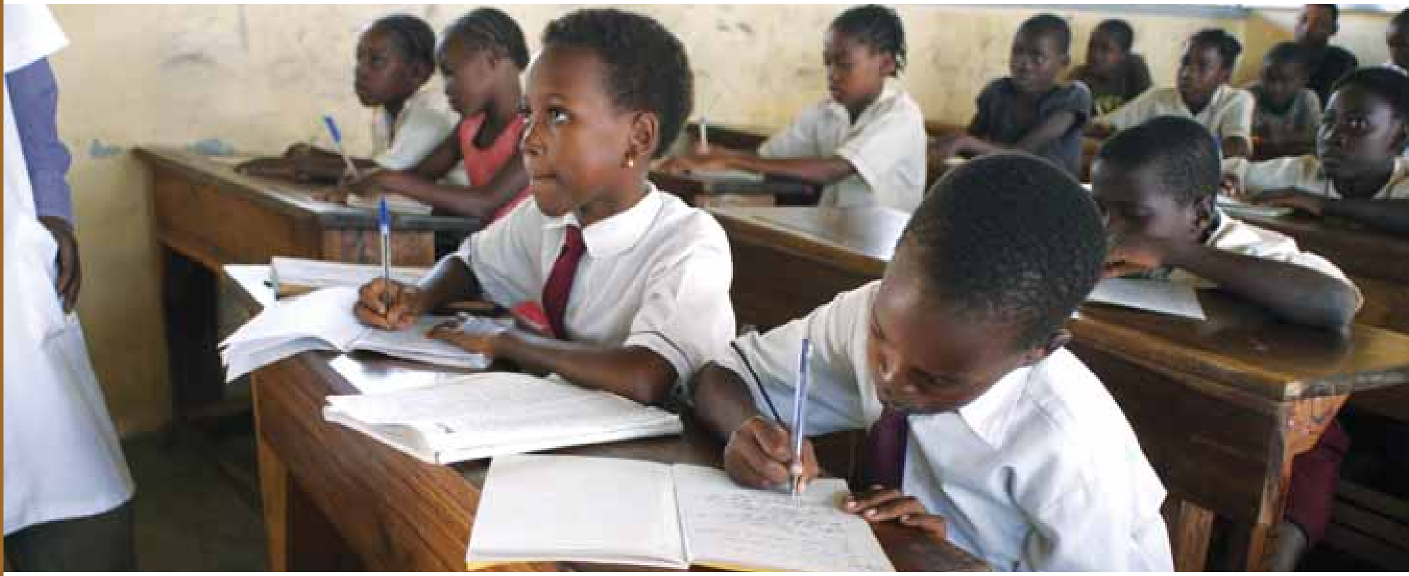
Tanzania Economic Update
Stairways to Heaven

Fiscal Prudence, Value for Money in Education, Economic Transformation of Firms



THE WORLD BANK

THE WORLD BANK GROUP AFRICA REGION POVERTY REDUCTION & ECONOMIC MANAGEMENT

February 2012

ISSUE I

Public Disclosure Authorized
Public Disclosure Authorized
Public Disclosure Authorized
Public Disclosure Authorized

Table of Contents

LIST OF TABLES

LIST OF FIGURES

Foreword

The World Bank Office in Tanzania is pleased to launch the *Tanzania Economic Update,* which will be published biannually. This first edition addresses issues related to inclusive growth, outlining a series of policy recommendations that suggest how such growth might be achieved.

In particular, it focuses on how efficiency gains in the education sector might be achieved and how structural changes are required to support the activities of the private sector.

The publication of economic reports of this nature constitutes an important aspect of the World Bank's analytical program in a number of client countries, including Kenya, Rwanda, and South Africa. Such reports aim at fostering a constructive policy dialogue between stakeholders and policymakers and to stimulate debate on essential economic issues.

The Tanzania Economic Update has two primary objectives. The first objective is to offer a perspective on the recent economic developments, with a particular examination of the interplay between global and domestic trends. The second objective is to conduct an examination of topics of special interest and high relevance to the country. In these turbulent times, Tanzania has one of the fastest growing economies in the world, with a growth in GDP of 6.5 percent in 2010/11.

However, fiscal and monetary prudence is vital in the management of potential external and domestic risks. After three years of an intensive fiscal stimulus program, fiscal buffers have now been exhausted.

Any slippage could result in a rapid decline into macroeconomic instability, as occurred in the second half of 2011, when Tanzania experienced high inflation and exchange rate volatility.

If economic growth cannot be achieved through fiscal expansion, the policy emphasis needs to shift to longer term structural issues. For Tanzania, addressing these structural issues involves the more efficient use of public resources, particularly in the areas of social services.

The authorities need to ensure a higher degree of cost efficiency in the delivery of education services. If they do not achieve this, they will be not able to respond to the challenge posed by the massive arrival of new students in secondary schools over the next decade.

The Economic Update aims at fostering a constructive dialogue between stakeholders and policymakers

The crucial challenges associated with structural changes in the private sector, such as the emergence of small informal firms and manufactured exports, are covered in this inaugural issue. We hope that this Economic Update will contribute to the national debate on an important topic and help shape informed policy decisions for sustainable and equitable development in Tanzania.

Mercy Miyang Tembon
Acting Country Director
for Tanzania, Uganda and Burundi
The World Bank

Acknowledgement

This first edition of the Tanzania Economic Update was prepared by Jacques Morisset and Stevan Lee. The authors acknowledge the contributions of Emmanuel A. Mungunasi, Josaphat Kweka, Goodluck Mosha, and Yutaka Yoshino.

The report benefited from the insights of several peer reviewers, including Wolfgang Fengler, Zeljko Bogetic, and Sarwat Husain, as well as from the comments shared by David Rohrbach, Barjor Mehta, and Arun Joshi.

The team received guidance from J. Humberto Lopez and Mercy Tembon. Irfan Kortschak edited the report, while Agnes Mganga and Mwanaisha Kassanga provided invaluable assistance during its preparation.

Key Messages

- ***Among the best performers***

Tanzania's GDP growth in the last 12 years has been extremely strong, averaging close to 7 percent annually. This rate is high, but still lower than that of successful emerging countries when the nation's high population growth rate of about 3 percent is factored into the equation. Economic growth has failed to eradicate poverty, with one third of households still living below the poverty line. If Tanzania aims to reduce the income gap between itself and middle income countries, it will have to grow faster and better.

Tanzania's economy was highly resilient to the global financial crisis of 2008/9. This resilience was largely due to its relative isolation from international markets, favorable events, and the relatively large fiscal stimulus package launched by the Government. The problem is that the stimulus package, which was rightly intended to be a temporary response to global economic conditions, became permanent. This resulted in a deterioration of the fiscal situation. The level of concern increased when the budget deficit, after grants, reached 6.9 percent of GDP and the debt level exceeded 40 percent of GDP by mid-2011.

In response, the Government announced measures to limit and reduce the budget deficit to begin in late 2011. Spending will be cut by approximately one percent of GDP, while taxes will increase. Concurrently, the Central Bank of Tanzania has tightened its monetary policy, raising interest rates to control a rate of inflation that reached close to 20 percent at the end of 2011.

- ***Positive outlook in a dangerous world***

Tanzania's rate of economic growth is forecast at approximately six percent in 2011/2012, with falling inflation. In the current global economic context, this could be considered very good. In addition, growth is expected to accelerate in 2012/13. However, it would also be the slowest rate of growth for the Tanzanian economy since 2000. The explanations for the lower rate of growth are the slowest fiscal expansion, non–accommodating monetary policy, and the costs associated with the ongoing energy crisis. This slowdown was already demonstrated in the third quarter of 2011 when GDP grew by 6.4 percent, down from 6.7 percent in 2010. This is the third slowest quarterly increase since 2002.

Despite the positive forecast, risks threaten Tanzania. While in the past, the Tanzanian economy has shown itself to

If Tanzania aims to reduce the income gap between itself and middle income countries, it will have grow faster and better be resilient to global downturns, this may not hold into the future, as any new global downturn may be qualitatively different from previous experiences. In addition, climatic catastrophes (such as the recent floods in Dar es Salaam) or unexpected costs associated with the emergency energy program and road contracts, may result in increased fiscal pressure.

In case of new shocks, the Government may have no options except adherence to fiscal discipline and prudence. Any deviation from these principles is likely to result in higher inflation and interest rates, possibly destabilizing the current macroeconomic framework. Poor households and businesses would suffer the most.

- ***The quest for new drivers of growth***

Much of the growth of the 2000s was driven by fiscal expansion and massive aid inflows. The impact of fiscal expansion has been particularly significant since 2008/9. However, these are unlikely to continue to drive growth to the same extent in the tougher economic climate of the 2010s. Aid may increase more slowly than in the past due to the current fiscal state of many donor nations. Therefore, the Tanzanian Government needs to find new drivers of growth.

This Tanzania Economic Update focuses on the need to transform the education system and to foster growth amongst business enterprises. These are the two vital elements by which Tanzania will achieve accelerated and shared growth. There is a synergistic effect between these two elements, since better educated people are more productive and therefore play a major role in making business enterprises become more competitive. The reverse is also true, since more competitive business enterprises can invest more in human capital. Those synergies are at the heart of economic development.

- ***Getting better value for money in the educational sector***

Education accounts for the largest share of the massive increases in public spending 2000-2011, accounting now for about 20 percent of the total budget. Despite this investment, the education system has not yet succeeded in delivering a large number of graduates. Worse, the pass rates in primary and secondary schools have actually declined since 2007.

The major challenges in the educational sector are limited resources and fast-growing school populations. Fiscal conditions will severely limit the potential for growth in expenditure on education in coming years. However, the student population is increasing rapidly, growing by more than 30 percent per year at secondary school. It is difficult or impossible for the government to control this population growth.

International experience shows that a number of steps can be taken to improve the efficiency of the educational system. Evidence show that in Tanzania these include (i) a better regional allocation of financial and human resources; (ii) improvements in teachers' capabilities and in financial management; and (iii) synergies with the private sector and parents.

If economic growth cannot be achieved through fiscal expansion, the policy emphasis needs to shift to longer term structural issues

Small firms have become the fastest growing source of employment

• ***Harnessing the power of economic transformation***

The success of emerging economies in Asia is embedded in their businesses' capacity to transform and adapt over time. Tanzania's small business sector has begun to show incipient signs of similar capacities. The development of these new capacities has been driven by technological improvements. This is indicated by the following: small firms have become the fastest source of employment; manufactured exports have been booming since 2005; options for firms' financing have expanded; and recent initiatives have led to productivity gains in the agricultural sector.

Indications of the transformation of the business sector are encouraging, but the foundations for ongoing growth are not firmly entrenched. The growth of the business sector needs to be supported by smart public policies that emphasize (i) innovation through competition; (ii) training, training, and training, and (iii) diversification of exports. These three areas are self-reinforcing as they should lead to more and better jobs. This is necessary to absorb new entrants on the labor market and reduce poverty levels.

1 The State of the Economy

Part 1

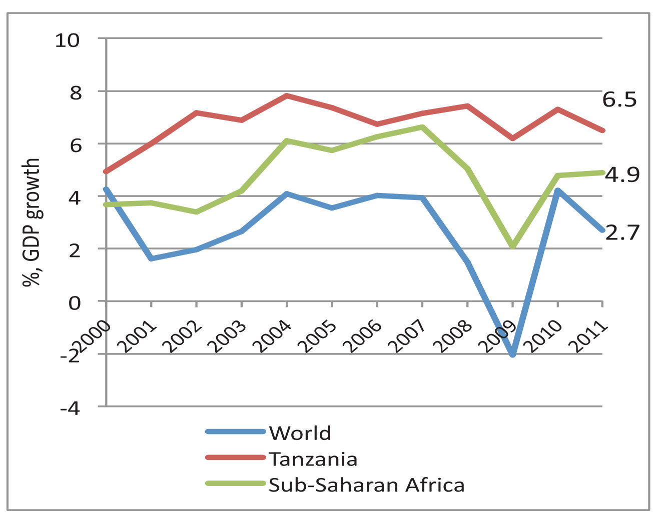
The State of the Economy

Main points

- Tanzania's economy has resisted regional and global turbulence, as GDP is expected to expand around 6 percent in 2011/12.
- Short-term policy options have been exhausted –except for adherence to fiscal prudence and discipline.
- Economic growth will have to come from additional drivers after three years of rapid fiscal expansion.

Following three years of a high rate of economic growth, Tanzania's economy is forecast to grow by approximately six percent in 2012. That rate may appear higher in the current global context, but it would represent the slowest rate of growth in Tanzania since 2000. The challenge for policymakers will be to resist new external and domestic shocks with a drastically reduced fiscal buffer. Looking forward, additional drivers of growth are needed to diversify the economy, to provide more extensive and better social and infrastructure services and to promote job growth and innovation.

Fig.1: Tanzania growth performance tops world and regional standards



Source: World Development Indicators, 2011

1.1 Recent developments up to 2011

Over the past decade, despite global and regional economic turbulence, Tanzania's economy has been one of the fastest-growing in the world. Over the past two years, the GDP grew by 7.3 in 2009/10 and by 6.5 percent in 2010/11 (Figure 1). This rate of growth was achieved largely through the combination of the relative isolation of the domestic economy from external shocks and through effective demand policies.

There are three main reasons to explain Tanzania's resilience in the face of global economic turbulence:

- The domestic economy is relatively isolated from global trade and financial markets: The cumulative GDP ratios of trade and financial flows in Tanzania represent only 60 percent. By comparison, they exceed 100 percent in small, open economies such as Mauritius, Lesotho or Congo Republic.

- The combination of exogenous factors has helped to stabilize the trade and capital accounts: In terms of balance of trade, the increased price of gold is more than compensated for the lower international demand for crops (see Figure 2). At the same time, decreased crude oil prices have reduced the total value of imports. In terms of capital, donors continued to provide financial assistance. The concentration of FDI in the mining sector at least partially explains those flows' resilience during the crisis (Figure 3). As a result, the current account balance remained stable at approximately 10 percent of GDP in 2009 and 2010. The level of international reserves stayed at a comfortable level, equal to the value of approximately 4.5 months of imports.

- Local banks had a low level of international exposure, which limited the risk of financial contagion: The ownership structure of Tanzanian banks kept them at arm's

GDP grew by 7.3 in 2009/10 and by 6.5 percent in 2010/11

Fig. 2: Export earnings up in contrast to the region, 2009-10

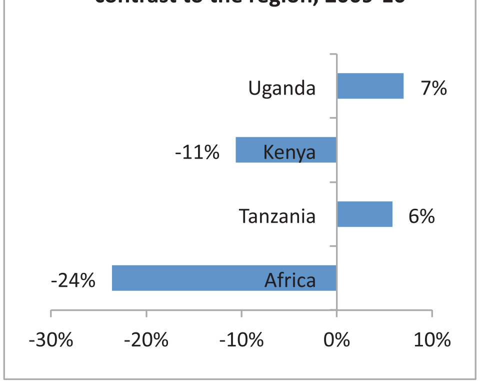
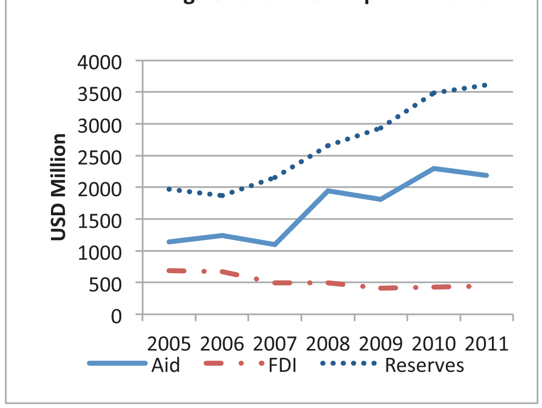


Fig. 3: Sustained capital inflows



Source: World Bank and Ministry of Finance length from international banks. As a result, very few Tanzanian banks have been involved in large-scale international financial transactions. Furthermore, most local banks have managed to remain financially sound, well capitalized[1], and with a low level of non-performing loans.[2]

The fiscal stimulus package first launched by the authorities in early 2009 and implemented throughout 2010 and the first half of 2011 also contributed to economic growth. The ability of the government to launch this fiscal stimulus package was based on the country's strong fiscal position, characterized by a low deficit and a low level of debt. The fiscal stimulus package generated an unprecedented increase in public expenditures, exceeding four percent of GDP between 2007/8 and 2010/11. It also resulted in a concurrent increase in aggregate demand. This increase was concentrated on recurrent spending, which increased by more than 50 percent in real terms during this period. It was also concentrated in a limited number of Ministries, including Foreign Affairs, Finance, Energy, and the Prime Minister's Office.

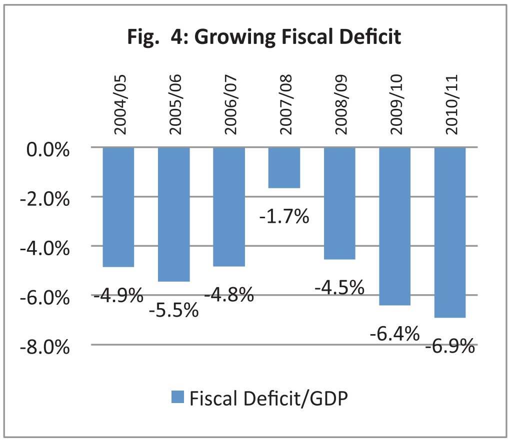
Unfortunately, the cost of three years of fiscal stimulus led to the gradual deterioration of the fiscal balance. The spending drive wa not accompanied by a higher revenue-to-GDP ratio, with this ratio standing at approximately 16 percent because of lower tax rates and additional tax exemptions. This contrasted sharply with the six percentage points of GDP increase recorded between 2000 and 2008. Concurrently, aid inflows have failed to keep pace with the surge in public expenditures. In 2010/11, these inflows actually fell by 11 percent in real terms. The stagnation or decline in aid inflows, combined with ambitious investment plans, has meant that the authorities have had to turn to financial markets for financing for the first time since the early 2000s. In the period between 2008/9 and 2010/11, the government borrowed more than TSh 2,500 billion to close the fiscal gap.

By mid-2011, fiscal indicators demonstrated a disturbing decline:

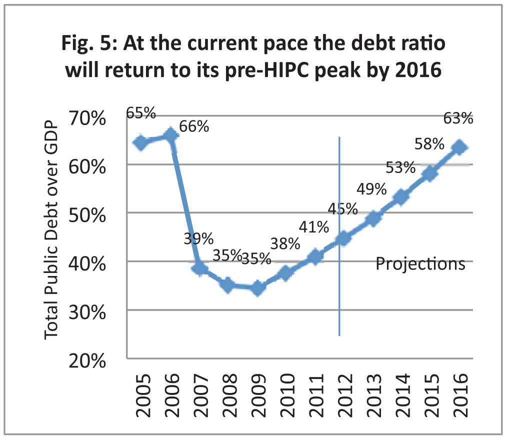
- The fiscal deficit reached a value equal to 6.9 percent of GDP, up from 1.7 percent of GDP in 2007/08 (Figure 4);
- The public debt-to-GDP ratio increased from 35 to more than 40 percent between 2007/8 and 2010/11 (Figure 5).
- Arrears increased substantially (reportedly in the magnitude of TSh400 billion or over 1 percent of GDP in 2010/11 alone), especially in the road sector.
- The share of development spending accounted for approximately one quarter of the executed budget, despite the fact that such expenditure wasabout one third of the initially approved budget. This raises serious concerns regarding the degree to which the budget remained aligned with the nation's priority, especially since only around half of the development budget is considered to be "true" capital investment.

The fiscal stimulus package generated an unprecedented increase in public expenditures, exceeding four percent of GDP between 2007/8 and 2010/11

1 Reporting a ratio of overall capital to risk-weighted assets of 17.4 percent.
2 8 percent of total loans by September 2011.



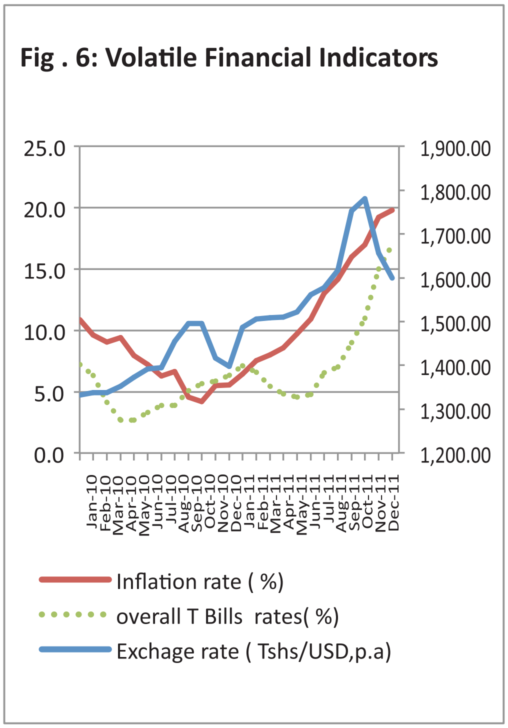
Source: Ministry of Finance and IMF



Note: Projections are based on the fiscal trends observed during 2008-2011.

The deterioration of fiscal accounts was accompanied by increasing volatility on the local financial markets (Figure 6). The inflation rate increased gradually to almost 20 percent by the end of 2011, largely as a result of regional food supply shortages due to droughts and higher fuel prices. The rate of foreign currency exchange fluctuated widely, depreciating by approximately 30 percent between August and October 2011 and then appreciating by about 20 percent between October and December 2011.[3] The T-bills returns reflected the pattern of inflation, booming from four percent in June 2011 to almost 18 percent in December 2011.

This volatility was partly the result of higher fuel and food prices and various other factors, but it was also the consequence of major shifts in fiscal and monetary policies. By November 2011, the Government rightly recognized that its fiscal stimulus was no longer sustainable. The fiscal deficit target for 2011/12 was revised to 6.6 percent of GDP, downwards from 6.9 percent in 2010/11 and the 8 percent initially projected in the 2012 Finance Law. The combination of spending cuts for about one percent of GDP and higher fiscal revenue collection was announced by the authorities as part of the IMF program.



3 The depreciation partly reflected demand for foreign currency to pay oil import bills inflated by high global prices and demand linked to back-up generators operated by businesses and households during load-shedding.

As a result, Foreign and domestic non-concessional borrowing should not exceed 3.1 percent of GDP in 2011/12. This is intended to stabilize the public debt-to-GDP ratio and consequently the Government's level of exposure.

The Central Bank of Tanzania has also tightened its monetary policy by increasing interest rates and deposit requirements. This is intended to reduce monetary expansion and control inflationary pressure. The authorities have succeeded in keeping core inflation (excluding food and energy prices) below 10 percent, preventing any pass through effect from higher food and energy prices to other items.[4] By October, the monetary authorities had also intervened directly in the foreign exchange market, sending the value of the local currency back to its August 2011 level. The level of international reserves declined slightly, but remained at a comfortable level equivalent to the value of approximately four months of imports at the end of 2011.

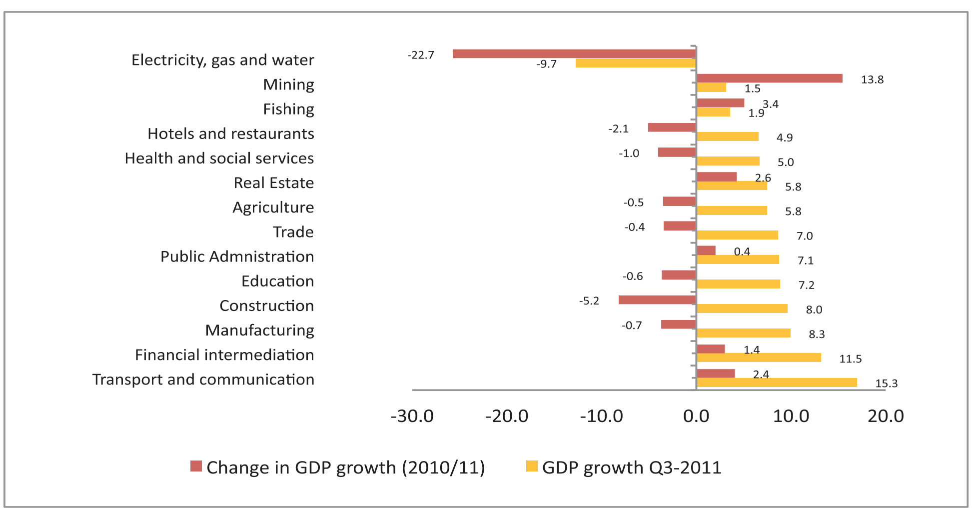
1.2 Economic outlook and short term risks

According to the World Bank's Global Economic Prospects,[5] the Tanzanian economy is expected to continue to expand by approximately 6 percent in 2011/12 (Table 1). While this rate is good, it is lower than the rate recorded last year. In fact, if achieved, it will be the lowest annual rate of growth for the Tanzanian economy for the past nine years. The decline in the rate of growth had already become visible in the third quarter of 2011, when growth stood at 6.4 percent compared to 6.7 percent for the same period in 2010 (Figure 7).

The Tanzanian economy is expected to continue to expand by approximately 6 percent in 2011/12

In particular, electricity, manufacturing, hotels and restaurants have been adversely affected by the energy crisis. Stronger growth was achieved in the mining, fishing, financial and telecommunication

Fig. 7: GDP growth by sectors, June-September 2011



Source: National Bureau of Statistics, 2011

4 This contrasts sharply with Uganda where the core inflation rate surged to close 30 percent in the last quarter of 2011, following the initial path of food and energy prices.

5 Global Economic Prospects 2012, World Bank, January 2012.

sectors. In the remainder of the year, the same sectors are expected to drive economic growth, while agriculture should perform at similar levels as in recent years, assuming good rainfall and favorable harvests in early 2012. In 2012/13, GDP growth is forecast to revert to its longer trend of approximately 7 percent following the projected recovery of developing and world economies.

Table 1: Tanzania macro-performance, 2007-12

	2007/8	2008/9	2009/10	2010/11	2011/12 Projected
Real GDP growth (%)	7.1	6.2	7.3	6.5	6.0
Inflation (%)	8.4	11.8	10.5	7.0	13.7
Broad Money (M3) (%)	20.1	18.5	25.1	20.1	20.0
Domestic Revenues (% of GDP)	15.9	16.2	15.9	16.5	17.8
Public Expenditures (% of GDP)	22.8	26.1	27.5	27.2	31.1
Overall Fiscal Balance (% of GDP)	-1.7	-4.6	-6.4	-6.9	-6.6
Current Account Balance (% of GDP)	-11.9	-10.7	-9.2	-9.8	-10.0
TSH/US$ exchange rate	1202	1264	1337	1491	--

Source: Ministry of Finance and IMF.

The ongoing energy crisis has contributed to the slowdown in economic growth. The economy suffered frequent fuel shortages in the second semester of 2011, as reflected by the 22 percent decline in electricity output during the third quarter, even though only 13 percent of the population has access to electricity. In August 2011, the Government implemented an emergency program to rehabilitate and construct new power supplies. This program has gradually helped resolve this problem. In January 2012, to support this program, electricity tariffs were increased by an average of 40 percent. This measure should help cover the costs of emergency power supply and of longer term investments. In the shorter term, it will protect the public company (Tanesco) from acute insolvency. Most of the additional short term cost will be borne by consumers in the top 10 percent income bracket and a few energy-intensive industries. Today, at USD 0.17 per kilowatt-hour, Tanzania's average electricity tariff is still half of the tariff in Uganda and about 20 percent lower than that of Kenya. This indicates that it is lack of access, and not high prices, that is the real problem for private sector development and sustainable economic growth. [6]

The economy suffered frequent fuel shortages in the second semester of 2011, as reflected by the 22 percent decline in electricity output

The second explanation for the slower rate of growth is the recent adjustment to unsustainable fiscal and monetary policies. Public spending expansion will have to be more moderate than initial projections, lowering its impact on the aggregate demand. The restrictive monetary policy has already pushed interest rates up and reduced credit to the private sector. The recent slowdown in construction (down by 5.2 percent in the third quarter of 2011 compared to last year) and manufacturing (down 0.7 percent) may reflect higher energy and borrowing costs.

6 Only 13.5 percent of Tanzanians have access to electricity with a high inequality depending on the household income levels. While almost 3 out of four wealthy households report to be connected to the national grid, the access rate is close to zero for the 80 percent poorest households in the country.

The overall fiscal balance should be better than last year, reversing the deteriorating trend observed since 2007/8. Following the recent agreement with the IMF, the fiscal deficit is forecast to improve to 6.6 percent of GDP, down from 6.9 percent in 2010/11. As described earlier, the public debt should increase only moderately. This is the result of a highly appropriate government endeavor to restore creditworthiness and limit the crowding out of credit to private sector.

Similarly, the external balance of trade is expected to remain at acceptable levels. The current account should stabilize at around 10 percent of GDP. Historically, there has been a close historical correlation between the variations in the volume of exports and imports. No major changes are expected in Tanzania's terms of trade, as the impact of the small projected decline in agricultural and gold prices should be balanced by lower energy prices.[7] Exports of merchandise are projected to increase by 26 percent in 2012, while imports should rise by 22 percent. Similarly, financial flows should not be significantly affected by short-term events, as FDI reflects longer term commitments in the mining sector, and donors have committed to disburse at approximately the same level than 2010/11. Other movements of capital will continue to have merely a marginal influence on the country's capital balance.

The restrictive policy stance of the Central Bank should bring inflation back to single digit figures by mid-June 2012. The current high rate of inflation has not impacted all domestic prices, with the core inflation rate (excluding food and energy prices) remaining below 10 percent during 2011. The prices of food and energy are expected to decline slightly on international markets, lessening the upward pressure on the domestic inflation rate in the near future. Such stability is reflected by the World Bank's Global Economic Prospects, which forecasts oil prices to average US$98/bbl in 2012, assuming the political unrest in the Middle East is contained and Libyan crude exports return to the market. In 2012, international food prices are expected to average 11 percent lower than 2011. At least equally important, domestic food production should remain constant or improve following the poor harvests in 2011, with lower food prices potentially pushing inflation down in 2012. The recent increase of 40 percent in domestic electricity tariffs should not have a significant impact on inflation because of the low weight of energy in most households' consumption basket.

Despite the relatively good forecast for Tanzania's economic performance, careful management is required in a risky global environment. A number of different factors could adversely affect the economy, and drive growth down. A combination of floods in urban areas, such as experienced recently in the Dar es Salaam conurbation, the monetary troubles in Europe, and lower gold prices, could all have a negative impact on the Tanzanian economy. Those exogenous shocks may be accompanied by additional internal fiscal pressures emanating from the energy emergency program and road contracts.

7 For more details on international commodity prices, see *Global Economic Prospects 2012*, op. cit.

The resilience of the Tanzanian economy to external shocks in the past does not necessarily guarantee immunity in the future. The looming global recession may have a greater negative impact on the Tanzanian economy as a result of one or more of the following:

- The fiscal crisis in donors' countries may push them to reduce aid inflows;
- The global recession may extend to emerging countries, thereby affecting negatively Tanzanian exports toward those markets;
- Prices of gold and oil can move in directions that will destabilize Tanzania's current account balance since those commodities count respectively for one third and one quarter of the country's exports and imports.

The Government is well positioned to manage these risks individually if their magnitude is limited. However, it may be considerably more difficult to manage several major shocks that coincide.

The Government is aware of these risks, as its recent prudent policy stance demonstrates. This policy stance guarantees a certain degree of stability in the macroeconomic and fiscal environment. Any deviation would be reflected almost immediately on local financial markets, leading to higher inflation and interest rates, and possibly to a loss in the value of the local currency, as experienced between June and October 2011. Donors are also likely to react negatively, as budget support is highly sensitive to the macroeconomic environment. And stability matters for the poor because they are most affected by price volatility. Stability also matters for business. What is the worst enemy of private investors? Taxes, administrative burden, limited access to credit? All are important but good businessmen can navigate through those obstacles. Their worst enemy is uncertainty. Uncertainty it pushes entrepreneurs to adopt a "wait and see" attitude, and inaction kills business.

At this point in time, the Government may want to consider the path followed by the countries that have

The World Economy in 2012

The World Bank Prospects Group projects that, even in the absence of a credit "event" in Europe, persistent uncertainty will dampen business and household spending in high-income economies and lowering growth in developing countries. Growth for high-income countries in 2012 is projected at 1.4 percent for 2012 including -0.3 percent in the Euro Area. Developing country growth projections have been revised down from 6.2 to 5.4 percent in 2012. World trade is projected to grow at 4.7 percent in 2012 compared to 6.6 percent in 2011.

China and other dynamic emerging economies in Asia and Latin America, though not directly affected, will see their high rates of economic growth dented through lower exports growth, and lower capital inflows. Like Tanzania, the big developing economies have less fiscal space than in 2008. Recent data suggest a certain amount of contagion from the European sovereign debt crisis, with spread on T-bill for emerging economies on the increase, falling stock markets worldwide and a 55 percent decrease in gross capital flows to developing countries.

Source: World Bank Global Prospects, January 2012

The looming global recession may have a greater negative impact on the Tanzanian economy entrenched rules of fiscal discipline in their legal framework. For example, Mauritius has entrenched a ceiling on its public debt to GDP ratio through legislation (see Box). Other countries (e.g. UK, Germany, and Switzerland) have adopted legislative measures to entrench the "golden fiscal rule" that caps their level of recurrent spending at a given ratio to domestic revenues, or other fiscal rules. Entrenching such measures to achieve fiscal stability through legislation limits the possibility of political interference and creates a sense of long term commitment to guide policymakers. Of course, to be credible, as the experience of the EU shows, such legislation needs the inclusion of sanctions or remedies to be applied in case of deviations from those rules. However, the trade-off of such legislation is the loss of some fiscal flexibility, although this flexibility can be retained through careful formulation of legislation. The adaptation of such measures in Tanzania requires cautious and analysis, with adjustments for Tanzania's reality.

Mauritius: The Public Management Act 2008

This Act does set up a ceiling on public debt but also specifies a number of principles in terms of debt policy and management.

- *Medium term planning.*
- *Close monitoring and supervision.*
- *Power of Ministers and public agencies must be limited.*
- *Public debt should include contingent liabilities of local governments as well as public enterprises and agencies (including social security and saving schemes).*
- *Flexibility should be provided for exceptional circumstances (natural disasters and emergencies, large priority investment projects).*
- *Remedies measures should be explicitly incorporated in the Law as well as the responsibilities and eventual sanctions.*
- *Debt management (currency mix, interest rate-mix, maturity profile).*

1.3 In the search of new drivers of growth: A shift in policymaking?

The Tanzanian economy is growing at a high rate. Mining profits are at record highs. The nation's construction and financial service firms are humming along. But for many Tanzanians, even those with jobs, the "economic growth" has been hardly worth celebrating. This disconnect calls for a shift in policy-making as recently recognized by national policies, including MUKUTA II.

Moreover, a slowdown in government spending could add downward pressure on the forecasted growth figure. Fiscal expansion has been a major driver of growth over the past decade, particularly during the last three years. While financially prudent policies are vital, these fiscal policies will reduce the stimulus in the short term. In the longer term, this driver of growth is also likely to diminish as aid inflows are unlikely to grow as fast as they did in the past decade (Figures 8 and 9). External financing declined since

Fig. 8: Government spending the engine of growth since 2007/8

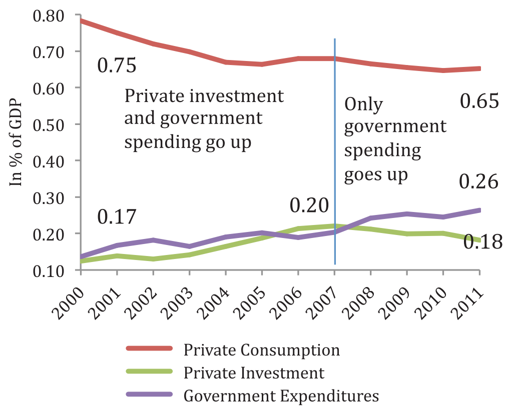
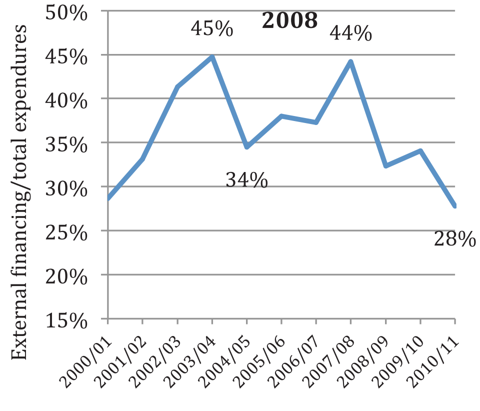


Fig. 9: The declining share of official aid in the budget since 2008



2008, and this trend is likely to continue in the near future due to the current fiscal distress in most OECD countries. Public spending may stabilize as a share of GDP at little more than current levels.

Opportunities exist for other sources of public financing, but those appear relatively limited in the short term. Non-traditional foreign assistance, while growing, is unlikely to transit through the national budget. Additional no concessionary borrowing would be difficult to obtain at large magnitude due to volatile international markets and the thinness of the local financial market. Ultimately, public spending patterns should be more closely associated with the Government's capacity to raise additional fiscal revenues. If policy and administrative reforms (including the rationalization of existing tax exemption regimes) can be pushed more actively, the margin of progression will become narrower after substantial gains achieved over the past decade and given the current structure of the economy (high informality, non-monetary economy, agricultural activities).[8] Over the medium term, the Government will benefit from the prospects of natural gas exploitation but the associated burst in fiscal revenues is not expected to take place before the end of the decade.

It is difficult to forecast future aid inflows and other sources of funding. However, if recent trends are an indication, it will become increasingly difficult for the government to utilize such resources to facilitate a sustainable rapid fiscal expansion in the near future. If the government's capacity for expenditure becomes increasingly limited, it will have to adjust and to find new drivers of growth. Otherwise, the economy may go again through its traditional cycle of lower aid and growth episodes, such as occurred in 1993 and 1996.[9] The search for new drivers should also aim at becoming more inclusive, particularly considering that the

8 For more details on the link between tax performance and the structure of the economy, see: IMF, *Revenue Mobilization in Developing Countries*, Fiscal Affairs Department, March 8, 2011.

9 For a historical perspective of the link between Tanzania's economic cycles and aid inflows, see S. Edwards, *Tanzania: A Success Story?* NBER working paper, 2011.

overall poverty rate has remained constant at around one third of the population throughout the rapid economic expansion recorded during the 2000s.

It is only a matter of time before a healthier economy encourages businesses to hire more workers. In the end, this will improve the fortunes of poor households. However, time is short for Tanzania. The experience of successful emerging countries suggests that the cost-effective management of public resources and the productivity gains of the private sector will continue to drive economic growth. Therefore, Tanzanian policymakers must focus on the implementation of policies that encourage these outcomes.

The next sections contain detailed analyses of how more effective management of public resources may be achieved in the education sector and of how to encourage positive changes in the private sector. These two issues are central to the building of two virtuous circles for shared and sustainable growth (see Figures 10 and 11). The first circle underscores the links between improved education and skills, which in turn generate jobs and improved incomes that facilitate further investments in human capital.

The second virtuous circle relates to the role of the private sector in the generation of additional tax revenues, which will finance additional education expenditures. This expenditure will lead to improved educational outcomes and so more productive workers and firms, which in turn will increase the potential for government revenue collection. For Tanzania, the development of such virtuous circles is a means of connecting good macroeconomic performance and improved living standards for the majority of the population. Through such means, Tanzania may succeed in its ambitious to reach middle income status by 2025.

Fig. 10: Virtuous circle #1: education, skills and jobs

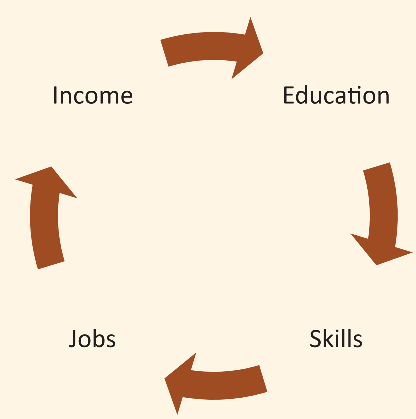
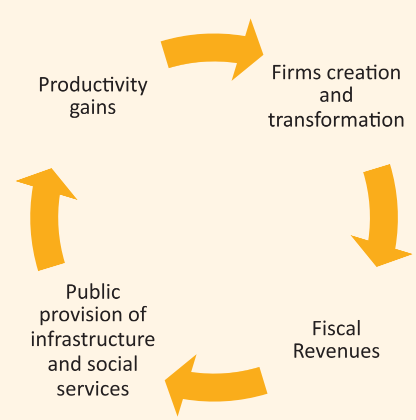
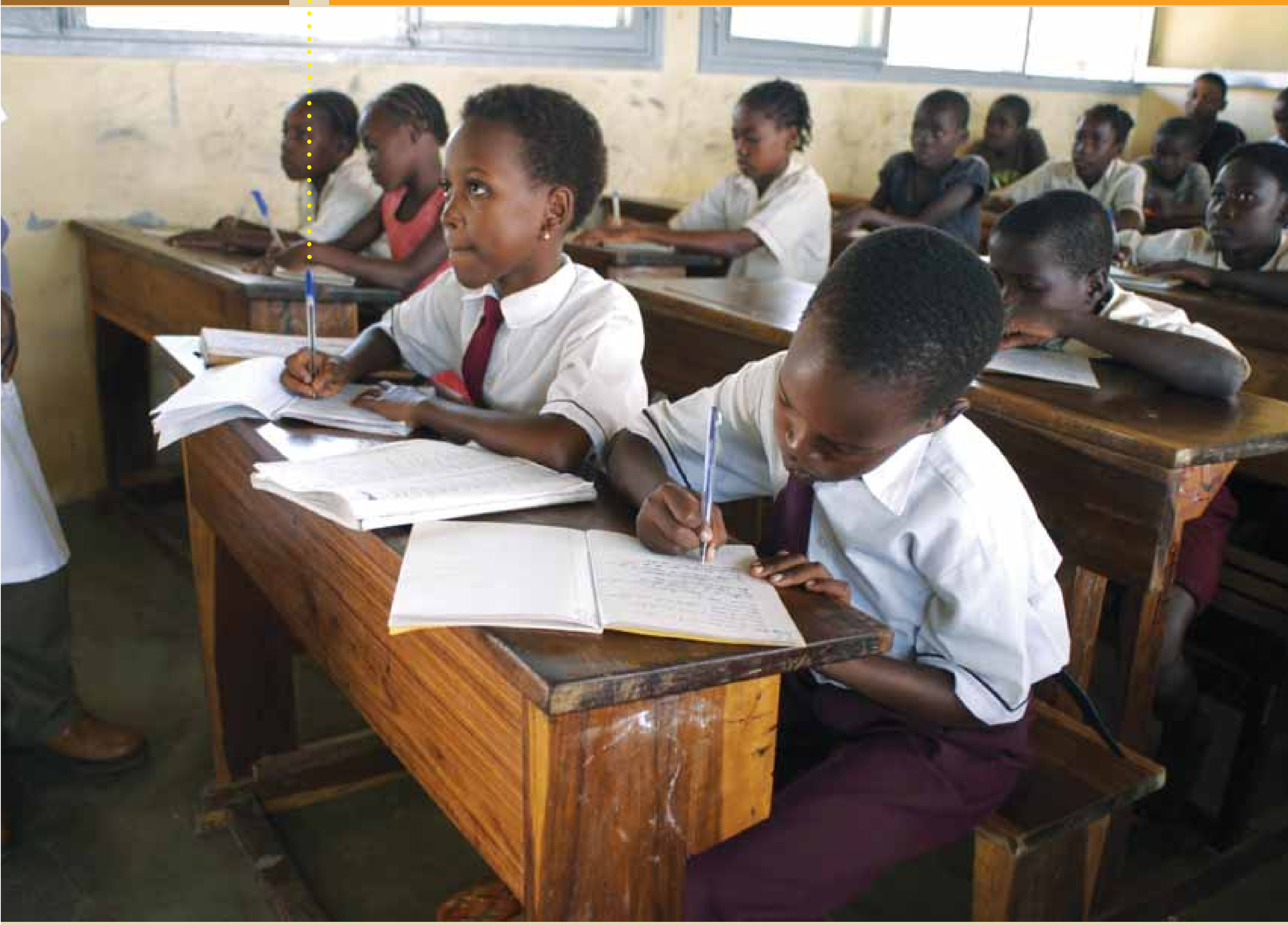


Fig. 11: Virtuous circle #2: Firm transformation, fiscal revenues and basic services provision



If the government's capacity for expenditure growth becomes increasingly limited, it will have to adjust to find new drivers of growth

2 Getting more value for money in the education sector



Part 2 Getting more value for money in the education sector

Main points

- Tanzania has selected education as a priority area for its development, spending close to 20 percent of its budget.
- While attendance has boomed, pass rates remain low both in primary and secondary schools.
- Urgent actions are required to address the triple challenge of limited resources, quality upgrade, and fast-growing school populations.

Over the past decade, the Government has launched an unprecedented fiscal effort to provide more and better infrastructure and social services. The Tanzanian State has expanded rapidly, from 15 percent of GDP in 1998 to almost 30 percent in 2011. Unfortunately, this has not yet resulted in it catching up with most developing countries in terms of infrastructure and social services provision. At present, in terms of road infrastructure, Tanzania has 9 times less paved roads per km^{2}than Uganda; in terms of electric power capacity, it has 10 times less Kwh per habitant than in Mozambique; while in terms of medical services, it has 40 percent less hospital beds per capita than in Burkina Faso.[10] Equally worrisome is that due to fiscal adjustment and slower external capital inflows, the public sector is unlikely to grow much faster in the near future.

If the Government cannot spend more, other means of delivering more and better public services and infrastructure will have to found. One such means may be through partnerships with the private sector, with such partnerships benefiting from the private sector's expertise and financial resources. The second means may involve the improved management of investment projects in terms of their selection, implementation, and maintenance. The third means would be to ensure that greater value for money is derived from the delivery of social services.

The attainment of a high level of proficiency in the education sector is particularly important, considering that the development of the educational sector has been a main focus of policymakers over

10 Source: World Development Indicators.

the past decade.[11] The level of public expenditure per student has more than doubled since 2005. Despite this increase, approximately half of all students still do not graduate at the end of the primary cycle and only around 10 percent successfully graduate from secondary school. There is an increasing demand for better results now. A failure to rapidly improve the efficiency and effectiveness of the educational system will result in government failure to meet the challenge created by the massive arrival of new students in secondary schools. Given the importance of this sector and the level of resource devoted to it, such a failure may result in the destabilization of the entire budget.[12]

2.1 Government's drive to increase finance for service delivery

The development of human capital is vital for Tanzania's long term economic development. Efficient public service delivery is the key to achieving this development. This double causal relationship has been well understood by the Tanzanian policymakers. Thus, these policymakers have directed significant resources towards improving the national education and health systems over the past decade. The goal of policymakers is to increase the capacity of the education and health systems by financing both recurrent and capital spending to enable members of the community to attend schools, hospitals and health centers to receive good quality education and health services. The availability of such services is rightly seen as a means of improving the stock of human capital in the country.

The level of public expenditure per student has more than doubled since 2005

Since 2005, combined expenditure on education and health has increased by 190 percent in real terms. In the education sector, this increase in expenditure is equivalent to an average growth of 10 percent per capita per year. Initially, the increased expenditure was the result both of the increased deployment of teachers and increased investment in new schools. In more recent years, the school building program has slowed down dramatically. In fact, the great expansion of primary education occurred before 2005. While the proportion of expenditure on primary education has slowly decline, it still accounts for half of the total expenditure on education in 2011/12. At the same time, expenditure on post-primary education has increased. Initially, expenditure on higher education amounted to more than 30 percent of frontline spending, whilst the proportion of expenditure on secondary education declined to about 13 percent in 2009/10. Since 2010/11, efforts have been made to accelerate the funding of secondary education.

11 This section of the economic update is based on the analysis carried in the 2010 World Bank Public Expenditure Review United Republic of Tanzania Public Expenditure Review 2010, September 2011, World Bank Report Number 64584-TZ.) It focuses on education, while the same approach is currently developed to assess the value for money in the health sector. The result of this analysis will be part of the forthcoming 2011 Public Expenditure Review.

12 The issue of upper education and its adaptability to the need of the labor market is not directly addressed in this section. There is no need to stress that skill developments through the education system and close partnerships with the private sector are crucial for job creation and productivity improvements. The opportunities for private firms' participation in skill development programs are discussed in the next section of this economic update.

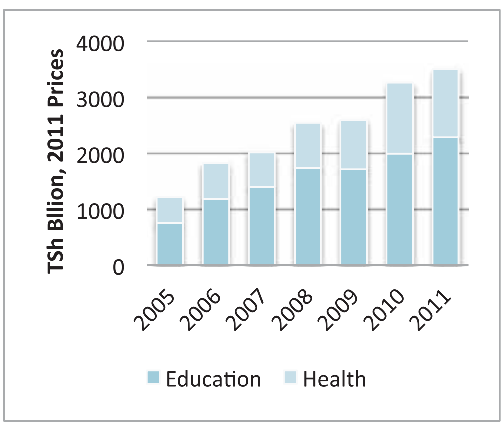
Development Partners have been highly supportive of the expansion of the Tanzanian educational system. This support was initially channeled through earmarked investment projects, although an increasing proportion is now provided through general budget support. Since 2010/11, the World Bank has introduced a Secondary Education Development Project (SEDP) to address the low level of resources and the poor quality of secondary education.

While private educational service providers are important in Tanzania, they are less so than in many other developing countries. Historically, the expansion of the Tanzanian educational system through cooperation between public and private educational service providers has been less important in Tanzania than in other East African countries, especially Kenya.

In recent years, private schools have become increasingly significant in urban centers, although the proportion of students enrolled at such schools still accounts for less than two percent of the total number of primary school students in the country.

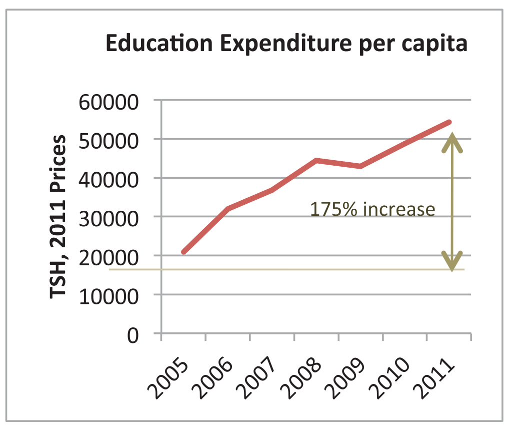
In secondary schools, the proportion of students at such institutions is somewhat higher, with students at these institutions constituting 15 percent of the total numbers of students. Household spending on education remains very low, although it is rapidly increasing amongst higher income households. It is estimated that the average monthly spending on secondary education per 13-19 year old is just TSh 2,000 in poorer households, compared to TSh 33,000 in richer households.

Fig.12. Almost 200 percent real increase in social sector spending



Source: World Bank, 2010 PER

Fig 13. Education Expenditure per capita



2.2 Money has put children in schools, but learning outcomes are lagging

The Tanzanian government has been very successful in increasing the proportion of students initially enrolled in primary school. The Millennium Development Goal of achieving universal registration for boys and girls in primary schools came close to being achieved by 2005 (Figure 14). Increases in rates of enrolment at secondary school have come later: while only 5 percent of 17 year olds were enrolled at secondary schools in 2005, this had increased to more than 30 percent by 2010 (Figure 15).

Despite the rapid increase in rates of enrolment, results in terms of average learning outcomes have been mixed both in both the primary and secondary educational sectors. After a dramatic improvement in the early 2000s, learning outcomes in primary education actually declined, at least in terms of the pass rates at the exam taken at the end of the primary cycle (the PSLE exam) (Figure 16). Until 2007, results steadily improved, with more than 70 percent of 13 year olds passing the exam. However, since then, pass rates have declined, not only in terms of the proportion of candidates, but even in terms of the proportion of the entire 13-year-old population. In secondary schools, CSEE pass rates declined from 34 to 9 percent between 2005 and 2010, although there are now considerably more graduates than in 2006 (Figure 17).

Figure 14: Pupils in primary Schools

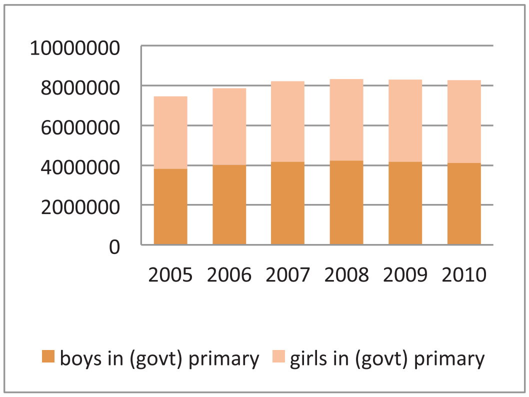
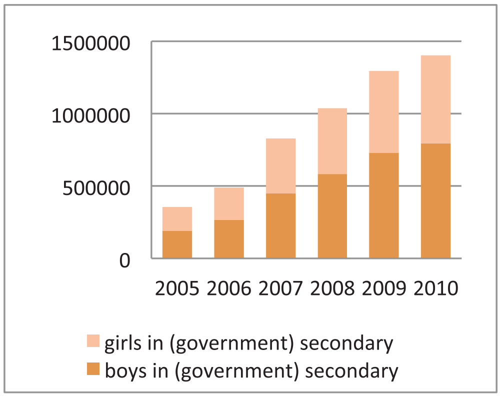


Figure 15: Secondary Student Numbers



Source: World Bank, 2010 PER

Fig 16: Primary Cycle: Less Graduates and lower pass rates since 2007

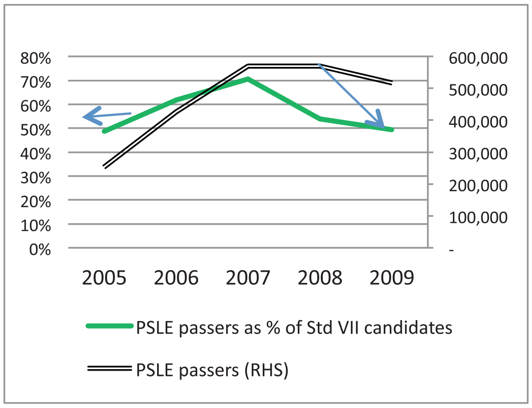
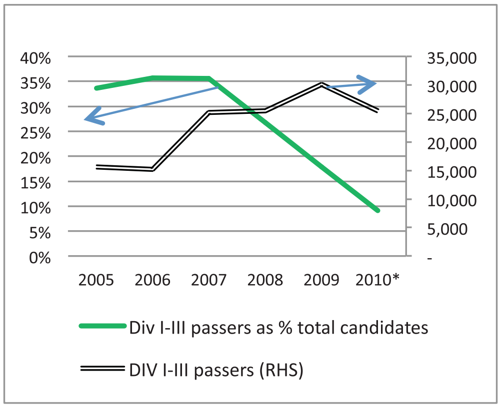


Fig 17: Secondary Cycle: more graduates but steep deterioration in pass rates



Source: World Bank, 2010 PER

Fig. 18: Expenditure per PSLE-Passer

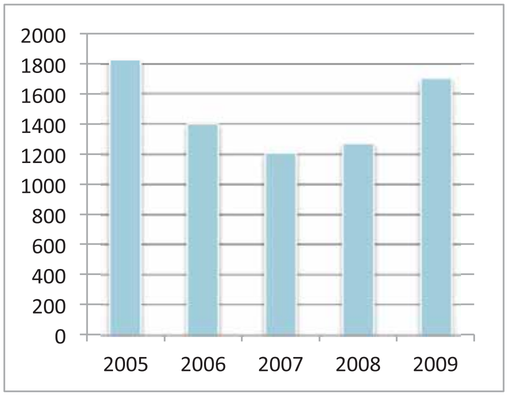
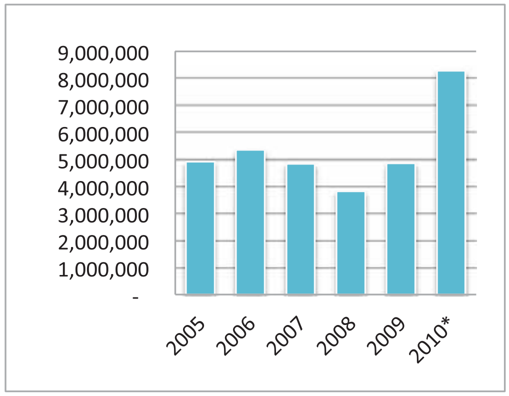


Fig 19: Expenditure per CSEE passer



Source: World Bank, 2010 PER

Despite the additional expenditure on education, pass rates have actually declined: in other words, the government's return on investment in the educational sector is decreasing. The value of public resources spent for each successful candidate of the PSLE exams has increased in real terms by more than 41 percent since 2007 (Figure 18). In parallel, the expenditure for each successful candidate of the CSEE exams has skyrocketed to more than TSh 8 million in 2010, from only TSh5 million (Figure 19) in 2005. These rising costs almost certainly depress the private and social returns to education since 2007. Figure 20[13] shows that even then, returns to primary were particularly low in Tanzania, possibly linked to poor learning outcomes. This decline means that achieving desired educational outcomes will become increasingly expensive and will ultimately become unaffordable. For example, to see 300,000 secondary graduates with CSEE passes (figure equal to about one third of the country's population of 17-year-olds) would require an annual expenditure level of more than TSh 2,400 billion at the current "cost per successful student". This exceeds the current budget for the entire education sector! It is impossible to achieve secondary education goals simply by allocating additional resources to the sector. For these goals to be achieved, efficiency must improve.

The deterioration in the cost efficiency of the education system may partially reflect the expected lag between current efforts and final pass rates. Building schools takes time and teachers need time and experience to become fully effective. Thus, expenditure on current projects, particularly at the secondary level, may generate a visible return on investment only after several years, when the current cohort of students begins to graduate. Nevertheless, a highly regarded pan-East-African survey conducted by Uwezo shows that the quality of education in Tanzania's primary education system was significantly worse than in Kenya and Uganda, as measured by a performance in maths and English by second grade students.[14] Tanzanian

Quality of education in Tanzania's primary education system was significantly worse than in Kenya and Uganda, as measured by a performance in maths and English by second grade students

13 Figure 15 rates of return are derived from the relationship between earnings and education reevaled in household budget surveys 2001 and 2007.

14 These results were challenged in all three participating countries but another survey, SACMEQ, Tanzania confirms the above ranking even though Tanzania performed relatively better.

While low rates of return are the result of multiple factors, they are partially due to the persistent low quality of education, with many school leavers unprepared for the labor market

pupils showed lower average levels of achievement in Kiswahili compared to their Kenyan counterparts, even though Kiswahili is the primary language of instruction in Tanzania.

The return on investment for students and their families remains relatively low. This reinforces the need to improve the efficiency of the educational system. As a general rule, a household is more likely to invest in education if its future earnings exceed the direct and indirect cost of schooling. Unfortunately, in Tanzania, these rates of return are comparatively very low and have not improved over time, except for tertiary education (Figure 20). While low rates of return are the result of multiple factors, they are partially due to the persistent low quality of education, with many school leavers unprepared for the labor market. If this is the case, households may rightly determine that they are not getting value for their money in terms of their investment in education.

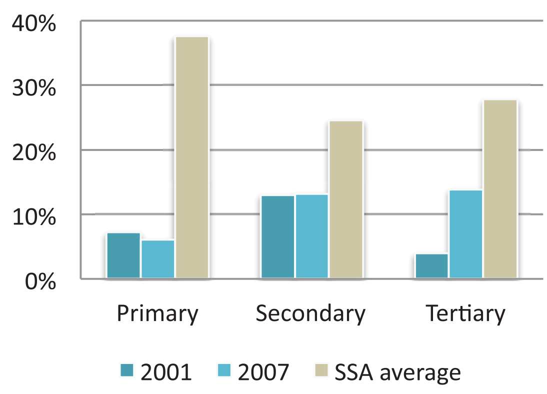
2.3 Understanding the variations in education efficiency across districts

The efficiency and effectiveness of the education system fluctuates enormously across districts. In order to increase the efficiency of the education system as whole, these variations need to be understood by policy makers.

There is a strong correlation between the level of performance of schools in different districts and the distribution of resources and/or teachers.[15] The more resources each district receives, the more likely it will be efficient. On average, after accounting for social and economic factors, up to 70 percent of the variation in PSLE pass rates can be explained by the level of public spending and/or the level of deployment of personnel in a district. This correlation is obvious as one can expect better educational outcomes with more teachers, books, and schools.

However, the positive correlation between deployment of resources and performance is not linear: at a certain point, return on investment declines. This reflect a simple rule of economics: there is likely to be a decreasing level of returns, as each additional teacher or book will have a more dramatic impact in a district where these resources are extremely limited than when they are widely available. Empirical evidence suggests that returns from incremental changes in resources decrease quite rapidly when a district receives more

Fig . 20: Private Returns to Education in Tanzania – Well Below SSA Average



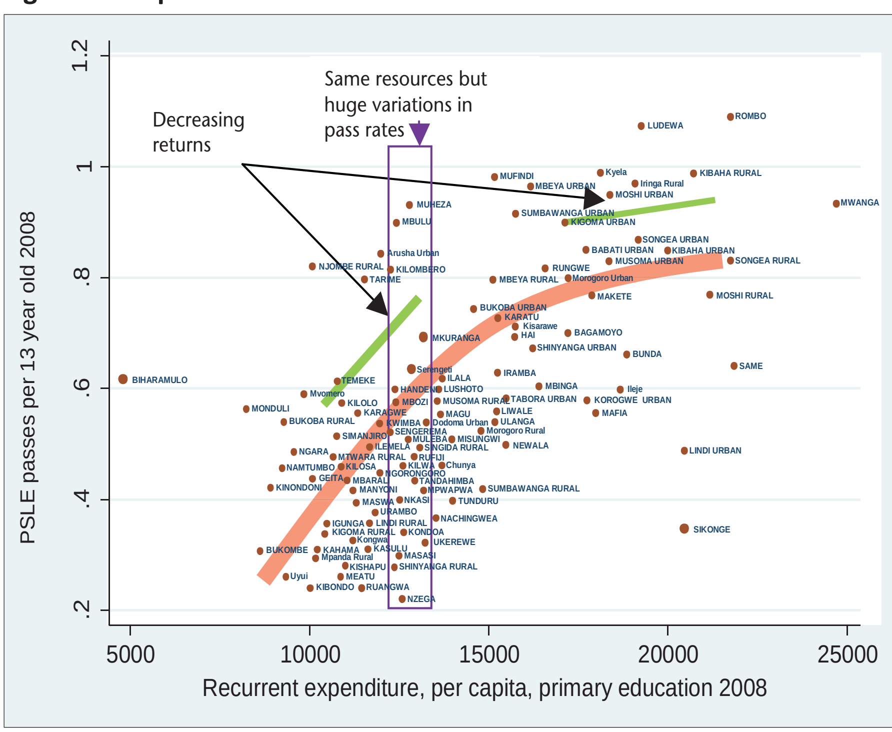
15 The inequality of resourcing is largely a function of unequal distribution of teaching personnel.

than TSh 18,000 per capita. This indicates that a higher level of return on investment will be achieved from allocating resources to underserved districts.

In addition to this, performance is also highly variable in some districts with very similar resources, so technical and financial management efficiency is also an issue. The vertical box in Figure 18 shows that some districts spending roughly TSH13,000 per capita on primary education achieve pass rates of around 30 percent, compared to others with 100 percent pass rates with the same level of resources (top of the box). The latter are districts with really efficient schools. Something must be undertaken to improve the way schools are managed or teachers are motivated in the inefficient districts.

While the capacity of the educational system of each district to produce graduates correlate strongly with the level of deployment of resources, it is also influenced by other factors. This has to be expected because efficiency depends on the context in which the education system has to operate. For example, significant factors may include the level of literacy of parents and their income and their children's health. Figure 21 shows large variations in pass rates between districts that have received almost the same level of resources. Interestingly, if the context does matter, it seems that the internal efficiency of each education system plays an important role, particularly for districts that receive more resources than the average. For example, the districts of Mblulu and Masani receive approximately the same level of resources (TSh 12,000 per capita) and are characterized by roughly the same social context, but the pass rate is three times higher in Mblulu than in Masani. Further

Fig. 21: Unequal distribution of resources across districts



This Figure illustrates the close and positive relationship between resources (recurrent expenditure per capita) and the ratio of primary graduates (PSLE pass rate) in each district (red line). This relationship varies nonetheless depending on the level of resources. In an underserved district (receiving less than Tsh18000 per capita), the pass rate is more sensitive to a change in resources than in an over-served districts (this is captured by the slope of the green lines). Lastly, variations in pass rates do exist even if two districts are receiving the same amount of resources, suggesting that other factors influence the system efficiency (this is illustrated by the vertical box in purple).

Source: World Bank, 2010 PER

analysis revealed that the administrative and technical capacity of local staff and synergies between the public system, private service providers and households are more developed in the district of Mbulu than in Masani.

2.4 Higher value for money through a three-step approach

These three findings indicate directions for improving the efficiency of the education system in Tanzania. To achieve a higher level of cost efficiency and to conserve financial resources, a three-step approach is proposed. The value of savings may reach up to one quarter of the existing budget for the education sector. With these savings, freed up financial resources could be used to address the formidable demographic challenge that the secondary education system will have to face in the coming years, with the student enrolment increasing by approximately 30 percent each year.

A significant step would involve the development of an information system by which levels of performance of the educational systems in different districts could be measured. Currently, policymakers, teachers and students are not able to determine the level of efficiency of their schools or districts largely because there is no meaningful system by which this efficiency can be measured. Ideally, stakeholders should have access to information by which to assess the performance of their school compared to others. In order to facilitate this, the Government should collect and disseminate information by which the performance of each district may be assessed. Such an effort would increase accountability both at the national and local levels and would foster healthy competition between schools and districts.

Secondly, it is necessary to reallocate financial and human resources towards relatively underserved districts. A more equal distribution of resources between districts would improve outcomes without requiring additional public expenditures (see box for a quantitative example).

Savings from reallocation of resources across districts

Efficiency gains from re-allocation of resources amongst district could be substantial as illustrated by the following numeral example.

Take first the group of 20 "underserved districts", where mean expenditure per 7-13 year old was TSh82450 and the average pass rate was 53 percent in primary school lever's exams in 2008/9. Then, compare this group with the sample of 20 relatively "overserved" districts with average spending at TSh146000 and pass rates at 80 percent.

If resources, say TSh10 billion, are re-allocated from the second to the first group, the net increase of passers will be as much as 3827 or over 200 percent gains for those 40 districts. This net increase accounts for the gain of 5606 in underserved districts and the loss of 1779 in over served ones.

For larger sums the amount of gain would diminish but efficiency savings of around TSh240bn per annum might be possible just from geographical re-allocation.

Source: World Bank, 2010 Public Expenditure Review.

Thirdly, the government should take steps to replicate and spread the practices of districts that achieved relatively good results not immediately explainable in terms of the level of financial and human resources that these districts receive. A close monitoring of districts which achieve lower than average results relative to the level of resources they receive may also result in improved efficiencies. Efficiency gains can be achieved through (i) internal management of financial and human resources (including expanded teacher training programs); (ii) partnerships with private providers through performance contracts; and (iii) participation of households through incentives schemes, including vouchers and conditional cash-transfers. The close partnership with the private sector is an opportunity in growing markets, such as in urban centers due to migration flows.

At the higher educational levels, it becomes increasingly important to ensure the compatibility of syllabuses with the demand from the labor market. Private sector participation is even more essential for technical and vocational training. Ensuring that a greater number of districts achieve results commensurate with the level of resources invested in their educational systems could result in savings of up to TSh 340 billion per year.

International experience demonstrates that countries implementing the appropriate policies can achieve efficiency gains from their educational system. For example, Uganda and Brazil include an equalization element in their local government funding formula to move financial and human resources from over-served to under-served areas. Many countries, such as Norway, Australia, and Indonesia, also pay substantial incentives to teachers and other staff working in difficult areas. To achieve this objective, the necessary steps are clear: there should be sufficiently high incentives available to encourage teachers to seek posts in understaffed districts. In addition, there needs to be disincentives and effective limits on hiring levels in relatively overstaffed districts, including limits on in-year staff transfers.

The effective implementation of policies to achieve increased efficiency in the educational system requires a strong degree of commitment. At present, accountability and responsibility for educational outcomes is diffused between local and central authorities and between a wide range of various institutions at the central level (Ministry of Education, Finance, Prime Minister Office, and President's Office).

There is an urgent need to assign clear roles and responsibilities so that decisions are taken with the objective of improving the efficiency of the education system.

Despite the challenges and difficulties of improving the efficiency of the educational system, the success of such endeavors is vital to the future of the Tanzanian economy and of the nation itself. If the education system continues to fail to produce a sufficient number of graduates, the availability of the necessary human resources will remain limited, which in turn will limit the potential for growth of the Tanzanian economy. On the other hand, if the number of graduates increase too fast, the cost will be unbearable for the State. The only solution is to generate a higher level of return on public investment in education.

If the education system continues to fail to produce a sufficient number of graduates, the availability of the necessary human resources will remain limited

3 Harnessing the power of economic transformation

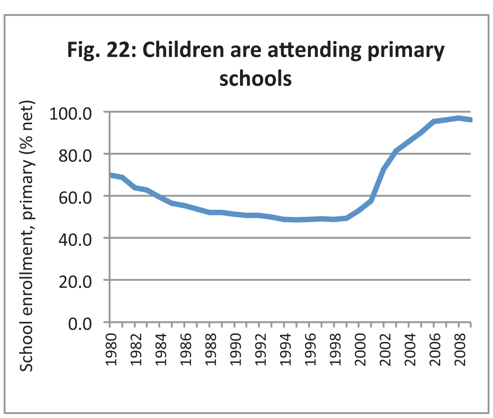
Part 3 Harnessing the power of economic transformation

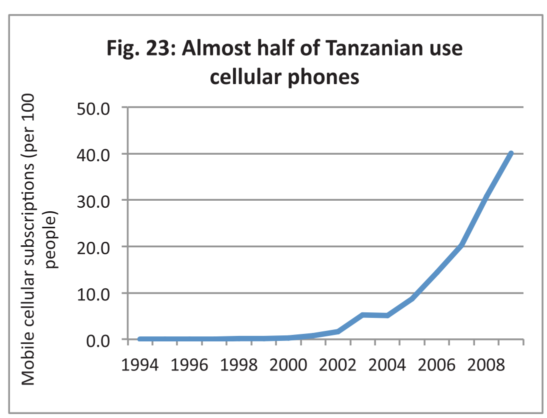
Main points

- The Tanzanian economy is on the move thanks to technology and education improvements.
- Emerging signs of transformation in the private and financial sectors.
- Smart supportive policies are needed based on innovation, training, and diversification.

"How was school today? Don't forget to bring home the milk!" This simple conversation between Halima, a 36-year-old woman from Dodoma, and her young daughter on their mobile phones demonstrate how much has changed in Tanzania over the past 15 years. Firstly, the conversation was conducted on a mobile telephone: 15 years ago, only 2 percent of Tanzanians had access to a mobile telephone. Secondly, 15 years ago, only one out of two children attended a primary school. These days, access to both facilities is entirely unremarkable, with around half the population having access to a mobile telephone and almost all children of primary school age attending schools (Figures 22 and 23). Daily life has changed dramatically in Tanzania, and technology and education have been the main drivers of change.

Education and technological improvements over the past decade





Source: World Development Indicators

There are incipient signs of transformation in the Tanzanian economy

However, the questions remain: Have these changes led to productivity gains in the domestic economy? Will they do so in the future? How can policymakers encourage such positive developments? This section will attempt to demonstrate that there are encouraging signs of emergence in the Tanzanian economy that are as yet not reflected in national accounts and/or international statistics. These encouraging signs of development should be promoted through supportive policies based on three guiding principles that international experience shows have been central in the success of emerging countries.

3.1 Is the Tanzanian economy on the move?

Advances in technology and improvements in the educational system have the potential to facilitate improvements in productivity in Tanzania's private sector. International experience shows that successful emerging economies have been able to achieve productivity gains by (i) by adopting more efficient production functions and (ii) by shifting their private resources to most productive sectors. The shift should be moving away from traditional agriculture and other low-productivity primary activities and developing the "modern" sectors (including non-traditional agriculture, manufacturing and services). As Mc Milan and Rodrik observe: "*The speed with which this structural transformation takes place is the key factor that differentiates successful countries from unsuccessful ones.*"[16]

16 McMillan, M. and D. Rodrik, 2011. *Globalization, Structural Change and Productivity Growth*, mimeo, February. See also, Ndulu, B. et al., 2007. *The Political Economy of Economic Growth in Africa*, 1960-2000, vol. 1, New York, Cambridge University Press.

Discouragingly, at first glance, there have been few indications of positive structural changes and productivity gains in Tanzania over recent years. Between 2000 and 2008, the proportion of the GDP derived from the agriculture and fishing sectors declined only slightly, falling from 29.5 to 24.6 percent.[17] Conversely, the proportion of the GDP derived from the industrial and services sectors increased only slightly, with the proportion from the industrial sector increasing from 19.9 to 22.0 percent; and with the proportion from the services sector increasing from 45.3 to 43.6 percent (Figures 24).

This lack of structural transformation which could drive economic renewal contrasts sharply with the situation in Malaysia over the past three decades (Figure 25).[18] In all sectors of the Tanzanian economy, productivity gains have been limited. The performance of the agricultural sector has been poor, while the services and industrial sectors have been characterized by a lack of dynamism resulting from technological, administrative, infrastructure, finance, and regulatory constraints (see Box). The productivity of Tanzanian manufacturing businesses was roughly 50 percent and 30 percent lower than those of similar

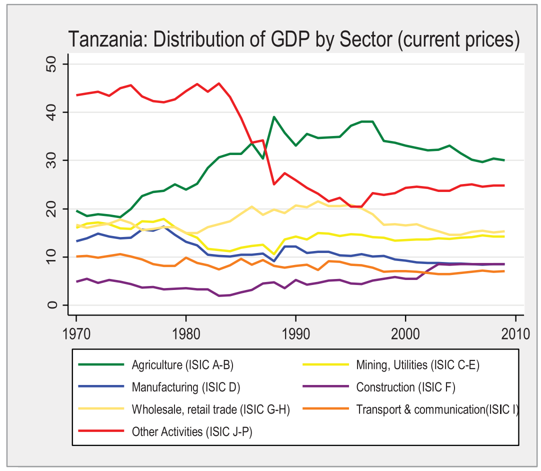
17 This decline my capture the recent emerge of non-farm activities in rural areas and the growing urbanization –two phenomena further discussed later as emerging signs of economic transformation.

18 African economies exhibit signs of limited structural transformation that explain why progress has remained slow since independence. In 1965, agricultural value-added represented 22 percent of SSA's gross domestic product (GDP), services 47 percent, and industry 31 percent (of which manufacturing contributed 17.5 percent). In 2007, it was estimated that agricultural value-added still contributed a healthy 15 percent of GDP while services contributed 52 percent and industry 33 percent (of which manufacturing represented less than 15 percent).

businesses in China and in Kenya in the mid-2000s.[19] In 2009, in terms of value added per worker, the level of productivity of the Tanzanian agricultural sector was only 4 percent of that of Malaysia's agricultural sector. Productivity was also significantly lower than in Kenya, despite agricultural endowment advantages.[20]

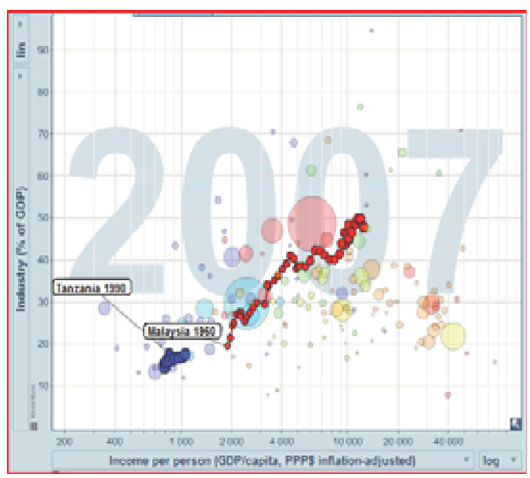
However, despite these discouraging figures, there are signs of incipient growth in the Tanzanian economy. The dramatic advances in technology, indicated by the equally dramatic expansion in the rate of usage of mobile communications, and improvements in education have resulted in significant structural transformation. While the results of this transformation have not yet been reflected in national accounts, they are likely to shape the future of the Tanzanian economy.[21]

Fig. 24 : Lack of Structural Transformation since early 1980s



Source: National Accounts

Fig. 25: Moving up the industrial ladder – Tanzania vs. Malaysia



Source: World Bank
Note: the size of the circle represents total population

19 Source: Investment climate assessment, *Improving Enterprise Performance and Growth in Tanzania*, the World Bank, November 2004,
20 Source: Word Development Indicators
21 Major structural changes are also expected to emerge from recent gas and oil discoveries, but those will take time to materialize while dangers in terms of corruption and misallocation of funds are already imminent when contracts are being negotiated.

3.2 Four early signs of transformation

Significant early signs of a forthcoming structural transformation of the Tanzanian economy include the following:

1. The dynamism of informal firms, especially those operating in off-farm activities;
2. The emergence of manufacturing exports;
3. Increased options for financing;
4. New pilot projects to improve the productivity of crop agriculture.

The dynamism of informal firms, especially those operating in non-farm activities: The agricultural sector remains the largest provider of jobs in Tanzania. However the most dynamic source of employment in recent years has been household enterprises, with the number of jobs in such businesses rising by approximately 13 percent per year, or 3 times faster than the national average (Figure 26).[22] This expansion reflects both a diversification of economic activities in rural areas, particularly on the part of agricultural households seeking complementary income and a rapid process of urbanization. Many informal businesses have been established in or around cities to take advantage ready access to markets and supportive infrastructure.

The emergence of manufacturing exports (Figure 27): With the decline in purchasing power of markets in the OECD crisis and as a result of ongoing efforts to promote regional integration, this expansion of manufacturing exports is focused on markets in neighboring countries. Approximately 55 percent of all manufacturing exports in 2009 and 60 percent in 2010 were sold to East African Community and South African Development Community trading blocks.

Small firms do create jobs and manufacturing exports are emerging

Fig. 26: Average annual growth rate in employment by type of employer, 2000-2006

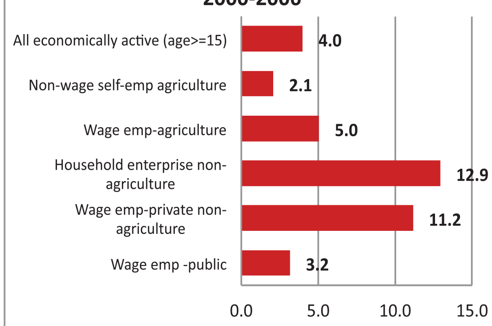
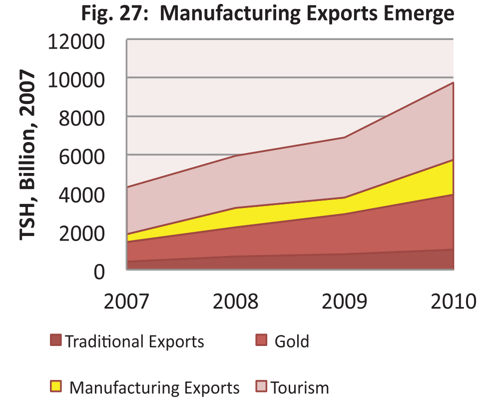


Fig. 27: Manufacturing Exports Emerge



Source: World Bank

The data shows that while a small number of existing companies dominate the manufacturing export market, their range of products is becoming wider. In particular, these products range from cement to plastic items, steel and iron products. The increase in the volume of exports from the

22 For a detailed discussion, see recent paper by J. Kweka and L. Fox, *The Household Enterprise Sector in Tanzania: Why It Matters and Who Cares,* World Bank Policy Research Series, n. 5882, November 2011.

manufacturing sector may reflect recent improvements in productivity and the improved competitiveness of Tanzanian firms.

Increased options for financing: In 2005, the total value of net credit to the private sector was just TSh 1.4 trillion. By 2010, this had increased to TSh 5.2 trillion, or 17 percent of GDP. Such an increase, while still marginal by regional standards, demonstrates the growth and profitability of the financial sector, with increasing competition among banks. In addition, as in many African countries, alternative forms of financing have become available, including microcredit for small firms and regional stock markets for large enterprises.[23] In addition, new sources of finance have become available for large projects in infrastructure, agriculture, mining and manufacturing activities. Chinese investors, for instance, have become active business partners in a number of significant Tanzanian enterprises with recent deals amounting to more than US$5 billion.[24] These new developments may help relieve the country's financial constraints and encourage further private sector development.

23 For example, Precision Air (a joint venture between Tanzania and Kenya's private capital) recently launched an initial public offering (IPO) on the local market.

24 China's Sichuan Hongda Co. Ltd. signed a $3 billion contract with Tanzania to mine coal and iron ore in a deal that has been dubbed as the single-biggest investment transaction in East Africa. In parallel, China and Tanzania have signed a $1 billion loan agreement to build a major natural gas pipeline that will lay a 532-kilometre pipeline from Mnazi Bay and Songo Songo Island in southern Tanzania to the country's commercial capital, Dar es Salaam.

New pilot projects to improve the productivity of crop agriculture: With modern irrigation systems, it has been possible to increase the productivity of rice crops: the country is now virtually self sufficient in rice production and can become a major regional exporter. A more intensive use of fertilizers has been encouraged by so-called "smart farming contracts", while the implementation of mobile phone in the Rungwe District[25] have encouraged productivity gains. Improving connections between farmers and input as well as consumer markets is now a major priority of the Southern Agricultural Growth Corridor of Tanzania project (SAGCOT). Despite such encouraging signs, many of Tanzania's farmers face untenable transport costs and insuperable tariff and non-tariff barriers to accessing international markets. One of the more significant of such barriers is the cereal export bans, which make it unprofitable for Tanzania's low-cost food producers to sell to regional markets.

These trends are small but significant signs of incipient structural transformations. Encouragingly, most emerging countries displayed similar trends in the earlier phases of their transition. Malaysia, for example, relied on: (i) a dynamic, innovative and expansive Small and Medium Enterprises (SME) sector, with one of the greatest number of new SMEs created per year

Most emerging countries displayed similar trends in the phases of their transition

25 For details, see A. G. Mwakaje, *Information and Communication Technology for Rural Farmers market Access in Tanzania*, Journal of Information Technology Impact, vol. 10, n.2, 2010.

If the majority of school graduates and others of working age are employed productively, the youth bulge will yield a demographic dividend

in the developing world [26], (ii) a rapid increase in the contribution of the manufacturing sector to total exports, with this proportion increasing from 20 percent to more than 75 percent of total merchandise exports between 1980 and 2000, (iii) an unprecedented increase in the volume of credit made available to the private sector, with the total value of this credit increasing from the equivalent of 20 percent of the national GDP in 1970 to 85 percent in 1985 and close to 120 percent in 2009; and (iv) rapid increases in the productivity of the agricultural sector, with the productivity of this sector in Malaysia being six times more productive than the world average.

3.3 Smart policy: three guiding principles

Structural transformations are highly sensitive to the policy environment in which they are embedded. While the appropriate policy environment can encourage structural transformations that facilitate economic growth, an inappropriate policy environment can stifle or even destroy such transformations. The debate is not whether or not Tanzania should have an industrial policy: rather, it should focus on how to design and govern sectoral policies in order to encourage competition and growth.

In Tanzania, the following underlying principles are the key to encouraging a virtuous cycle of growth:

- ***Promote what is already moving.*** The private sector is generally better than the Government at identifying opportunities for growth. In recent years, SMEs and manufacturers have been expanding, with this expansion expected to continue into the future as the result of demographics. With the entry of six million post-primary educated youth into the workforce this decade, the rate of growth of non-agricultural sectors is likely to become increasingly significant. If the majority of school graduates and others of working age are employed productively, the youth bulge will yield a demographic dividend. However, if a significant proportion of school leavers and other young people cannot find employment and earn a satisfactory income, it may instead become a potential source of social and political instability. For the government, policy should focus not so much on encouraging the establishment of small innovative businesses, but on staying out of the way to allow them to expand and become competitive. However, there is evidence to suggest that policymakers can assist innovative businesses by facilitating access to credit, information, skills, and markets.[27] Such assistance should be provided in a fashion that encourages competition: otherwise, it may have a negative impact on productivity, productivity growth, and product innovation.[28]

26 The registration rate of new SMEs per 1000 habitants is about 2.5 in Malaysia in 2009, which is four times faster than in Uganda or 3 times faster than in Kenya (Tanzania is not in the sample). Source: World Bank Group Entrepreneurship Snapshots 2010.

27 M. Dutz, I. Kessides, S. O'Connel, and R. Willig, *Competition and Innovation Driven Inclusive Growth*, World Bank. Policy Research Working Paper, N. 5852, 2011.

28 In other terms, targeted assistance should not occur in sector with low competition or should not be concentrated on one or small number of firms in the sector. See, P. Aghion et al., *Industrial Policy and Competition*, mimeo, June 2011.

How to get long lasting benefits from foreign investors: The lesson from Asia

Foreign firms are mobile, and they may locate in a country on a temporary basis. This is especially true in textile, ICT or light manufacturing where fixed capital requirements are small and obsolete very quickly. The challenge for the host country is therefore to get long-term benefits from possibly short term investments.

The lesson from East Asia is straightforward: success lies in the number of locally trained workers because they are the country's main asset. Not only training of local workers employed by the foreign company but also of those used by local suppliers and distributors. The good news with training is that it is also beneficial to investors since trained local staffs are generally more productive and cheaper than expatriates. Yet, there is a risk that training will be underused since firms might be afraid to see their employees leaving the company or they might reluctant to spend short financial resources on a long term gain.

Malaysia offers an example where training was part of its central strategy. Not only this activity was explicit in every contracts negotiated with potential investors, including for public works, but also the Government took initiatives towards providing training, aimed at encouraging the role of the private sector and reducing the role of the government in training activities. The following initiatives were introduced:

• Promoting private sector participation in human resource planning through membership in institutions such as the National Vocational Training Council.

• Promoting the role of the private sector in the provision of training through tax deduction on training expenses in approved institutions; the establishment of a Human Resource Development Fund (HRDF) with private sector steering imposing a levy of 1 per cent of employees' wages which employers can partly reclaim for training budgets; as well as through a liberalization of regulation of private sector training.

• Promoting the sharing of public and private sector training resources, through exchange of trainers or allowing the use of public training facilities.

- The encouragement of skill and technology transfers: In addition to providing financing, outside investors may facilitate skill and technology transfers. The Government should establish the appropriate regulatory and institutional framework to minimize possible conflicts of interests and abuse of powers in sectors with quasi-natural monopoly structures and to encourage skill and technology transfers. Encouraging the provision of skills to and training of local workers should be a top priority of Tanzanian policymakers, as these workers will become an important part of the nation's human capital and provide a basis for ongoing, future growth (see box). As the experience of the Asian tigers demonstrates, every trained employee has the potential to serve as a teacher and/or entrepreneur. The appropriate transfer of skills through partnerships will result in a upgrading of the country's skill base and will ensure a more efficient and effective use of technologies and machines.[29]

- ***Diversification of exports***: The recent dramatic increase in the volume of the manufacturing exports to non-OECD countries is good news for Tanzania. First, opportunities for spillovers are boosted through job creation and supplier as well as distribution networks.[30] Second, the growing intra-regional trade encourages increased product diversity because trading partners have similar endowments and factor allocation.[31] Finally, a decreased emphasis on the OECD market allows for the decoupling of the Tanzanian economy from business cycles in the North and for increased participation in the highly prospective regional and Asian markets.[32]

This economic update indicates that with care, diligence and commitment, Tanzanian policymakers may be able to successfully seize the opportunity to encourage and direct the incipient transformation of the nation to ensure that this transformation results in both economic growth and an improved standard of living for all members of society. An increasing number of Tanzanians have access to the Internet, mobile phone technology, and an improved transportation infrastructure, fostering a dramatically higher degree of virtual and physical connectivity. Urbanization is encouraging the development of small, innovative businesses and facilitating the movements of goods, services, and ideas. An increasing number of Tanzanians have received the education required to increase their productivity. These changes have resulted in irreversible structural changes to the way people live, communicate and think. It is the responsibility of Tanzanians policymakers to ensure that these structural changes yield the highest possible level of benefits to all of the nation's stakeholders.

29 These complementarities between skills and capital are at the basis I economic development for Damon Acemoglu. See, D. Acemoglu and F. Zilibotti, *Productivity Differences*, Quarterly Journal of Economics, 116, pp. 563-606.May 2001

30 For more empirical evidence, see Hausmann, Ricardo, Jason Hwang, and Dani Rodrik. 2007. *What You Export Matters*. Journal of Economic Growth 12(1): 1–25.

31 For such argument, see J. Regolo, *Export Diversification: How Much Does the Choice of the Trading Partner Matter?*, November 2011.

32. O. Canuto, M.Haddad, and G.Hanson, *Export-led Growth v2.0*, PREM Notes, N. 148, March 2010.

Statistical Annexes

Statistical Annexes

1. Key macroeconomic indicators

Indicator	Unit	2000	2005	2007	2008	2009	2010	2011*
Population (Mainland)/2	Millions	31.9	36.2	38.3	39.4	42.9	43.7	45.0
Per capita Income/2	US$	319.3	390.7	439.3	525.4	498.1	524.0	523.6
GDP Growth/2	%	4.9	7.4	7.1	7.4	6.0	7.0	5.8
Gross Domestic Savings/2	(as a % of GDP)	10.1	16.2	12.8	16.1	17.0	16.9	16.2
Gross Investments/2	(as a % of GDP)	16.8	25.1	29.6	29.8	29.0	28.9	28.6
Inflation/2 (period average)	%	6.0	4.4	7.0	10.3	12.1	7.2	12.0
Exchange Rate/1 (period average)	TZS/US$	800.4	1128.9	1245.0	1197.2	1320.3	1410.2	1578.2
External Sector								
Exports - Goods & Services/1	Mil. US$	1307.1	2843.4	3750.7	4834.0	5086.4	5736.7	7099.3
Imports - Goods & Services/1	Mil. US$	-2063.9	-3852.7	-5684.4	-7541.9	-7875.9	-8334.4	-9951.3
Current Account Balance/1	Mil. US$	-437.8	-703.9	-1,575.6	-2,255.7	-2,237.9	-2,085.4	-2,283.2
Balance of Payments (Overall balance)/1	Mil. US$	56.9	55.5	232.6	500.2	18.1	477.6	99.7
Foreign Reserves/1	Mil. US$	1,183.8	2,247.4	2,157.3	2,660.0	2929.8	3,482.6	3,610.3
External Debt/2	Bil. US$/1	6.9	8.3	4.7	5.8	7.0	8.2	10.0
Foreign Direct Investment/1	Mil. US$	463.4	689.0	492.3	490.8	407.8	423.8	443.6
Tourism Earnings/2	Mil. US$	739.1	823.6	1037.0	1198.8	1160.0	1250.0	#N/A
Monetary Sector								
Average Deposit Rate/1	%	7.4	4.7	8.7	8.3	8.0	6.6	#N/A
Average Lending Rate/1	%	21.6	15.2	16.1	15.0	15.0	14.5	#N/A
Growth in Money Supply (M2)/1	%	-1.7	22.6	25.9	20.5	26.6	19.5	26.2
Government Finance								
Total Domestic Revenue/1	(as a % of GDP)	10.0	11.8	14.1	15.9	16.2	15.9	16.5
Tax Revenue/1	(as a % of GDP)	9.0	10.8	13.0	14.7	15.3	14.6	15.2
Non-Tax Revenue/1	(as a % of GDP)	1.0	1.1	1.1	1.2	0.9	1.2	1.3
Total Expenditure/1	(as a % of GDP)	17.0	22.3	23.0	22.8	25.7	27.5	27.2
Recurrent Expenditure/1	(as a % of GDP)	10.5	15.4	16.1	14.9	17.7	18.8	19.2
Development Expenditure/1	(as a % of GDP)	4.7	6.3	6.9	7.9	8.0	8.6	7.9
Grants/1	(as a % of GDP)	4.0	6.8	4.9	6.9	4.7	4.6	4.7
Fiscal Balance (after grants)/1	(as a % of GDP)	-3.0	-3.6	-4.0	0.0	-4.8	-7.0	-6.0

Note

/1 Fiscal year is used, and it ends June 30th of the mentioned year

/2 Calendar year is used, and it ends in mentioned year December 31th.

* Preliminary estimates

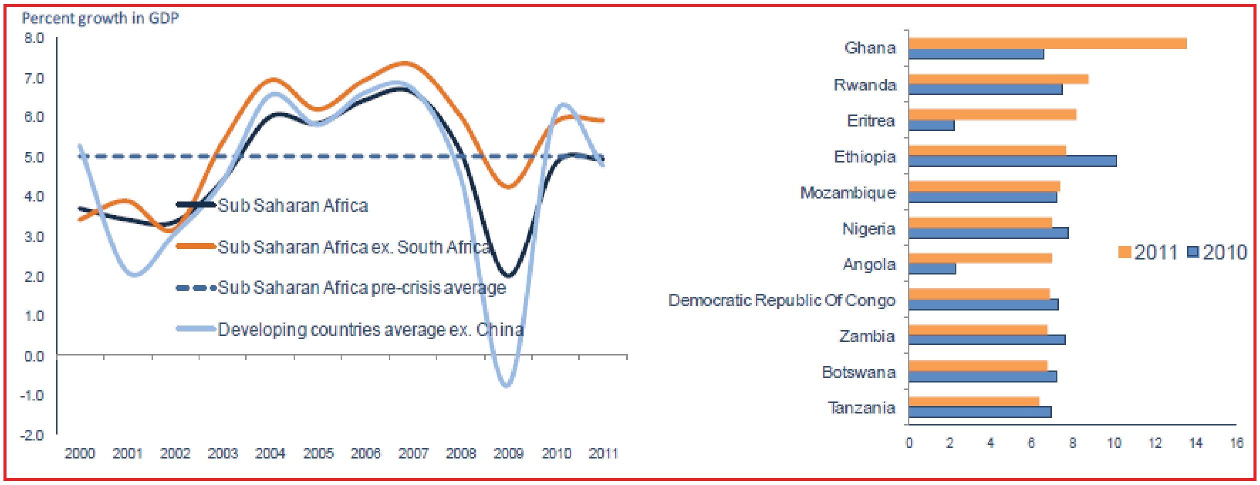
Source: IMF and Tanzania Authorities (MoF, BoT, NBS,).

2. GDP per capita over the past two decades

	1990	1995	2000	2005	2006	2007	2008	2009	2010
Constant 2005 international $									
Tanzania	860	798	866	1065	1105	1151	1201	1237	1286
Sub-Saharan Africa	1617	1504	1569	1759	1831	1909	1966	1967	2017
Uganda	563	671	774	911	977	1025	1079	1121	1141
Kenya	1421	1315	1283	1346	1395	1455	1441	1440	1477
East Asia & Pacific	1394	2123	2730	3911	4303	4793	5162	5507	5991
In comparison to Tanzania (multiplier)									
Sub-Saharan Africa	1.9	1.9	1.8	1.7	1.7	1.7	1.6	1.6	1.6
Uganda	0.7	0.8	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Kenya	1.7	1.6	1.5	1.3	1.3	1.3	1.2	1.2	1.1
East Asia & Pacific	1.6	2.7	3.2	3.7	3.9	4.2	4.3	4.5	4.7

Source: World Bank Indicators

3. Growth performance: Regional comparison



Source: World Bank, Global Economic Prospects, 2012.

4. Growth and structure of the economy

Economic Activity	2005	2006	2007	2008	2009r	2010p	2011*
Real GDP growth rates (%)							
Agriculture and fishing	4.3	3.8	4.0	4.6	3.2	4.2	3.6
Industry and construction	10.4	8.5	9.5	8.6	7.0	8.2	7.0
Services	8.0	7.8	8.1	8.5	7.2	8.2	6.4
Gross domestic product at market prices	7.4	6.7	7.1	7.4	6.0	7.0	5.8
Shares of GDP (%) 2001 prices							
Agriculture and fishing	27.7	27.0	26.2	25.5	24.8	24.1	23.6
Industry and construction	20.2	20.5	20.9	21.2	21.4	21.6	21.8
Services	46.4	46.9	47.3	47.8	48.3	48.8	49.1
FISIM and net taxes	5.7	5.7	5.6	5.6	5.5	5.5	5.4
Contribution to real GDP growth (%)							
Agriculture	1.3	1.1	1.1	1.2	0.8	1.0	0.9
Industry	2.0	1.7	1.9	1.8	1.5	1.8	1.5
Services	3.7	3.6	3.8	4.0	3.4	3.9	3.1
FISIM and net taxes	0.4	0.3	0.3	0.4	0.3	0.3	0.3
Shares of GDP by type of expenditure (%)							
Final consumption expenditure	83.8	85.5	87.2	83.9	83.0	82.8	83.4
Households	66.3	68.0	67.9	66.4	65.5	64.7	65.2
Government	17.6	17.5	19.3	17.4	17.5	18.2	18.2
Gross capital formation	25.1	27.6	29.6	29.8	29.0	28.9	28.6
Gross fixed capital formation	24.7	27.2	29.2	29.4	28.4	28.4	28.1
Changes in inventories	0.4	0.4	0.4	0.4	0.5	0.4	0.4
Net exports	-8.9	-13.1	-16.9	-13.6	-11.9	-11.7	-12.0
Gross domestic saving (% of GDP)	16.2	14.5	12.8	16.1	17.0	17.2	16.6
Public	-3.0	-2.1	-1.4	1.1	0.5	-0.2	1.7
Private	19.2	16.6	14.2	15.1	16.6	17.3	14.9

Key: *= estimates, r= revised, p= preliminary actual

Source: National Bureau of Statistics, IMF and Bank Estimates

THE WORLD BANK

5. Fiscal framework as % of GDP

	2005/06		2007/08		2008/09		2009/10		2010/11		2011/12
	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Actual	Budget	Actual	Budget
Total domestic revenue	12.2	12.5	15.3	15.9	17.9	16.2	16.9	15.9	17.8	16.5	17.7
Tax revenue	11.2	11.5	14.0	14.7	16.8	15.3	15.6	14.6	16.2	15.2	15.8
Nontax revenue	1.0	1.1	1.4	1.2	1.1	0.9	1.3	1.2	1.5	1.3	1.8
Total expenditure	23.8	22.8	26.3	22.8	26.9	25.7	29.8	27.5	31.0	27.2	32.1
Recurrent expenditure	15.6	15.7	16.6	14.9	17.6	17.7	20.7	18.8	20.0	19.2	19.6
Development expenditure	8.2	7.1	9.6	7.9	9.3	8.0	9.1	8.6	11.0	7.9	12.5
Overall deficit before grants	-11.6	-10.3	-10.9	-6.9	-9.0	-9.5	-12.9	-11.6	-13.2	-10.6	-14.5
Grants	6.1	5.4	7.4	6.9	5.4	4.7	6.7	4.6	5.8	4.7	6.9
Program	2.1	2.0	2.7	2.7	2.0	2.3	2.7	3.1	1.8	3.1	2.8
Project	2.0	1.9	3.0	2.8	2.3	1.2	2.7	1.5	3.4	1.1	2.9
Basket support	1.4	1.0	0.8	0.9	0.8	1.0	0.9	0.9	0.6	1.0	1.0
HIPC, MDRI (IMF, IDA and Afdb)	0.6	0.5	0.9	0.5	0.2	0.3	0.4	0.1	0.0	0.0	0.0
Overall deficit after grants	-5.6	-4.9	-3.5	0.0	-3.6	-4.8	-6.2	-7.0	-7.4	-6.0	-7.6
Expenditure float	0.0	-0.9	0.0	-1.3	0.0	-0.8	0.0	-1.4	0.0	-1.4	0.0
Adjustment to cash	0.0	0.4	0.0	-0.3	0.0	1.0	0.0	2.0	0.0	0.5	0.0
Overall balance	-5.6	-5.5	-3.5	-1.7	-3.6	-4.5	-6.2	-6.4	-7.4	-6.9	-7.6
Financing	5.6	5.5	3.5	1.7	3.6	4.5	4.9	6.4	7.4	6.9	7.6
Foreign (net)	3.5	3.3	3.6	3.2	3.5	3.6	3.3	4.6	5.6	3.3	6.1
Domestic (net)	2.1	2.1	-0.1	-1.5	0.1	1.0	1.6	1.9	1.8	3.6	1.0

6. Public Accounts –real annual increase

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
Total domestic revenue	16%	23%	26%	10%	-3%	13%
Tax revenue	16%	24%	27%	12%	-2%	9%
Import Duty	67%	22%	13%	16%	-10%	12%
Value Added Tax	14%	-2%	19%	10%	1%	0%
Excise Duties	5%	93%	21%	7%	-2%	15%
Income Tax	18%	24%	31%	16%	-3%	14%
Other Taxes	0%	54%	69%	12%	-4%	10%
Nontax revenue	8%	12%	25%	-18%	-18%	79%
Total Expenditure	18%	10%	10%	22%	8%	5%
Recurrent Expenditure	23%	12%	2%	29%	7%	10%
Wages and salaries	15%	43%	10%	33%	-5%	26%
Interest	49%	-7%	17%	-17%	-9%	31%
Domestic	83%	7%	22%	-21%	-12%	27%
Foreign	-5%	-50%	-16%	19%	5%	56%
Goods, services and transfers	24%	3%	-4%	33%	15%	1%
Development Expenditure	9%	5%	29%	9%	11%	-5%
Locally financed	19%	64%	6%	51%	-1%	-12%
Foreign financed	6%	-14%	43%	-10%	19%	-1%
Overall deficit before grants	22%	-6%	-16%	52%	28%	-5%
Grants	22%	-1%	59%	-28%	0%	5%
Program	-13%	39%	24%	-12%	-2%	-1%
Project	145%	-32%	157%	-58%	32%	13%
Basket Support	9%	-42%	71%	25%	-14%	19%
HIPC, MDRI (IMF, IDA and Afdb)	2%	50%	-10%	-49%	-79%	-111%
Overall deficit after grants	22%	-12%	-106%	103304%	55%	-12%
Expenditure Float	8%	-22%	121%	-36%	90%	0%
Adjustment to cash	-16%	-140%	220%	-460%	107%	-84%
Overall balance	23%	-4%	-66%	209%	49%	13%
Financing	23%	-4%	-66%	209%	49%	13%
Foreign (net)	-8%	22%	-5%	21%	34%	-27%
Program Loans	290%	-2%	30%	-18%	57%	-79%
Project loans	-34%	26%	-58%	125%	31%	-18%
Basket Support	-52%	-48%	318%	-33%	16%	3%
Domestic (net)	146%	-45%	-265%	-182%	105%	112%

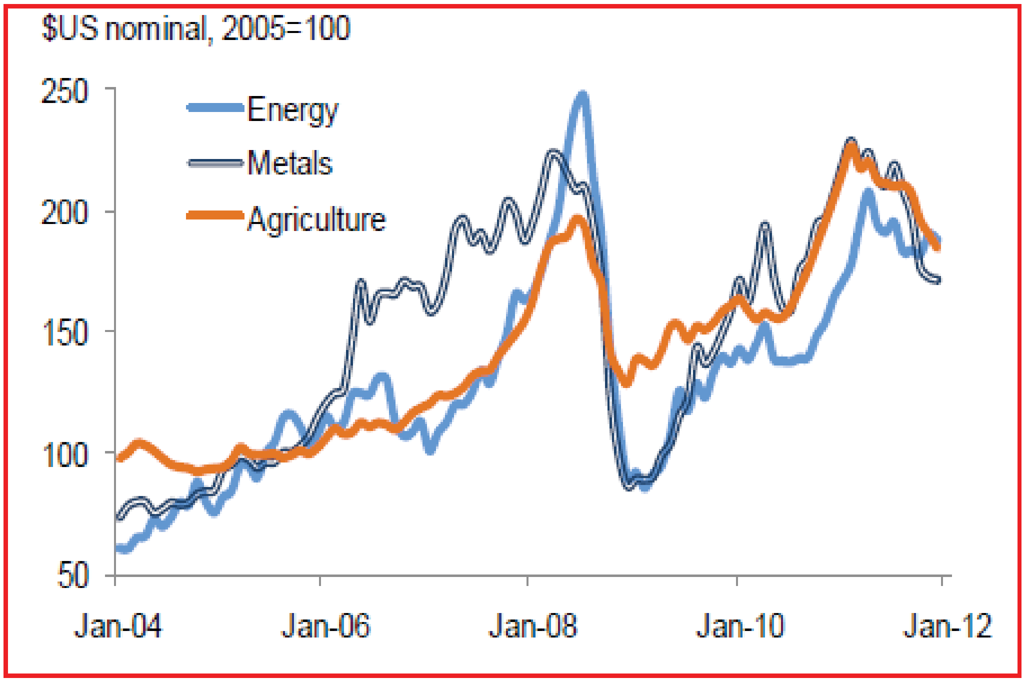
Source: Ministry of Finance

7. Balance of payments, % of GDP unless otherwise indicated

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12 Proj
1. CA balance (including grants)	-8.2	-10.4	-11.9	-10.7	-9.2	-9.8	-10.1
Exports of Goods	12.5	13.4	15.3	15.6	16.8	21.0	24.5
o/w Gold	4.8	5.4	5.5	4.4	6.6	7.7	9.3
Import of Goods	-24.0	-28.6	-31.6	-29.7	-29.0	-34.5	-37.8
Services (net)	1.1	2.4	2.1	0.8	0.8	1.2	1.4
Trade balance	-10.4	-12.7	-14.2	-13.3	-11.5	-12.3	-11.9
Income (net)	-1.2	-1.1	-1.2	-0.9	-0.7	-0.8	-1.2
Current transfers (net)	3.4	3.4	3.6	3.5	2.9	3.3	3.1
2. Capital and financial account	9.3	9.8	11.3	8.0	9.9	9.4	11.2
Capital account	4.1	31.6	3.6	1.8	2.7	2.4	2.6
Financial account	5.2	-21.7	7.7	6.2	7.2	7.0	8.6
o/w Direct investment	4.7	3.2	2.6	1.9	1.9	1.9	2.3
3. Overall balance	2.4	1.5	2.6	0.1	2.1	0.4	1.1
Gross international reserves(Mil USD)	1863	2157	2660	2930	3483	3610	3868
In months of imports (current year)	4.8	4.6	4.2	4.5	5.0	4.4	4.1

Source: BoT, IMF and World bank

8. International commodity prices, 2004-12



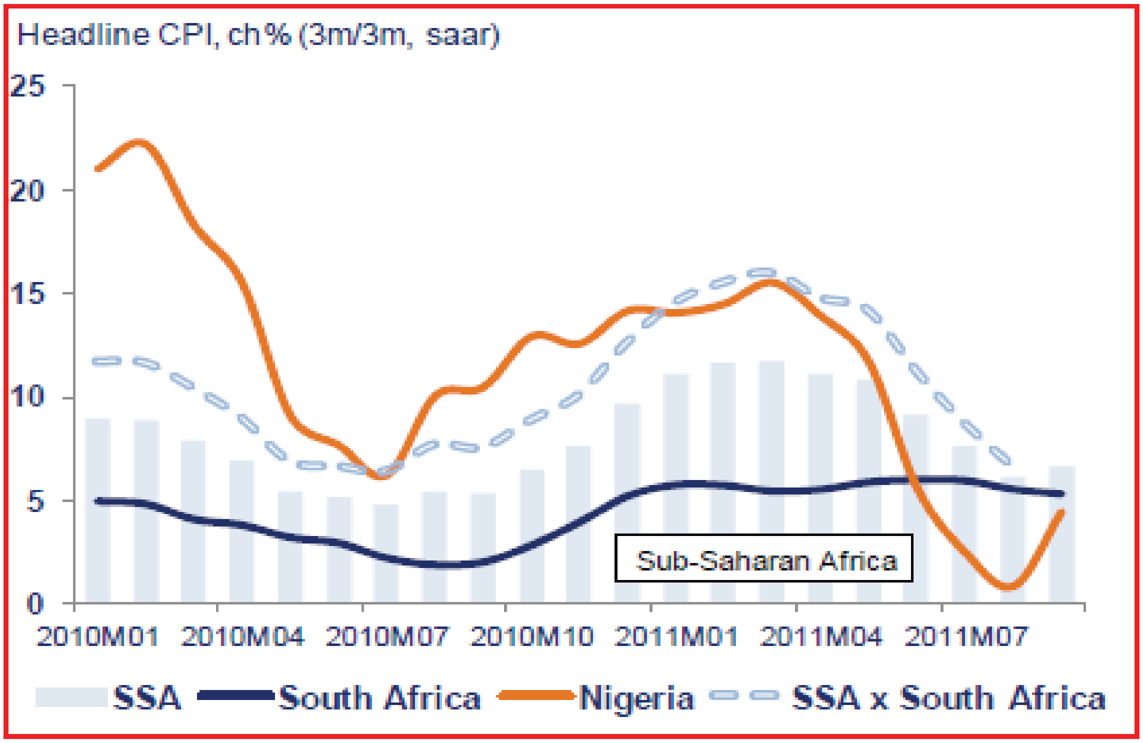
Source: World Bank.

9. Annual inflation rates

Percentage changes	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011*
CPI (annual average)	5.1	4.6	4.4	4.1	4.4	7.3	7.0	10.3	12.1	7.2	12.0
CPI (end-of-period)	4.9	4.4	4.6	4.1	5.0	6.7	6.4	13.5	12.2	5.6	15.6
Food (end of period)	6.1	2.9	5.8	5.0	7.2	6.6	6.6	18.6	14.5	7.3	20.1
Non Food (end of period)	1.5	8.8	1.1	2.9	2.0	6.8	6.2	5.8	8.5	3.8	11.3

* Estimates

10. Inflation Rate (CPI): Regional comparison, 2010-11



Source: World Bank Global Prospects, 2012.

11. Monthly Food Crop Prices (Wholesale) in Arusha, Dar es Salaam, and Mbeya: Tsh per 100 kg.

Crop	Maize			Rice			Wheat			Beans			Sorghum		
Month-Year	Arusha	Dar es Salaam	Mbeya	Arusha	Dar es Salaam	Mbeya	Arusha	Dar es Salaam	Mbeya	Arusha	Dar es Salaam	Mbeya	Arusha	Dar es Salaam	Mbeya
Oct-11	40,250	47,896	39,917	151,458	142,083	148,500	73,542	108,333	93,750	107,083	141,625	143,125	48,833	71,750	-
Sep-11	43,308	47,673	38,385	143,462	128,500	114,769	76,154	96,923	83,269	124,808	127,269	121,000	53,000	78,731	-
Aug-11	43,778	51,778	37,636	134,444	132,944	109,591	73,889	98,333	77,273	107,222	133,222	121,136	55,611	73,333	-
Jul-11	49,636	50,313	37,227	130,000	124,583	108,500	80,000	92,000	89,545	106,000	128,000	115,682	49,688	75,208	-
Jun-11	43,000	41,500	33,000	125,000	115,000	90,000	60,000	85,000	45,000	100,000	111,500	120,000	45,000	40,000	-
May-11	46,904	44,271	38,375	122,292	122,500	108,125	71,667	86,875	82,083	109,167	127,500	123,292	49,500	65,208	-
Apr-11	40,000	42,700	37,135	116,750	128,000	112,250	70,000	84,722	65,500	105,000	112,250	124,500	52,889	59,480	65,000
Mar-11	35,875	40,625	39,206	111,875	115,625	113,125	75,000	75,000	63,438	94,429	128,125	135,000	54,375	57,500	70,000
Feb-11	32,361	39,000	33,500	109,000	111,300	104,650	60,556	79,722	60,100	108,056	109,550	121,000	42,278	57,750	50,800
Jan-11	31,083	35,479	32,208	117,667	99,167	97,833	57,917	93,917	51,375	100,625	99,167	100,938	41,250	65,000	25,000
Dec-10	28,500	32,400	30,100	102,800	99,500	90,075	57,700	94,000	50,000	97,000	106,000	98,525	47,000	62,250	
Nov-10	27,083	32,958	29,000	99,667	93,958	89,042	57,917	88,333	50,000	88,542	100,417	94,583	52,708	58,750	
Oct-10	26,750	32,813	28,583	93,700	82,550	78,675	60,000	82,100	48,722	94,600	87,889	88,750	48,500	60,000	81,000
Sep-10	28,800	29,650	29,100	97,000	88,250	79,025	55,000	87,000	46,222	89,600	99,500	90,500	40,500	59,000	56,250
Aug-10	26,923	28,981	29,442	95,000	94,231	79,000	53,923	83,692	46,500	83,962	103,462	85,923	46,769	54,423	
Jul-10	24,500	27,375	24,708	95,000	96,325	77,396	57,500	81,708		85,500	103,042	85,000	49,000	53,875	
Jun-10	26,000	28,269	22,962	95,000	102,731	80,308	57,500	81,173	49,000	95,625	112,538	88,636	45,000	55,696	
May-10	31,042	33,875	24,208	101,042	102,783	89,750	65,313	85,208	51,875	96,667	111,875	89,438	48,571	56,614	
Apr-10	37,917	34,875	32,125	105,417	107,667	95,000	62,500	90,000	49,583	100,000	112,500	90,917	52,250	54,750	
Mar-10	39,904	36,455	35,808	105,577	110,923	103,942	61,538	85,000	49,308		114,231	94,712	47,308	58,846	
Feb-10	44,500	47,270	35,625	110,000	115,833	105,000	65,000	85,313		107,500	111,479	101,250	46,250	58,625	
Jan-10	43,625	48,021	37,125	110,000	111,625	107,708	64,750	85,000	48,083	111,250	116,583	104,458	48,250	58,292	

Source: Ministry of Industry, Trade, and Marketing (MITM), Government of Tanzania

12. Inflation rates (selected items of the CPI basket)

Inflation rates(y/y), end of period	2010 Oct	2010 Nov	2010 Dec	2011 Jan	2011 Feb	2011 March	2011 April	2011 May	2011 June	2011 July	2011 Aug	2011 Sept	2011 Oct
All items (end period)	4.2	5.5	5.6	6.4	7.5	8.0	8.6	9.7	10.9	13.0	14.1	16.8	17.9
Food	4.4	6.0	6.3	6.7	8.6	8.3	9.2	10.1	11.7	14.8	17.4	21.3	22.8
Non food	3.9	4.9	4.7	6.1	6.1	7.7	7.8	9.3	10.0	10.8	10.2	11.5	12.2
Energy and Fuel	6.8	14.6	12.3	19.1	13.0	17.2	22.1	24.5	29.0	34.2	30.1	33.1	37.4
Transport	-1.0	0.1	0.6	0.3	0.3	3.3	3.9	8.0	8.4	9.9	8.8	10.8	11.8
Housing, water, electricity and Gas	10.2	14.4	12.1	17.7	11.1	13.6	13.4	15.7	18.8	21.3	19.7	21.7	22.0
Furnishing, housing equipment	3.5	4.6	5.7	7.2	13.9	14.5	13.6	14.1	14.4	14.5	13.9	14.2	15.4
Excluding food and energy	3.5	3.7	3.7	4.4	5.2	6.3	5.7	7.1	7.2	7.4	7.3	8.2	8.5

Source: NBS and IMF

13. Average Wholesale Price (January to October 2011) in TShs./100kg

	Jan 2011	Feb 2011	Mar 2011	Apr 2011	May 2011	Jun 2011	July 2011	Aug 2011	Sept 2011	Oct 2011
Maize	35,086	37,451	40,252	41,841	41,943	41,915	44,639	41,994	42,195	42,453
Rice	104,134	105,614	113,578	119,119	123,767	112,200	126,505	121,561	129,661	143,233
Beans	115,624	121,572	116,873	115,640	119,515	110,667	112,420	116,519	119,917	124,831
Round Potatoes	61,058	63,311	57,607	56,014	55,372	49,737	49,737	60,189	59,205	59,770
Bullrush Millet	51,300	52,651	58,222	56,540	58,495	56,773	67,526	65,284	59,166	67,642
Finger Millet	75,871	75,779	74,276	73,011	70,453	68,750	78,486	71,047	69,542	74,426
Sorghum	51,348	53,940	58,568	62,766	61,582	54,821	59,133	53,589	53,839	54,671
Wheat	74,559	74,604	85,484	87,978	90,594	78,875	89,977	86,354	81,252	81,139

Source: Ministry of Industry, Trade, and Marketing (MITM), Government of Tanzania

14. Nominal exchange rates and T-Bill Rates

	Tshs/USD*	Tshs/EUR*	T-Bill Rate
Jan-10	1,332.4	1,914.7	7.2
Feb-10	1,338.5	1,845.5	6.3
Mar-10	1,338.5	1,840.8	4.2
Apr-10	1,352.0	1,838.6	2.7
May-10	1,372.9	1,791.5	2.7
Jun-10	1,391.8	1,782.3	3.3
Jul-10	1,395.1	1,919.9	3.9
Aug-10	1,455.1	1,959.0	3.9
Sep-10	1,495.6	1,986.3	5.1
Oct-10	1,495.5	2,078.8	5.7
Nov-10	1,417.3	2,037.6	5.9
Dec-10	1,397.2	1,938.2	6.3
Jan-11	1,486.8	1,998.2	7.1
Feb-11	1,505.5	2,058.0	6.6
Mar-11	1,508.5	2,118.2	5.5
Apr-11	1,510.4	2,181.1	4.8
May-11	1,521.5	2,187.9	4.5
Jun-11	1,562.0	2,281.4	4.8
Jul-11	1,577.3	2,259.8	6.4
Aug-11	1,617.0	2,313.5	7.3
Sep-11	1,636.5	2,258.9	7.8
Oct-11	1,671.0	2,294.6	11.6

Source: IMF, period average

15. Monetary indicators

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12 P
Monetary aggregates							
M3 as % of GDP	26.0	26.7	26.7	27.8	30.4	32.2	34.1
M2 as % of GDP	17.6	18.2	19.5	20.4	22.5	23.3	24.4
M3 growth rate (%)	31.3	20.1	18.1	18.5	25.1	22.0	20.0
M2 growth rate (%)	26.8	25.9	20.5	26.6	19.5	26.2	19.1
Domestic credit							
Total Domestic credit (% of GDP)	9.7	10.8	13.2	12.9	16.2	18.3	25.0
Total domestic credit growth (%)	24.7	42.3	15.7	43.4	29.0	57.3	7.4
Private credit (% of GDP)	11.7	14.0	16.0	18.0	18.4	22.9	21.5
Private credit growth (%)	31.3	34.5	32.9	33.1	16.7	42.6	8.0
Interest ratse structure/1							
Overall Tbills rate (%)	10.7	11.6	13.4	8.1	7.1	3.9	N/A
Average lending rate (%)	15.2	15.7	16.1	15.0	15.0	14.5	N/A
Average deposit rate(%)	4.7	6.7	8.7	8.3	8.0	6.6	N/A

P= Projections

Source: BoT, IMF

1/ Data in calendar year, e.g 2005/06 = 2005

THE WORLD BANK

http://www.worldbank.org/tanzania/economicupdate.