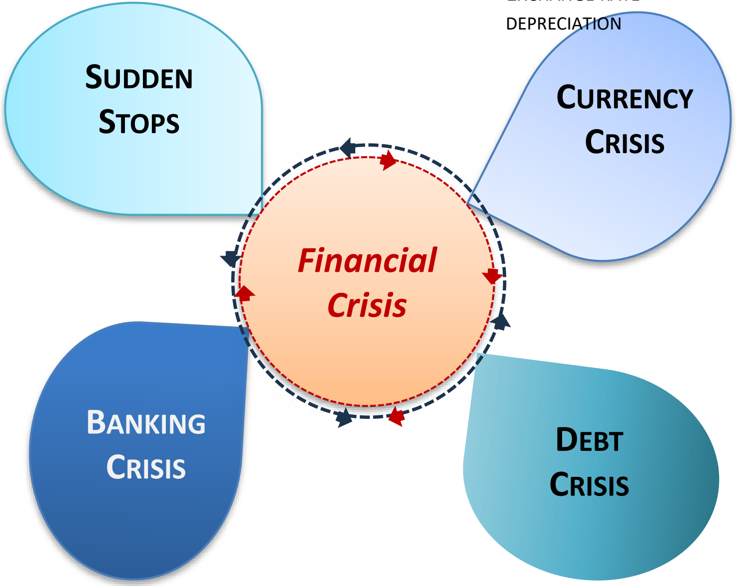
Sudden slowdown in private capital inflows into emerging market economies. Sudden stops are usually followed by a sharp decrease in output, private spending and credit to the private sector, and real exchange rate depreciation.

Sharp MP Tightening

- Risk of capital outflow
- Decline of capital inflow

- Foreign reserves drop
- Exchange rate depreciation

The massive slowdown in capital inflows, usually presented as large capital outflows, can be counteracted by exchange rate devaluation and loss of international reserves. In these latter cases, currency market turbulence will be reflected in steep increases in domestic interest rates by Central bank.



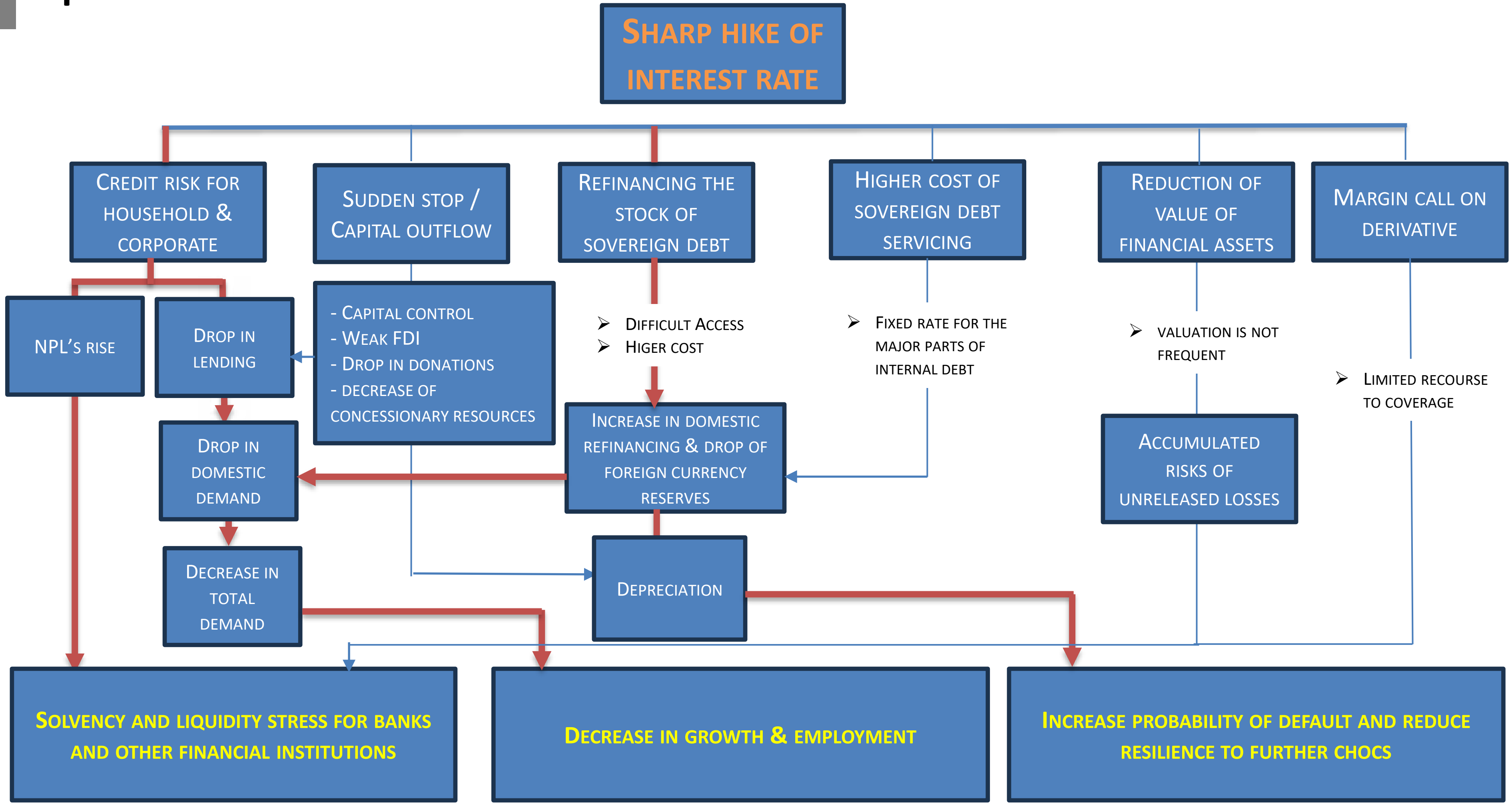
Banking crisis is marked by a bank runs and withdrawals. Often, the banking problems do not arise from the liability side, but from a protracted deterioration in asset quality, be it from a collapse in real estate prices or increased bankruptcies in the nonfinancial sector.

- Drop in quality of assets
- Higer NPL's
- Liquidity risk

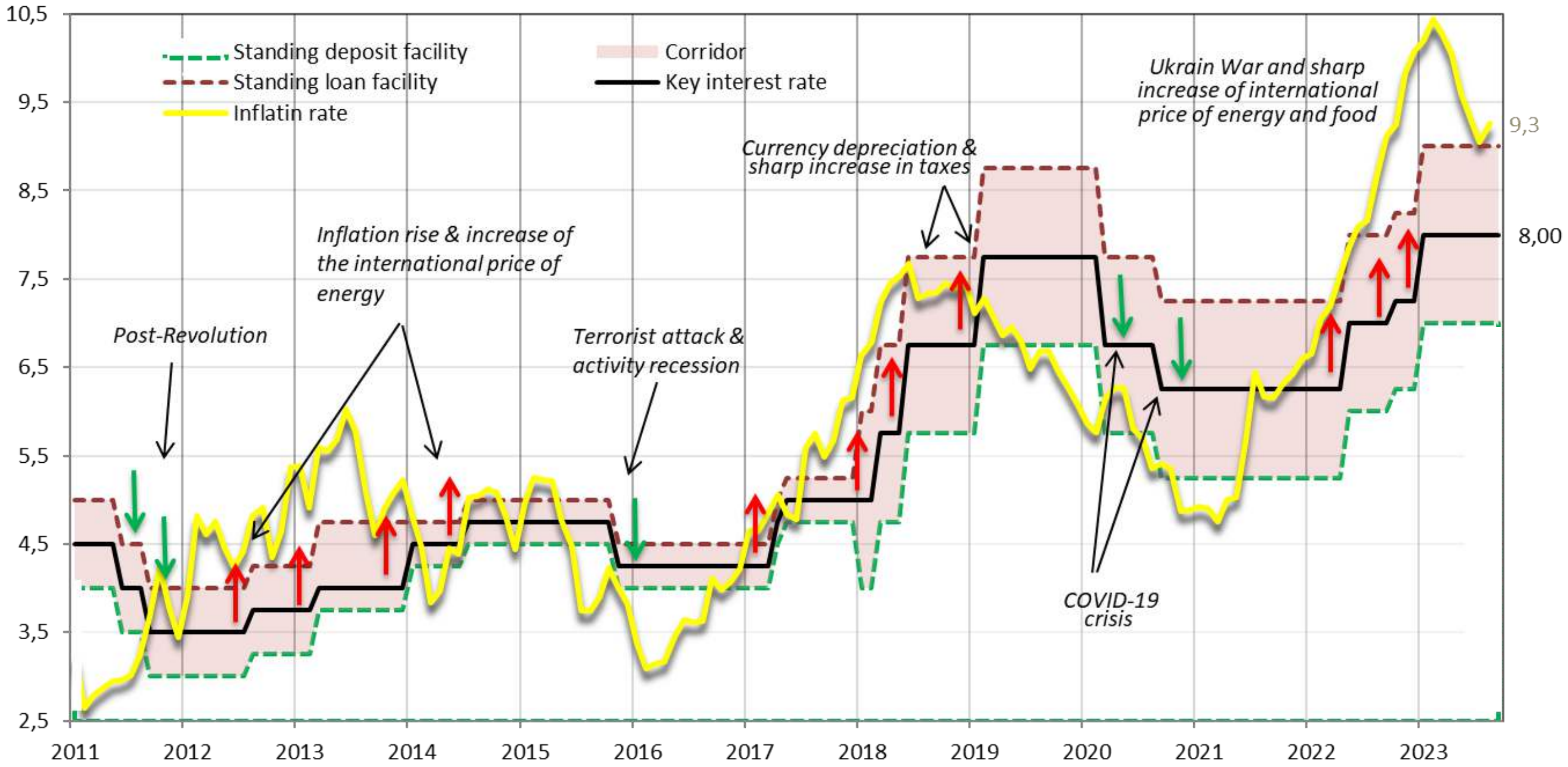
- Increase in cost of debt
- Debt unsustainability

Situation in which a government loses the ability of paying back its governmental debt. When the expenditures of a government are more than its revenues for a prolonged period or if sudden jump in debt levels occurs driven by large exchange rate depreciations or a sharp drop in external (public/private) resources flows.

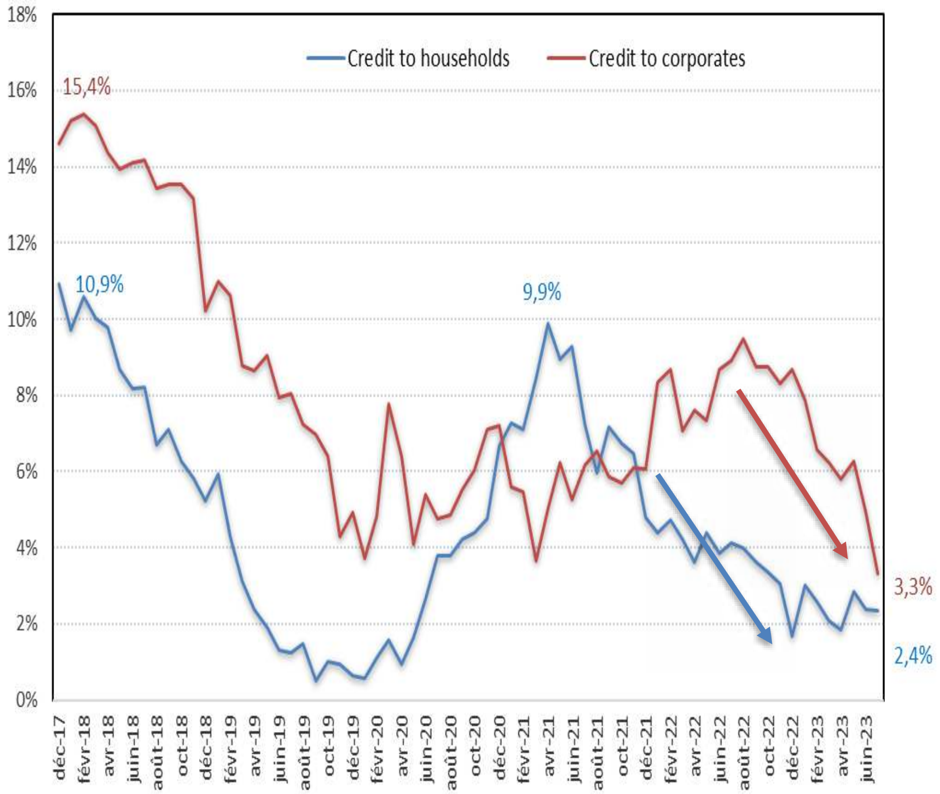
Spillover effects

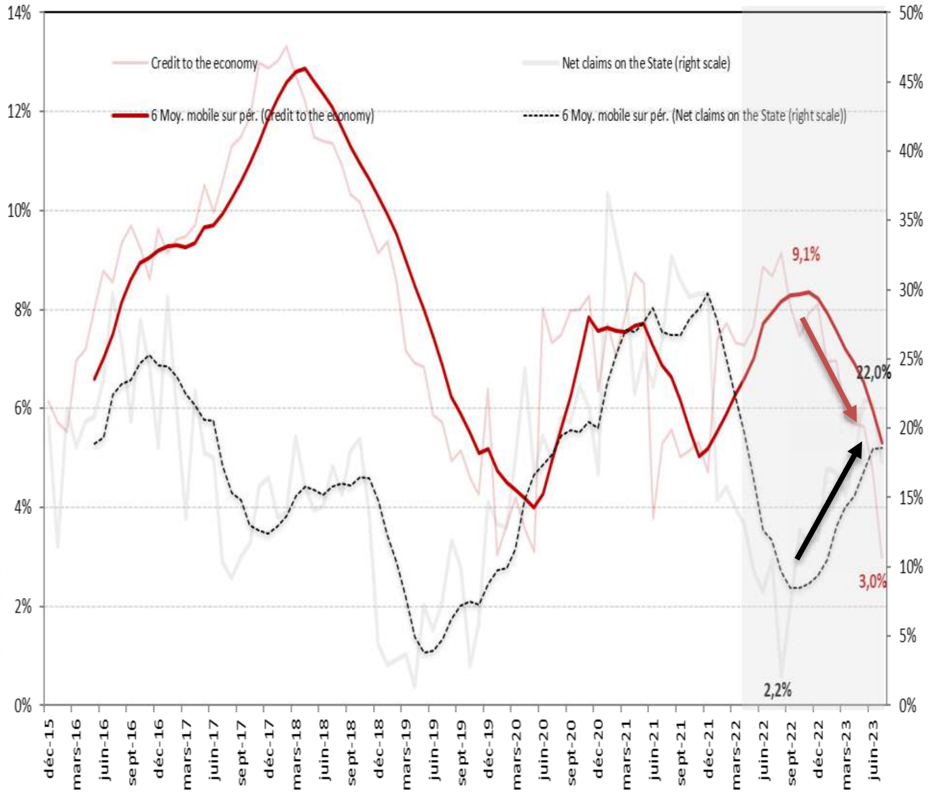


CBT monetary policy conduct



Drop in credits & crowding-out effect





Tunisian policies to mitigate financial crises

- <u>Capital market not totally liberalized</u>:

Tunisian authorities had maintained a relatively closed capital account by retaining tight controls on capital flows presumably provide significant protection against international financial crises compared to whose capital markets were more open. Maintaining such controls over a prolonged period, however, impairs a country's ability to take advantage of the efficiency gains from broader participation in the global financial system. It is for this reason that the authorities are currently moving towards introducing more flexibility and opening of the capital account through a project to reform the exchange code, but before that an effort to strengthen the framework to contain the risks was carried out.

- <u>Orientation towards inflation targeting regime</u>

Orientation towards the adoption of an inflation targeting regime (a strategic project for the CBT) and adoption of a more flexible management of the exchange rate through the minimization of the intervention of the CBT in the FX market to improve the transparency of the central banks and help to anchor inflation expectations.

- <u>Regulatory and institutional framework for macroprudential policy:</u>

The law 2016-35 Assigns the CBT a mission to contribute to macroprudential policy to prevent and mitigate systemic risk also it *created a Macroprudential Surveillance and Financial Crisis Management Committee*. This Committee is responsible for issuing recommendations on the measures that financial sector regulatory authorities should adopt and implement in order to contribute to financial stability.

TUNISIAN MACRO-PRUDENTIAL FRAMEWORK TO MITIGATE FINANCIAL CRISES

- **MACROPRUDENTIAL SUPERVISION PROCESS:**

Intermediate objective-based monitoring is based on a series of key indicators that serve five intermediate objectives; 1- Mitigate and prevent excessive expansion of credit and debt 2- Mitigate and prevent excessive transformation of maturity and liquidity 3- Limit the concentration of direct and indirect exposures and reduce moral hazard 4- Strengthen the resilience of the financial sector and 5- Limit the impact of macroeconomic risks on the financial sector.

- **MONITORING SOURCES OF SYSTEMIC RISK:**

The CBT carries out an assessment of the sources of risks that could affect the stability of the financial sector through a set of instruments: 1- A dashboard composed of a set of quantitative and qualitative indicators making it possible to monitor and measure the evolution of risks; 2- An aggregate index of financial stability; 3- Stress test exercises which have been conducted on the largest banks; 4- A list of early warning indicators to identify rising vulnerabilities.

- **IMPLEMENTATION OF SAFETY NETS:**

The presence of safety nets (Lender of last resort mechanism; Resolution mechanism for banks and financial institutions in difficulty and Bank Deposit Guarantee Fund) helps protect the financial system from the possible materialization of systemic risk.