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United Republic of Tanzania: Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Request for Waiver of Performance Criteria—Staff Report; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for the United Republic of Tanzania

In the context of the fourth review under the three-year arrangement under the Poverty Reduction and Growth Facility and request for a waiver of performance criteria with the United Republic of Tanzania, the following documents have been released and are included in this package:

- the staff report for the fourth review under the three-year arrangement under the Poverty Reduction and Growth Facility and request for waiver of performance criteria prepared by a staff team of the IMF, following discussions that ended on June 2, 2005, with the officials of the United Republic of Tanzania on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 18, 2005. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a staff statement of July 29, 2005 updating information on recent economic developments.

- a Press Release summarizing the views of the Executive Board as expressed during the July 29, 2005 Executive Board discussion of the staff report that completed the review and request.

- a statement by the Executive Director for the United Republic of Tanzania.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of the United Republic of Tanzania*
Memorandum of Economic and Financial Policies by the authorities of the United Republic of Tanzania*

*May also be included in the staff report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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UNITED REPUBLIC OF TANZANIA

Fourth Review Under the Three-year Arrangement Under the Poverty Reduction and Growth Facility and Request for Waiver of Performance Criteria

Prepared by the African Department

(In consultation with the Finance, Fiscal Affairs, Legal, Monetary and Financial Systems, Policy Development and Review, and Statistics Departments)

Approved by David Nellor and Michael T. Hadjimichael

July 18, 2005

- **Discussions for the fourth review under the Poverty Reduction and Growth Facility (PRGF) were held in Dar es Salaam during May 17-June 2, 2005** by a staff team comprising Messrs. Sharer (head), Dohlman, Sobolev (all AFR), Adedeji (FAD), Ms. Reif (PDR), and Ms. Schmitz (Senior Resident Representative). The mission met with the Minister for Finance (Mr. Mramba), the Permanent Secretaries for Finance (Mr. Mgonja and Mr. Lyimo), the Governor of the Bank of Tanzania (BoT) (Mr. Ballali), other senior government officials, and representatives of the business, banking, and donor communities. At the end of its stay, the mission was received by President Mkapa.

- **The program remains on track, with all end-March 2005 quantitative performance criteria and indicative targets met (Appendix I, Table 1).** Net domestic financing of the government was below the program target consistent with continued strong fiscal performance, and targets for reserve money and net international reserves (performance criteria) were met.

- **All structural performance criteria and benchmarks through June were met or completed with minor delays with one exception (Appendix I, Table 2).** The submission of amendments to the BoT Act and the Banking and Financial Institutions Act (BFIA) to parliament (performance criteria) has been delayed from end-April until end-July, due to longer than expected consultations with the Zanzibari authorities and a tight legislative schedule. The authorities have requested waivers.

- **Completion of this fourth review will entitle Tanzania to a disbursement of SDR 2.8 million (Table 1).** The government's letter of intent (LOI) relating to this review is presented in Appendix I. Tanzania's three-year PRGF arrangement was approved on July 28, 2003, and has been in effect since August 16, 2003, in the amount of SDR 19.6 million (10 percent of quota).

- **At the completion of the third review under the PRGF arrangement on February 23, 2005, Executive Directors commended the authorities for Tanzania's strong macroeconomic performance and solid record in addressing key impediments to growth through structural reforms.** They noted, however, that reducing poverty will require continued reform efforts, in particular in the areas of fiscal management, the financial sector, energy, infrastructure, the business environment and governance. Directors welcomed the authorities' commitment to sustain key reforms, and to resist pressures for increased spending and undue direct government intervention in the run-up to the October 2005 elections.

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List of Acronyms

ADB	African Development Bank
BEST	Business Environment Strengthening in Tanzania
BFIA	Banking and Financial Institutions Act
BoT	Bank of Tanzania
CAS	Country Assistance Strategy
CPI	Consumer Price Index
DFGF	Development Finance Guarantee Facility
DFI	Development Finance Institution
DTIS	Diagnostic Trade Integration Study
EAC	East African Community
FDI	Foreign Direct Investment
FSAP	Financial Sector Assessment Program
FSRP	Financial Sector Reform Programme
GGCU	Good Governance Coordination Unit
GDDS	General Data Dissemination System
GDP	Gross Domestic Product
HIPC	Highly Indebted Poor Country
IDA	International Development Association
IFEM	Inter-Bank Foreign Exchange Market
IFMS	Integrated Financial Management System
ITA	Income Tax Act
ITRS	International Exchange Transactions Reporting System
LGA	Local Government Authority
LIC	Low-Income Country
LOI	Letter of Intent
LTFF	Long Term Financing Facility
LTD	Large Taxpayer Department
MDA	Ministries, Departments, and Agencies
MEFP	Memorandum of Economic and Financial Policies
MKUKUTA	Kiswahili name for NSGRP
MTEF	Medium-Term Expenditure Framework
NBS	National Bureau of Statistics
NDS	National Debt Strategy
NGO	Non-Government Organization
NMB	National Microfinance Bank
NPV	Net Present Value
NSGRP	National Strategy for Growth and Reduction of Poverty (new PRSP)
PFMRP	Public Financial Management Reform Program
PRBS	Poverty Reduction Budget Support
PRGF	Poverty Reduction and Growth Facility
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
PSD	Private Sector Development
PSRP	Public Service Reform Program
ROSC	Report on Observance of Standards and Codes
SADC	Southern African Development Community
SBAS	Strategic Budget Allocation System
SEZ	Special Economic Zone
SME	Small and Medium-Sized Enterprise
TANESCO	Tanzania Electric Supply Company
TASAF	Tanzania Social Action Fund
TRA	Tanzania Revenue Authority
VAT	Value-Added Tax

Executive Summary

- **Tanzania's sustained reforms have generated strong macroeconomic performance.** Nevertheless, per capita income remains very low, and Tanzania will need to maintain high growth, low inflation, and a steady pace of structural reforms for many years to achieve inroads against poverty. The authorities' new poverty reduction strategy paper—MKUKUTA in Kiswahili—provides a roadmap to achieve these objectives.

- **Performance under the program has remained strong.** All end-March 2005 quantitative performance criteria and indicative targets were met, and all structural performance criteria and benchmarks through June 2005 were met or completed with minor delays, with one exception. Plans to submit amendments to key banking legislation to parliament (end-April performance criteria) were delayed. The authorities have requested waivers and intend to complete these actions by end-July.

- **The main goals of the PRGF program are to achieve higher growth and further reduction of poverty. To this end, the program targets real growth of 6.9 percent (for CY 2005), inflation of 4 percent, and net domestic budget financing of 1.1 percent of GDP.** Essential to achieving these goals are the continuation of appropriate macroeconomic policies combined with key structural reforms. Risks mainly center around the vulnerability of the economy to drought and terms of trade shocks and pressures for more direct intervention and higher spending by government to address employment and poverty concerns, particularly in the run-up to the October 2005 elections.

- **Tanzania's fiscal strategy is focused primarily on facilitating the implementation of MKUKUTA, while enhancing domestic resource mobilization and limiting domestic financing to avoid crowding out the private sector.** In support of these goals, the program envisages a further increase in government expenditure to 26.8 percent of GDP. The authorities are also pushing ahead with significant reforms of revenue administration, budget transparency and accountability, and public expenditure management.

- **A principal challenge for monetary policy continues to be liquidity management in the face of high foreign aid inflows**. The 2005/06 (July/June) program proposes higher reserve money and M3 growth paths consistent with strong private sector demand for credit and subdued inflation. This should help ease pressures on interest and exchange rates and help meet growth and inflation objectives.

- **A comprehensive Financial Sector Reform Implementation Action plan has been completed**. Under the plan, efforts to remove key structural impediments to broaden access to financial services will be accelerated, including measures to facilitate increased medium- and longer-term lending, and streamline the pensions sector.

- **The staff supports the authorities' requests** for waivers for the nonobservance of the end-April structural performance criteria related to amendments of banking laws and for completion of the fourth review under the current PRGF arrangement.

I. Background

1. **Tanzania has made major strides over the past decade (Figure 1).** Per capita growth has accelerated to nearly 5 percent, inflation has declined to around 4 percent, official assistance has increased along with donor confidence, foreign reserves have risen to comfortable levels, the debt burden has fallen, expenditures in priority areas have increased, and poverty is declining. Institutional capacity has also improved, albeit from a weak base, including stronger structures for domestic revenue collection and expenditure management.

2. **Tanzania nevertheless has a long road ahead to overcome poverty (Figure 2).** Per capita income remains low, aid dependence is high, trade volume is comparatively low, and the financial sector—though growing rapidly—still plays only a limited role in the economy. The cost of doing business remains high, and basic infrastructure remains poor. Tanzania will need to sustain sound economic policies and reforms for many years to achieve lasting inroads against poverty.

II. Recent Economic Developments and Performance Under the Program

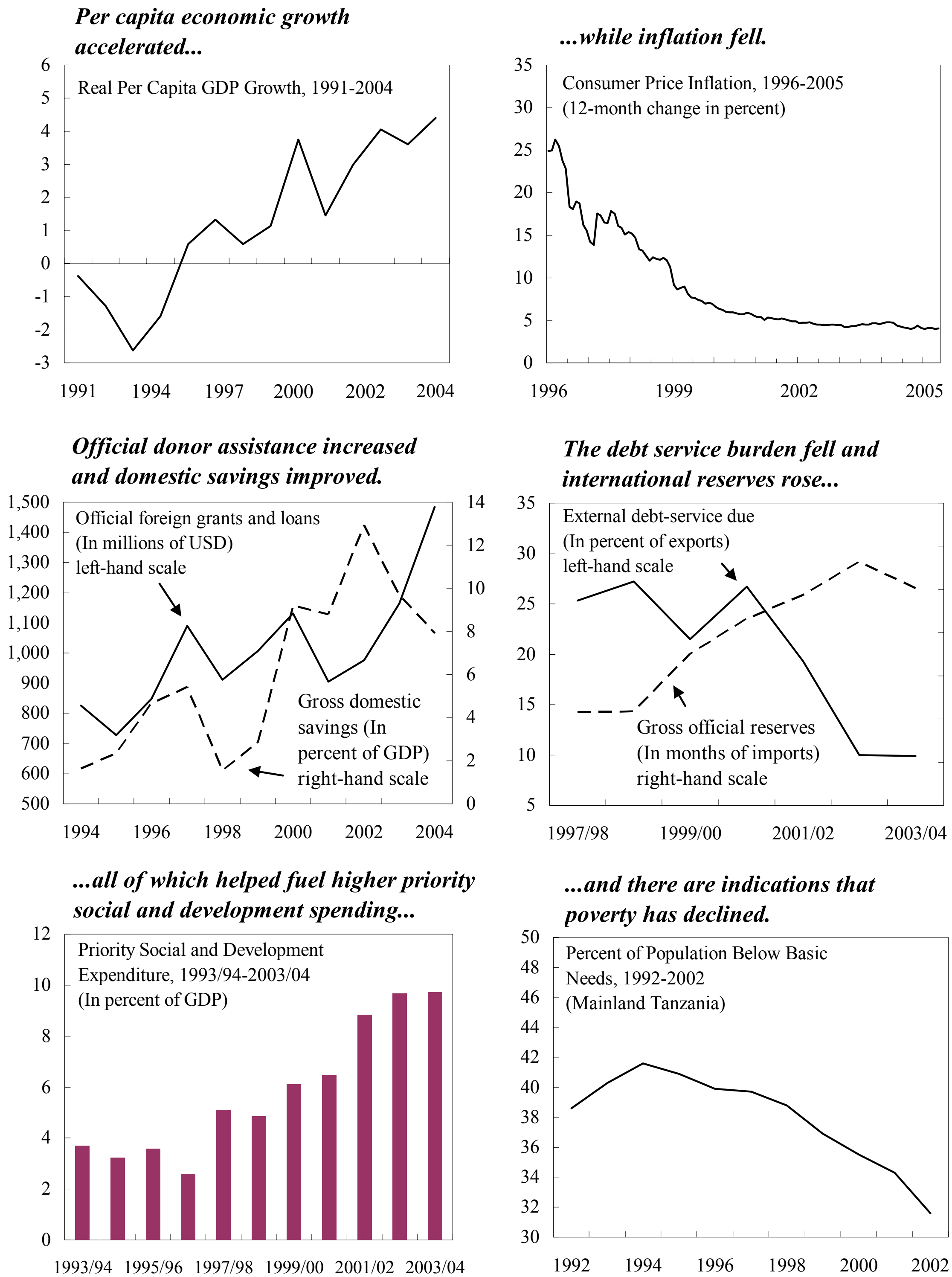
3. **Macroeconomic performance was better than projected (Table 2).** Real economic growth in CY 2004 reached 6.7 percent, compared with projected growth of 6.3 percent and 5.7 percent in 2003. Growth was broad-based, with agriculture (nearly half of GDP) receiving a boost from a return to normal weather and better access to inputs. Inflation (through May 2005) remained low at around 4 percent, with lower food prices offsetting higher fuel costs.

4. **Fiscal performance during 2004/05 was also somewhat stronger than envisioned with net domestic budget financing estimated at 0.6 percent of GDP, well below the program target of 1.3 percent of GDP** (partly reflecting the higher nominal GDP outturn) (Table 3). Revenues rose 22 percent, slightly more than programmed, driven by ongoing implementation of the Tanzania Revenue Authority's (TRA) reform program as well as growth in some high revenue impact sectors.[1] Expenditures rose by some 29 percent, broadly as programmed, mostly for priority sectors. Foreign financing marginally exceeded the program projection.

5. **Tanzania's estimated 2004/05 current account deficit was somewhat smaller than envisaged, partly due to stronger growth of traditional exports (Tables 2 and 6).** Good weather, the recovery of some commodity prices, and better access to inputs

[1] However, revenue as a percent of GDP was below expectations, as the higher-than-expected growth was concentrated in the agricultural sector, which has a relatively lower impact on revenues.

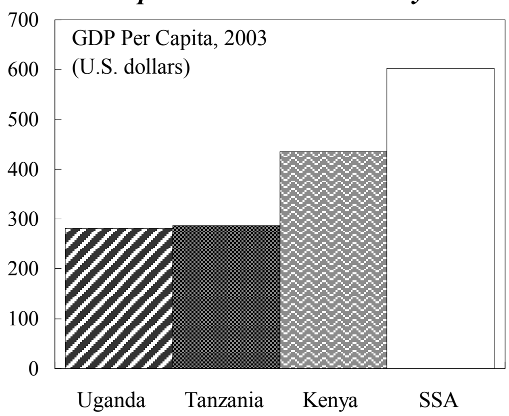
Figure 1. Reform Efforts Are Bearing Fruit



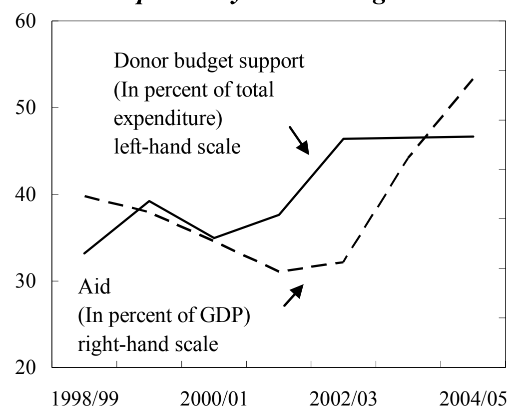
Sources: Tanzanian authorities and staff estimates.

Figure 2. But The Path Ahead Remains Long

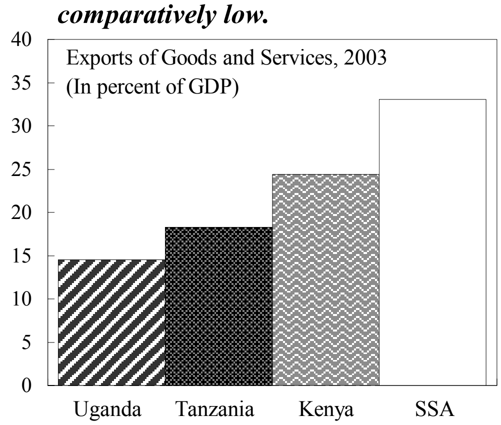
Per capita income remains very low.



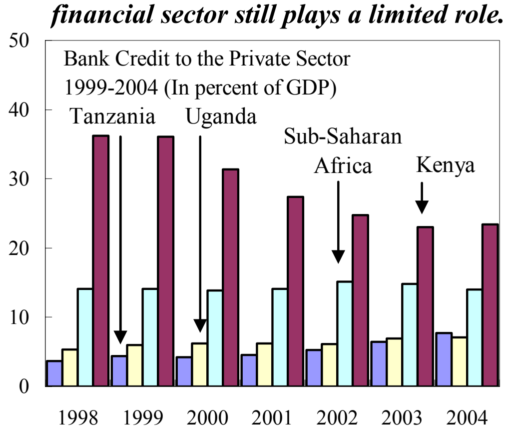
Aid-dependency remains high.



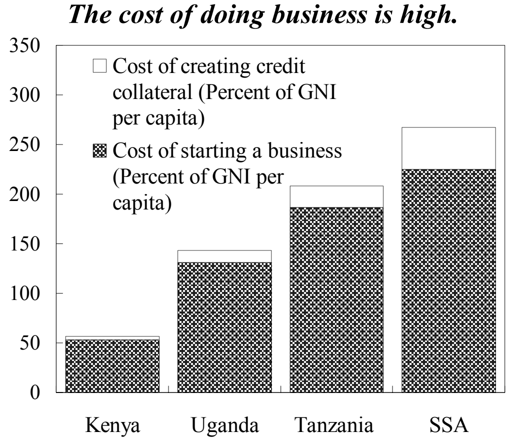
Exports of goods and services are comparatively low.



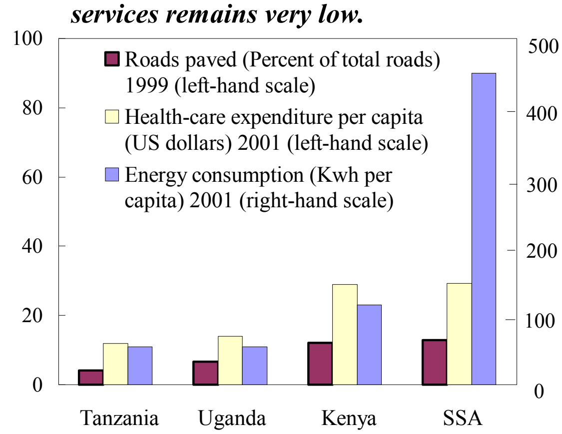
Despite sharp improvements, the financial sector still plays a limited role.



The cost of doing business is high.



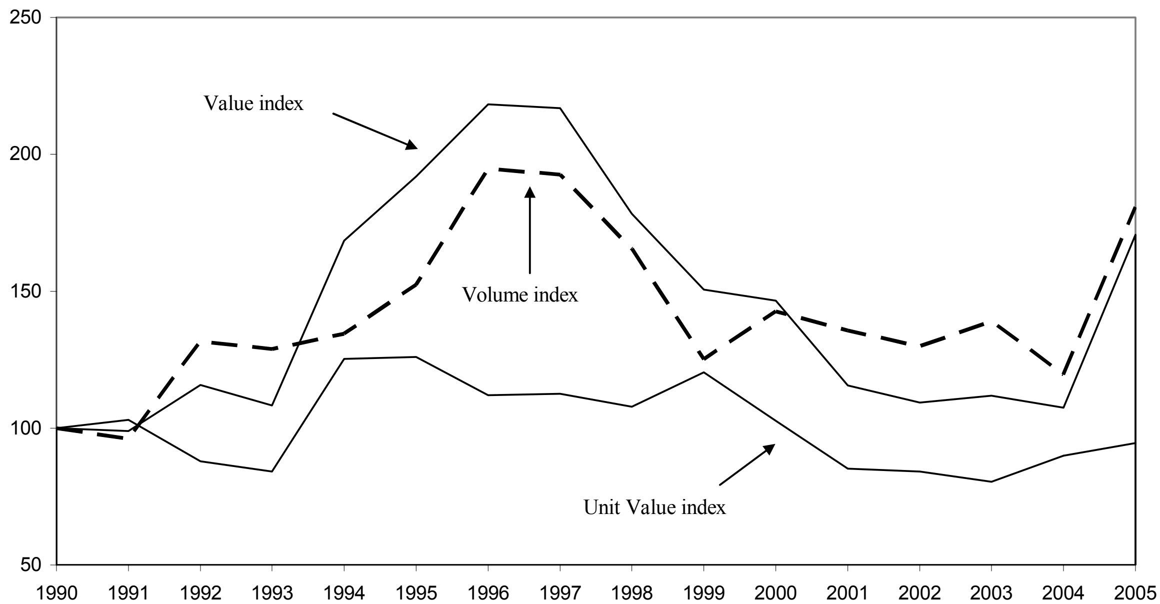
Provision of infrastructure and basic services remains very low.



Sources: Tanzanian authorities, World Economic Outlook, International Financial Statistics,World Bank, World Development Indicators, and African Indicators.

contributed to this outcome. It is noteworthy that the recovery in traditional exports has been driven more by increased production than prices (Figure 3). Nontraditional exports continued their robust performance, mainly gold, but also manufactures. Imports, particularly capital and intermediate goods, expanded as expected.[2] The current account deficit was financed by foreign assistance as well as higher FDI, which amounted to more than 4 percent of GDP.[3] Net inflows resulted in an increase in official gross reserves to US$2.1 billion, equivalent to about 6 months of imports.

Figure 3. Tanzania Traditional Exports: 1990-2005 (1990=100)



6. **The nominal exchange rate of the shilling to the U.S. dollar has remained mostly flat since the third review, but depreciated somewhat in real effective terms (Figure 4).** The staff continues to believe the exchange rate is aligned with fundamentals and is not hampering competitiveness.

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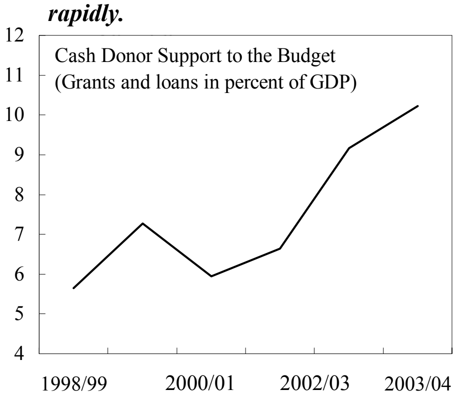
[2] Progress has been slow in harmonizing the remaining conflicts of the EAC protocol with other regional arrangements. However, these problems have not significantly disrupted intra-EAC trade.

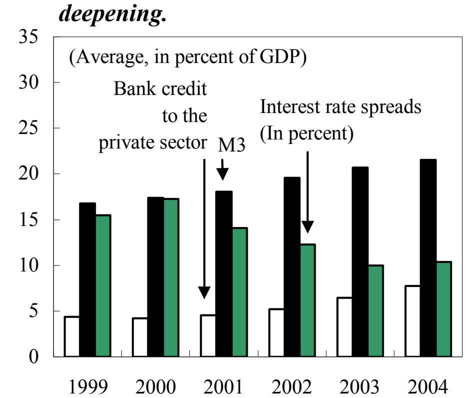
[3] FDI data were updated using a new survey (see Appendix IV), which indicates higher FDI inflows for the last three years. Most FDI inflows have been for mining (40 percent) and manufacturing (30 percent).

Figure 4. Challenges of Liquidity Management

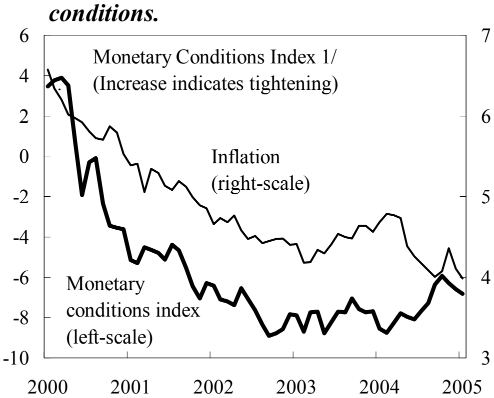
Aid inflows to the budget increased rapidly.



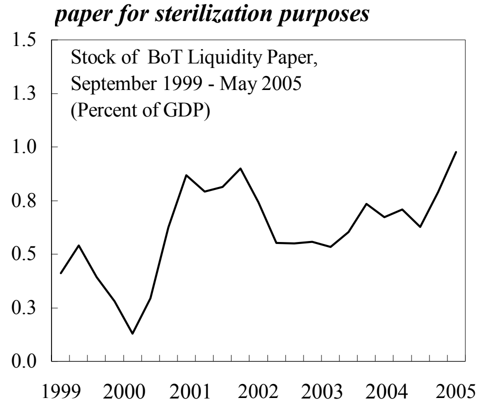
The resulting liquidity pressures were mitigated somewhat by financial deepening.



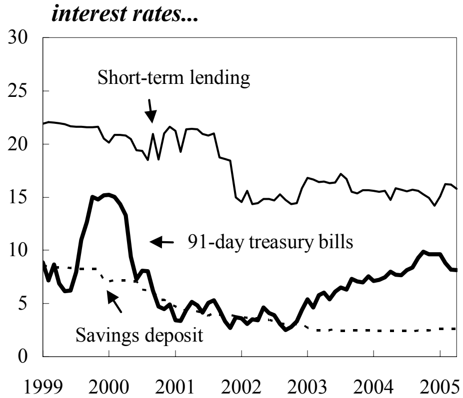
Sustained sterilization efforts resulted in low inflation and tightening of monetary conditions.



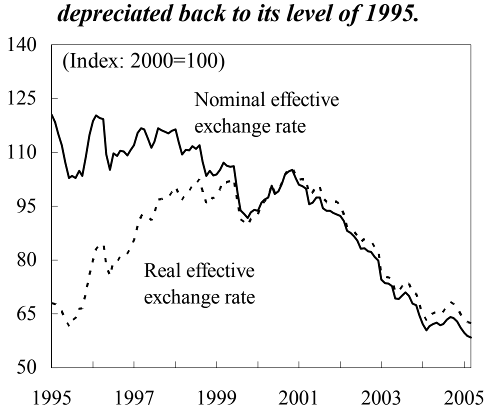
...however increased sales of liquidity paper for sterilization purposes



...have led to some upward pressure on interest rates...



...while the real exchange rate has depreciated back to its level of 1995.



Sources: Tanzanian authorities, Information Notice System, and staff estimates.

1/ Weighted sum of changes in the interest rate and the effective exchange rate relative to base period.

7. **The government continued negotiations with bilateral creditors for HIPC comparable debt relief.** Dialogue is moving ahead with the United Arab Emirates, Hungary, Iran, and Libya. The U.K. has committed to pay 10 percent of Tanzania's debt service obligations to IDA and ADB.

8. **Monetary policy has evolved in line with program goals** (Tables 4 and 5), amid continued challenges to liquidity management (Figure 4). Despite liquidity pressure emanating from high donor inflows, the BoT met the end-March 2005 reserve money target through sales of government paper, foreign exchange, and other measures. Reflecting the increased open market operations, interest rates paid on treasury bills rose during much of 2004/05.[4] The end-March performance criterion on net international reserves was also observed. M3 growth has accelerated at a faster than expected pace, owing to higher-than-expected deposit growth. Credit to the private sector has continued its robust expansion at about 35 percent, concentrated in the high growth sectors of the economy. Financial soundness indicators show that the banking sector remains strong (Box 1).

9. **Key structural reforms have continued to progress favorably, particularly in the fiscal and financial sectors.** Specific progress in tax administration includes amendment of the Tanzania Investment Act to limit the applicability of fiscal stability clauses, a further increase in coverage in the Large Taxpayer Department (LTD), and completion of the quality assurance review of the Customs and Excise Department (all structural benchmarks), as well as integration of the Value-Added Tax (VAT) and income tax departments, intensification of audits, and further progress in customs modernization. In the area of expenditure management, measures were implemented to further improve procurement and to mitigate the large year-end check float, which has complicated liquidity management (MEFP, paras. 5 and 8).

10. **Financial sector reforms have proceeded broadly as expected, except that amendments to the BoT Act and the Banking and Financial Institutions Act (BFIA) were not submitted to parliament by end-April (structural performance criteria).[5]** The structural performance criterion on government approval and announcement of the preferred

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[4] To alleviate pressure on BoT profitability from interest payments on liquidity paper, the government will pay much of those interest costs from the budget (MEFP, para. 40).

[5] The authorities are committed to submit the amendments to parliament by end-July 2005 (MEFP, para. 39). To that end, the amendments were approved by cabinet in late June and are now in the process of being printed and then submitted to parliament, for first reading by end-July.

Box 1. Tanzania— Financial Sector Developments

Available information shows that the financial sector as a whole is sound with lending concentrated mainly in high growth sectors of the economy. The last two years have witnessed remarkable progress in financial sector development, albeit from a low base. Financial soundness measures indicate that the system is liquid, well-capitalized, profitable, has good asset quality, and is resistant to shocks. In terms of these indicators, Tanzania also compares favorably to other countries in the region. However, Tanzania's M3 and bank credit to the private sector remain modest relative to other Sub-Saharan African countries.

Tanzania -- Financial Soundness Indicators: 2002-2004
(in percent, end of year)

	2002	2003	2004
Access to Bank Lending			
Claims on non-government sector to GDP	6.3	9.0	9.4
Capital Adequacy			
Capital to risk weighted assets	20.6	21.0	21.2
Capital to assets	8.6	9.9	10.2
Asset Composition and Quality			
Total loans and advances to total assets	25.4	30.2	33.7
Foreign exchange loans to total loans	28.1	27.2	28.5
Gross non-performing loans to gross loans	8.2	4.5	3.0
NPL's net of provisions to total capital	22.0	9.3	6.5
Large exposures to total capital 1/	58.2	59.3	64.1
Sectoral Distribution of Loans (as percent of total loans)			
Trade	22.1	23.8	22.4
Mining and Manufacturing	24.4	27.3	22.2
Agricultural Production	12.9	14.1	12.8
Building and Construction	3.6	5.5	3.8
Transport	11.8	10.3	8.3
Earnings and Profitability			
Return on Assets	1.8	2.1	2.9
Return on Equity	20.6	20.7	28.4
Interest margin to gross income	41.7	45.0	47.5
Non-interest expenses to gross income	60.9	58.5	53.4
Liquidity			
Liquid assets to total assets	58.0	56.3	53.6
Liquid assets to total short term liabilities	68.9	62.8	62.0
Total loans to customer deposits	34.0	41.2	44.4
Sensitivity to Market Risk			
Net open positions in FX to total capital	70.3	55.6	38.8

Source: Bank of Tanzania
1/ Five largest borrowers to total banking sector capital.

bidder for the National Microfinance Bank (NMB)[6] was observed, as was the benchmark on submission to government of The Financial Sector Reform Implementation Action Plan (MEFP, para. 38) albeit with slight delay to incorporate additional stakeholder comments. The framework for the Development Finance Guarantee Facility (DFGF) has been largely finalized, in line with earlier commitments (MEFP, para. 42). The government has approved the Strategic Plan for the Implementation of the Land Laws, and new microfinance regulations have been approved. The government is also continuing its efforts to strengthen its anti-money laundering regime.

11. **In other areas of structural reform,** the government has prepared a plan for clearer delineation of public and private functions in crop boards. The local government development levy has been abolished and fees on agricultural products capped at 5 percent, and business license fees were eliminated for small businesses. The Law Reform Commission has prepared amendments to anti-corruption legislation intended to strengthen prosecution and incorporate commitments under international treaties (MEFP, para. 47). Draft anticorruption strategies have been completed for all local government authorities and submitted for government approval (end-June structural benchmark). Progress in the energy sector, however, has been mixed. Better rainfall has improved the outlook for hydropower, but TANESCO's cash flow has come under strain due to delays in commissioning additional gas turbines.

III. Report on the Discussions

12. **The discussions centered mainly on the 2005/06 framework**, particularly (i) the budget, in the context of the authorities' goals for growth, employment, and poverty reduction; (ii) liquidity management in the presence of high aid inflows; (iii) progress on tax and expenditure reforms; and (iv) structural reforms to further strengthen the financial sector and business environment.

A. Macroeconomic Outlook and Poverty Reduction Strategy

13. **The macroeconomic framework targets real growth of 6.9 percent (in CY 2005) and inflation of about 4.0 percent.** Growth will be driven by a continued expansion of agriculture, agroprocessing, manufacturing, construction, and trade.

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[6] Government announced in April that a consortium led by Rabobank Nederland of the Netherlands was the winner of the technical evaluation of bids. Following the opening of this party's financial bid, the consortium is now in final stage negotiations with the government to complete the purchase of the 49 percent stake and to assume management control. NMB has the largest number of branches of any commercial bank in Tanzania and is one of the largest in terms of assets. Its most actively growing loan product is loans to micro- and small-enterprises, though salary loans (consumer, school fees, other business) remain its largest loan category.

14. **The main goals of the PRGF program remain to accelerate growth and reduce poverty. In this context, the authorities have begun implementing their new five-year PRSP—MKUKUTA in Kiswahili—**which adopts an outcome-based approach focusing on growth and reduction of income poverty, improved quality of life and social well-being, and good governance and accountability (MEFP, para. 18). MKUKUTA, which utilizes a macroeconomic framework broadly consistent with the PRGF,[7] focuses on a number of reforms to stimulate private sector activity, including better infrastructure, enhanced domestic savings, better access to financial services, stronger governance, and reducing administrative burdens on the private sector. The authorities have revised the timing and modalities of the budget guidelines to strengthen the link between budget preparation and the three broad outcomes targeted in the MKUKUTA. The next stage will be to carry this revised allocation process into the medium-term expenditure framework (MTEF).[8]

15. **The authorities at the highest level expressed their resolve to maintain steady, prudent policies up to and beyond the October 2005 presidential and parliamentary elections.** More generally, they reiterated their view that continued macroeconomic stability and steady implementation of ambitious structural reforms to improve the environment for productive private sector activity are key to improving the lives of all Tanzanians. The authorities also expressed the desire for ongoing Fund involvement in Tanzania to provide policy advice, technical assistance, and signaling to development partners.

B. Fiscal Policy

16. **Consequent to the authorities' 2005/06 growth and poverty reduction goals, the budget targets further increases in expenditure, mainly for priority sectors and infrastructure, financed by increased domestic revenue mobilization and higher foreign aid**. Net domestic budget financing will be contained at 1.1 percent of GDP in order to avoid crowding out the private sector.

17. **Domestic revenues are projected to rise from 13.6 percent of GDP in 2004/05 to 14.3 percent of GDP,** driven by a number of reforms (MEFP, para 23), in particular the full-year effect of the new Income Tax Act, the graduation of a number of tax-exempted companies into the tax net, and the ongoing reform of the TRA and customs administration.

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[7] Projections of aid inflows and development expenditures in 2005/06 are higher than staff projections, while projections for 2006/07-2007/08 are roughly in line with the staff's projections.

[8] While applauding the authorities' efforts to link MKUKUTA to Tanzania's economic plans (MEFP, paras. 22 and 28), the staff also indicated that MKUKUTA would benefit from stronger costing and prioritization, as well as clearer links with parallel initiatives such as those in the financial sector.

The staff and the authorities agreed that administrative controls on exemptions should be maintained.[9] In that same vein, in the context of plans to establish special economic zones (SEZs), the government will focus on strengthening infrastructure and providing efficient services, including expedited customs clearing and VAT refunds, rather than new tax exemptions.

18. **Expenditure is programmed at 26.8 percent of GDP, compared with 25 percent in 2004/05.** Recurrent expenditure is projected to rise by 0.5 percent of GDP mainly on account of wage and salary hikes, designed to boost capacity under the Public Service Reform Program (PSRP). Development expenditures are projected to increase by 1.2 percent of GDP, mainly reflecting higher outlays on infrastructure. The staff supported the proposed expenditures, but remarked that the wage hikes should be accompanied by reforms of the allowances system, including transparency about their magnitude, and the authorities agreed to study these issues (MEFP, para. 17). About 44 percent of programmed expenditures are expected to be financed by development partners, broadly unchanged from earlier years.

19. **It should be noted that expenditure levels in the budget submitted to parliament are 1.5 percent of GDP higher than the program (with net domestic financing of 2.6 percent of GDP).** The staff argued that the higher net domestic financing under the budget would unduly crowd out the private sector. The authorities agreed to constrain spending to limit net domestic financing to 1.1 percent of GDP (performance criterion, MEFP, para. 25). The staff is confident that the authorities will meet this program target, given their strong track record of significant overperformance on net domestic financing and high level of commitment to meeting program targets.[10] The authorities also noted they have consistently exceeded their revenue targets in past years, and are actively seeking additional donor support. If additional resources emerge, expenditures on infrastructure and goods and services will be increased, in line with the budget. The staff noted that even if such additional resources are attained, divergence between the program and the budget is detrimental to the budget process and to transparency, notwithstanding explicit discussion of this difference in the MEFP and this staff report, which are to be published.

20. **The staff views the medium-term fiscal outlook as positive, albeit dependent on sustained donor support. Moreover, the authorities agreed that the revenue to GDP ratio, notwithstanding its increase by 1.5 percentage points of GDP over the past two**

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[9] Including publication of tax exemption beneficiaries under the Treasury Voucher scheme (quarterly structural benchmark).

[10] The staff believes the risk of deviation from the expected path of expenditures, or accumulation of arrears, is minimal due to implementation of the Integrated Financial Management System (IFMS), the centralization of many payments through a Single Treasury Account system, and the strict adherence to the cash budgeting system (no releases are made without cash backing).

years, remains low by regional standards. They agreed that continuing to increase the revenue to GDP ratio over the medium term, particularly through broadening the tax base and improving tax policy administration is important (Box 2). They have requested technical assistance from the Fund in a broader review of tax policy.

21. **In this context, further strengthening of tax administration is envisaged for 2005/06 (MEFP, paras. 26-27).** In particular, the operation of the VAT and income tax departments will be enhanced, the LTD will be further strengthened, and efforts to streamline customs administration will continue. In support of these efforts, to improve the performance of customs, the authorities will strengthen the post clearance audit section, including through increasing the number of staff (end-March 2006,structural benchmark) and will integrate the destination inspection program with custom procedures in the Dar es Salaam custom offices (end-January 2006, structural benchmark). The authorities will also complete an action plan by June 2006 for establishing a single domestic tax department.

22. **The authorities will further strengthen public expenditure management (MEFP, paras. 28-30)**. In particular, the government will (i) review the organizational structure of the Ministry of Finance in light of the Public Finance Act 2001 and review the consistency of that Act with other legislation; (ii) address weaknesses related to projecting expenditure requirements; (iii) integrate local government agencies (LGAs) into the budget preparation and execution process; and (iv) act on weaknesses in procedures in internal and external audits of public expenditure.

C. Monetary Policy and Financial Sector Issues

23. **The staff agreed with the BoT that an increase in the targeted path of reserve money growth during 2005/06 and the associated continued strong growth in private sector credit will not pose undue risks to inflation**, given the absence of inflationary pressures, continued buoyant economic conditions, and strong private sector demand for credit. Under the proposed program, M3 growth is projected to rise to 27 percent by end-June 2006 from an estimated 24 percent through June 2005. Velocity is projected to decline, consistent with the deepening of the financial system and in line with the annual average decline of velocity over the past five years.

24. **The authorities and the staff agreed that the principal challenge in implementing monetary policy continues to be liquidity management in the face of high aid inflows** (Box 3). The staff has continued to emphasize heavier reliance on foreign exchange sales, noting that the real exchange rate would remain around its equilibrium level even if a moderate nominal appreciation materializes in the coming year.[11] The BoT indicated it does

[11] See "External Competitiveness and Export Performance in Tanzania" (Country Report No. 04/284).

see some additional room to increase sales of foreign exchange to complement open market operations, but nevertheless continued to express concerns about the potential loss of

Box 2. Tanzania— Revenue Performance in Perspective

The last three years have marked strong progress in tax administration reforms. The TRA is pursuing a modernization strategy that is supported by Fund TA. This includes increased coverage of the LTD, integration of the VAT and income tax departments, efforts to reduce exemptions, and increased emphasis on taxpayers' services. In addition, the Customs and Excise Department has embarked on an ambitious program of reforms and modernization. This is being strengthened through enhanced audit capacity and further simplifications of procedures in clearing goods.

These tax administration reforms have led to significant improvement in revenue performance. The revenue-to-GDP ratio increased from about 12 percent of GDP in 2002/03 to a estimated 13.6 percent of GDP in 2004/05.

Despite these improvements, the revenue-GDP-ratio remains low by regional standards. Achieving the government's growth and poverty reduction goals, and reducing aid dependency, will require increased domestic resource mobilization. A comparison of revenue performance in Tanzania with other countries of broadly the same level of development shows scope for further enhancing revenue**.**

Cross-Country Comparison of Revenue Performance (percent of GDP), 2003/04 2/

	GDP per capita (constant 2000 US$) 1/	Revenue 2/	Tax Revenue	VAT collection	Income Tax collection	Custom Dutes	Excises
Tanzania	309.0	12.7	11.7	4.4	3.2	1.2	1.9
Kenya	341.0	21.7	19.6	5.3	7.3	1.9	3.4
Mozambique	255.0	12.3	11.5	4.7	2.6	1.7	2.2
Uganda	277.0	12.6	11.7	3.9	3.4	1.0	3.4
Zambia	354.0	18.4	17.7	5.3	7.9	2.1	2.4

1/ As of 2003
2/ Calendar year 2004 for Mozambique and Zambia

Sources: World Development Indicators (WDI), IMF country reports, and IMF staff estimates.

Box 3: Liquidity Management in the Presence of High Aid Inflows

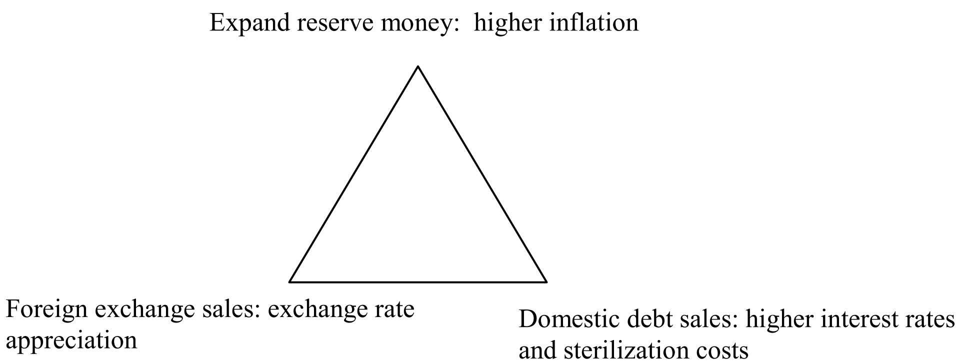
Since the mid-1990s, rapid GDP growth and deep structural reforms have helped attract substantial aid inflows, projected to reach 14.0 percent of GDP in 2005/06.

Given the natural lag in the expansion of absorptive capacity, the surge in aid inflows and the resulting increased liquidity present challenges to monetary policy. On the one hand, aid inflows allow for increased investment and poverty reducing expenditures as well as boost domestic demand. On the other hand, the resulting rise in liquidity threatens the BoT’s ability to meet its reserve money targets.

The challenge lies in effectively balancing the pressure on prices from increased liquidity versus the pressure on interest rates from the expansion of sterilization operations, and on exchange rates from increased foreign exchange sales. For a given reserve money target, increased sales of foreign exchange may adversely affect export competitiveness through an exchange rate appreciation. Conversely, the use of domestic debt sales for sterilization may (i) put upward pressure on interest rates, crowding out credit for private sector investment and (ii) strain the BoT’s balance sheet as it absorbs the interest it pays on domestic paper (and put pressure on the government’s budget as the costs of sterilization are eventually borne there).

The appropriate *policy mix* between these options has consequences for prices, the exchange rate and/or interest rates, and ultimately for growth and macroeconomic stability. A successful monetary response is one that avoids a jump in interest rates, an overshooting of the exchange rate or a surge in inflation.

The Trilemma: absorbing high inflows requires some combination of changes in inflation, interest rates and exchange rates



Given that in Tanzania: (i) inflation has been low at around 4 percent, (ii) the cost of sterilization operations has been increasing rapidly, with a negative impact on BoT profitability, (iii) Treasury Bill rates have moved up over the last couple of years, and (iv) the real exchange rate has depreciated to levels broadly in line with fundamentals the staff and the authorities agreed on a high reserve money path, consistent with estimated money demand growth. To achieve the reserve money targets, the staff urged a higher reliance on sales of foreign exchange, even if that entailed allowing for a slight nominal exchange rate appreciation. This could be achieved while continuing to smooth out large abrupt exchange rate fluctuations and avoiding any significant exchange rate overshooting.

The challenges of liquidity management underline the importance of improving the supply response and absorptive capacity of the economy. In this context, key focus areas include improving the business environment, expanding the availability of bank credit, strengthening labor productivity, and addressing infrastructural bottlenecks, particularly in the areas of transportation, utilities, and telecommunications.

competitiveness. To further improve liquidity management, the authorities also plan to strengthen liquidity forecasting, including improving projections of liquidity-injecting government expenditures.

25. **The authorities intend to accelerate financial sector reforms during 2005/06.** Despite rapid growth in recent years, Tanzania's financial sector remains small, and large portions of the economy work with little formal credit. The financial sector reform plan addresses structural impediments in nine areas, and includes a detailed matrix of reforms and identified donor support (MEFP, para. 38). In addition to the amendments to the BoT Act and the BFIA (MEFP, para. 39), near-term actions will include completion of the NMB privatization, restructuring remaining state-owned banks, and development of a legal and regulatory framework and investment guidelines for pension funds (end-June 2006, structural benchmark) to boost availability of funds for longer-term productive investments.

26. **The authorities are pursuing efforts to improve the availability of medium-term credit to key sectors of the economy (MEFP, paras. 42-46).** In addition to the DFGF discussed earlier, the government intends to establish a Development Finance Institution (DFI) that would channel donor funds and perhaps government seed money for development-oriented lending. Though the DFI's mode of operation is still under development, the authorities responded to staff concerns about potential government contingent liabilities by indicating that the DFI would not take any new deposits from the public (other than its credit customers) nor raise any other funds under government guarantee, and would operate under a strong governance structure. The authorities agreed that government exposure under the DFI and the DFGF will be strictly limited (continuous structural performance criterion), and that the instruments establishing the DFGF and the DFI will require annual independent operational audits—in addition to standard independent audits of financial statements—to verify that the funds are being employed as intended (structural benchmark). The government also hopes to facilitate creation of a privately owned and managed long-term financing facility (LTFF), with no government guarantees (continuous structural performance criterion), that would channel funds to be on-lent to commercial banks on a long-term basis.

D. External Sector Policies and Prospects

27. **The current account deficit is expected to widen somewhat in 2005/06 to 12.4 percent of GDP, driven by an increase in the trade deficit.** Imports of intermediate and capital goods are expected to increase, due to accelerating economic growth, infrastructure projects, government subsidies for fertilizer transport, and high oil prices. Export growth is expected to be solid, with mining and manufacturing exports remaining strong and traditional exports benefiting from an easing of structural bottlenecks such as road improvements and facilitated access to inputs, as well as favorable commodity prices. Non-traditional export growth will abate over the medium term as no new gold mines are foreseen. Ongoing structural reforms continue to aim at lowering impediments to exports.

28. **The trade deficit will be largely covered by increased aid inflows, which are expected to reach 14 percent of GDP in 2005/06**. Increased net inflows to the balance of

payments are projected to result in an overall international reserves position of around 5.7 months of imports. The BoT is committed to limit its interventions in the foreign exchange market to facilitate liquidity management and smoothing any short-run excessive fluctuations in the exchange rate.

29. **The government will continue efforts to negotiate debt relief agreements with the few remaining creditors under HIPC comparable terms (Table 8).** An updated debt sustainability analysis (Appendix V) shows that Tanzania's external debt position is sustainable, with moderate risk. On trade, the East African Community (EAC) aims to reduce conflicting regulations within and outside the regional trade blocks. Over the medium term, the authorities aim to increase intra-regional trade and economic integration.

E. Other Structural Reforms

30. **The authorities are continuing efforts to reduce structural impediments to private sector led growth and investment.** To this end, a new private sector development strategy is being prepared (MEFP, para. 15). Draft bills on Business Activities Registration and Reform of the Regulatory Licensing System are being finalized for submission to Parliament by July 2006. The government will also undertake reform of crop boards (MEFP, para. 50), and is moving ahead with anticorruption efforts (MEFP, para. 16), including Cabinet approval of the new Anti-Corruption Law by end-April 2006 (a structural benchmark), designed to strengthen the ability to prosecute those suspected of corruption.

31. **The authorities are taking further steps to address Tanzania's energy-generation capacity**. With only 7 percent of the population having access to electric power, the government is launching a rural and peri-urban electrification program with World Bank support. To avoid load shedding or further tariff increases, TANESCO is seeking to restructure its debt service related to the Songas facility, which would allow TANESCO to attract private investors and borrow to finance its capital investment needs.

IV. Program Monitoring

32. **The program will be monitored through quantitative and structural performance criteria and benchmarks specified in Tables 1 and 3 of Appendix I.** Quantitative performance criteria and indicative targets for end-September 2005 are proposed, and understandings have been reached on indicative targets for end-December 2005, end-March 2006 and end-June 2006, based on the 2005/06 macroeconomic framework. Structural conditionality focuses on tax administration, financial sector reform, and governance. Program implementation will be assessed during the fifth review.

V. Staff Appraisal

33. **Tanzania has achieved strong economic performance in recent years through adoption of market-oriented, outward-looking policies within an appropriate macroeconomic framework.** Strong monetary and fiscal policies, underpinned by structural reforms in key areas, have resulted in accelerated growth and low inflation, as well as some reduction in poverty. Nonetheless, Tanzania remains a country with a high degree of poverty, serious capacity constraints, and heavy reliance on donor inflows. The authorities will need to maintain sound policies and steadily pursue key structural reforms and capacity building for many years in order to improve the lives of all Tanzanians.

34. **Pressures for more direct government intervention in the economy to accelerate growth and poverty alleviation could be accentuated in the run-up to the October 2005 elections.** In this context, the staff welcomes the authorities' decision to limit their ambitious plans to further expand government expenditure, in order to contain net domestic financing of the budget to reasonable levels and thus limit the risk of crowding out productive private sector activity. More generally, the staff welcomes the authorities' commitment at the highest level to maintain prudent economic policies over the medium term.

35. **The staff welcomes the authorities' efforts to better link MKUKUTA goals to the budget process and the MTEF.** The staff supports the authorities' plans to further strengthen these links, including additional costing and prioritizing, and tighter coordination with parallel reform efforts, such as those in the financial sector. In this regard, the divergence between the program and budget expenditure levels is regrettable as it is detrimental to the budget process and undermines transparency.

36. **The authorities' ongoing efforts to mobilize domestic resources are critical to provide resources for key expenditures for development and to reduce somewhat the dependence on foreign aid.** Prospects for sustained improvements in revenue performance over the medium-term are favorable. The staff commends the authorities' implementation of well-grounded reform measures to enhance the effectiveness of the TRA and the customs administration.

37. **The staff views the proposed monetary program as fully consistent with the authorities' growth and inflation objectives.** The risk of higher inflation from the modest upward adjustment in the reserve money growth path is small given the strong private sector demand for credit. The staff commends the BoT's ongoing management of liquidity pressures and encourages the BoT to continue to use its full range of tools including foreign exchange sales, to help better distribute the impact of sterilization efforts on interest and exchange rates. The staff welcomes plans for improving liquidity forecasting. The staff also commends the government's commitment to pay much of the interest costs for liquidity management, thereby preserving the profitability of the BoT.

38. **The staff welcomes finalization of the authorities' Financial Sector Reform Implementation Action Plan.** Strong ownership and development partner backing should accelerate implementation of key reform measures. The staff regrets the delays in submitting banking legislation amendments to parliament, but believes the reasons for the delay underscores the authorities' commitment to full consultation with key stakeholders.

39. **The staff supports the government's willingness to introduce prudent safeguards to several new initiatives to stimulate medium-term lending and investment.** These rightly include strict limits on government exposure under the DFGF and the planned DFI, as well as strong governance. The staff also welcomes government efforts to attract investment by establishing two SEZs, with focus on strengthening infrastructure and providing efficient services rather than new tax incentives.

40. **The staff welcomes the authorities' ongoing efforts to improve the business environment, which is clearly central to the goal of sustaining and enhancing growth through productive private sector activity.** Investment is not yet increasing at the rate needed to materially reduce unemployment and poverty. As emphasized in MKUKUTA, enhanced efforts are needed to stimulate private-sector led growth, particularly in such areas as infrastructure, access to the financial sector, improving the business environment and governance.

41. **Based on the authorities' continued strong record of program implementation, and their commitments in the attached letter of intent, the staff recommends approval of the authorities' request for waivers for the nonobservance of structural performance criteria and completion of the fourth review under the current PRGF arrangement.**

Table 1. Tanzania: Proposed Schedule of Disbursements Under the Poverty Reduction and Growth Facility Arrangement, 2003-06

Date	Disbursement Schedule		Event
	Millions of SDRs	Percent of quota	
August 2003	2.8	1.4	Effectiveness of PRGF arrangement
End-September 2003	...	...	Test date for quantitative performance criteria for first review
February 2004	2.8	1.4	Completion of first review
End-March 2004	...	...	Test date for quantitative performance criteria for second review
August 2004	2.8	1.4	Completion of second review
End-September 2004	...	...	Test date for quantitative performance criteria for third review
February 2005	2.8	1.4	Completion of third review
End-March 2005	...	...	Test date for quantitative performance criteria for fourth review
August 2005	2.8	1.4	Completion of fourth review
End-September 2005	...	...	Test date for quantitative performance criteria for fifth review
February 2006	2.8	1.4	Completion of fifth review
End-March 2006	...	...	Test date for quantitative performance criteria for sixth review
August 2006	2.8	1.4	Completion of sixth review

Source: Fund staff

Table 2. Tanzania: Selected Economic and Financial Indicators, 2003/04-2007/08

	2003/04	2004/05		2005/06	2006/07	2007/08
		Prog.	Est.	Proj.	Proj.	Proj.
	(Annual percentage change, unless otherwise indicated)					
National income and prices 1/						
Nominal GDP (market prices; billions of Tanzania shillings)	10,686	11,821	12,321	13,673	15,243	17,011
Real GDP growth (factor cost)	5.7	6.3	6.7	6.9	7.2	7.3
Consumer prices (period average)	4.4	4.2	4.1	4.0	4.0	4.0
Consumer prices (end of period)	4.6	4.0	4.1	4.0	4.0	4.0
External sector						
Export, f.o.b (in U.S. dollars)	1,174	1,289	1,456	1,709	1,922	2,160
Imports, c.i.f. (in U.S. dollars)	-2,368	-2,738	-2,828	-3,459	-3,761	-4,050
Export volume	6.7	-0.6	11.6	10.6	7.9	9.9
Import volume	9.3	6.2	6.5	20.5	7.3	7.5
Terms of trade	-8.2	1.4	-1.0	4.6	2.9	2.1
Nominal effective exchange rate (end of period; depreciation -)	-10.6	...	...	...	...	...
Real effective exchange rate (end of period; depreciation -)	-7.1	...	...	...	...	...
Public finance						
Revenue (excluding grants)	19.9	19.2	21.5	16.5	14.0	12.8
Total expenditure	27.1	27.0	28.7	19.3	13.4	9.8
Recurrent expenditure	26.7	26.1	25.9	14.7	11.9	11.2
Development expenditure	28.3	29.6	36.7	31.9	16.9	6.8
Money and credit						
Broad money (M3)	18.0	23.5	24.4	27.0	…	…
Net foreign assets	16.8	15.8	8.9	12.1	…	…
Net domestic assets	24.3	60.6	99.7	66.4	…	…
Net credit to government	-51.8	124.7	56.5	134.7	…	…
Credit to nongovernment sector	46.7	30.2	30.0	33.2	…	…
Velocity of money (GDP/M3; average)	4.7	4.3	4.4	3.9	…	…
Treasury bill interest rate (in percent; end of period) 2/	7.7	…	10.4	…	…	…
	(In percent of GDP)					
Public finance						
Revenue (excluding grants)	12.7	14.0	13.6	14.3	14.6	14.8
Total grants	6.1	7.7	6.6	7.5	7.5	6.9
Expenditure (including adjustment to cash)	22.0	25.8	25.0	26.8	27.3	26.8
Overall balance (including grants)	-3.2	-4.1	-4.8	-5.1	-5.2	-5.1
Domestic financing 3/	-0.4	1.3	0.6	1.1	0.8	0.5
o/w: nonbank financing	0.3	0.5	0.3	0.0	0.0	0.0
Savings and investment 1/						
Resource gap	-9.0	-11.7	-10.5	-11.4	-11.5	-10.7
Investment	18.6	19.2	18.4	18.9	19.3	19.7
Government	7.4	7.6	7.3	7.5	7.7	7.8
Nongovernment 4/	11.2	11.6	11.1	11.4	11.6	11.9
Gross domestic savings	9.7	7.5	7.9	7.5	7.8	8.2
External sector						
Current account balance (excluding current transfers)	-11.0	-12.6	-11.2	-12.4	-11.7	-11.0
Current account balance (including current transfers)	-5.8	-5.9	-5.2	-7.0	-6.3	-6.1
	(In millions of U.S. dollars, unless otherwise indicated)					
Balance of payments						
Current account balance (excluding current transfers; deficit -)	-1,177	-1,380	-1,340	-1,661	-1,752	-1,834
Overall balance of payments (deficit -)	162	220	291	173	324	346
Gross official reserves	1,878	2,058	2,137	2,247	2,502	2,771
In months of imports of goods and nonfactor services	6.0	6.8	5.9	5.7	5.8	6.6
Exchange rate (eop, T Shillings per U.S. dollar)	1,115	...	1,126	...	...	...
Exchange rate (period average, T Shilling per U.S. dollar)	1,077	...	1,090	...	...	...

Sources: Tanzanian authorities; and Fund staff estimates and projections.

1/ Data are on calendar year basis. 2001/02 data are for calendar year 2001.
2/ Weighted-average yield of 35, 91-, 182-, and 364-day treasury bills.
3/ Excluding new debt issued to recapitalize government-owned banks.
4/ Including change in stock.

Table 3. Tanzania: Central Government Operations, 2003/04-2007/08 1/

	2003/04	2004/05		2005/06	2006/07	2007/08
		Prog.	Est.	Projections		
	(in billions of shillings)					
Total revenue	1,459	1,739	1,774	2,067	2,357	2,659
Tax revenue	1,343	1,599	1,613	1,869	2,134	2,407
Import duties	137	142	108	148	182	204
Value-added tax	504	615	675	776	890	1,014
Excises	215	243	239	268	295	331
Income taxes	364	458	459	531	605	675
Other taxes	123	141	131	146	163	182
Nontax revenue	117	140	160	198	223	252
Total expenditure	2,528	3,211	3,253	3,882	4,401	4,833
Recurrent expenditure	1,886	2,379	2,375	2,724	3,047	3,387
Wages and salaries	463	551	551	682	759	846
Interest payments	109	170	166	171	207	219
Domestic	71	94	95	101	140	147
Foreign	38	76	71	70	67	72
Goods and services and transfers	1,314	1,657	1,657	1,871	2,081	2,322
Development expenditure	642	832	878	1,158	1,354	1,446
Domestically financed	133	234	234	370	544	571
Foreign financed	509	598	644	788	810	875
Overall Balance before Grant	-1,069	-1,472	-1,479	-1,815	-2,044	-2,174
Grants	697	940	860	1,080	1,212	1,251
Program (including basket grants) 2/	371	561	574	549	689	714
Project	248	312	219	461	432	443
HIPC grant relief	77	90	67	70	91	94
Overall balance after grants	-372	-532	-619	-735	-833	-923
Adjustment to cash 3/	-28	-31	0	0	0	0
Overall Balance	-400	-539	-619	-735	-833	-923
Financing	400	539	619	735	833	923
Foreign (net)	434	388	546	561	720	849
Foreign loans	479	523	656	683	826	967
Program (including basket loans) 2/	218	236	231	356	448	535
Project	261	286	425	327	378	432
Amortization	-45	-135	-111	-122	-107	-118
Domestic (net)	-44	157	79	164	129	90
Bank financing	-83	97	44	164	129	90
Nonbank financing	39	60	35	0	0	0
Amortization of parastatal debt	0	-16	-16	0	-16	-16
Privatization proceeds	10	10	10	10	0	0
Memorandum items:						
Treasury vouchers	21	31	31	31	...	...
Foreign-financed development expenditure	-451	-703	-669	-855	-1,028	-1,081
Share of expenditures financed from foreign sources 4/	46	44	45	44	45	45
Share of current expenditures financed by foreign program assistance 5/	31	34	34	33	37	37
Public Domestic Debt (percent of GDP) 6/	15	15	13	12	10	9
Ratio of recurrent expenditures to total revenues (percent)	129	137	134	132	129	127
Priority sector spending	1,118	1,486	1,486	1,785	...	...
Nominal GDP	11,504	12,457	12,997	14,458	16,127	18,015

Table 3. (contd.) Tanzania: Central Government Operations, 2003/04-2007/08 1/

	2003/04	2004/05		2005/06	2006/07	2007/08
		Prog.	Est.	Projections		
	(In percent of GDP)					
Total revenue	12.7	14.0	13.6	14.3	14.6	14.8
Tax revenue	11.7	12.8	12.4	12.9	13.2	13.4
Import duties	1.2	1.1	0.8	1.0	1.1	1.1
Value-added tax	4.4	4.9	5.2	5.4	5.5	5.6
Excises	1.9	2.0	1.8	1.9	1.8	1.8
Income taxes	3.2	3.7	3.5	3.7	3.7	3.7
Other taxes	1.1	1.1	1.0	1.0	1.0	1.0
Nontax revenue	1.0	1.1	1.2	1.4	1.4	1.4
Total expenditure	22.0	25.8	25.0	26.8	27.3	26.8
Recurrent expenditure	16.4	19.1	18.3	18.8	18.9	18.8
Wages and salaries	4.0	4.4	4.2	4.7	4.7	4.7
Interest payments	0.9	1.4	1.3	1.2	1.3	1.2
Domestic	0.6	0.8	0.7	0.7	0.9	0.9
Foreign	0.3	0.6	0.5	0.5	0.4	0.4
Goods and services and transfers	11.4	13.3	12.8	12.9	12.9	12.9
Development expenditure	5.6	6.7	6.8	8.0	8.4	8.0
Domestically financed	1.2	1.9	1.8	2.5	3.4	3.2
Foreign financed	4.4	4.8	5.0	5.5	5.0	4.9
Overall balance before grants	-9.3	-11.8	-11.4	-12.6	-12.7	-12.1
Grants	6.1	7.7	6.6	7.5	7.5	6.9
Program (including basket grants) 2/	3.2	4.5	4.4	3.8	4.3	4.0
Project	2.2	2.5	1.7	3.2	2.7	2.5
HIPC grant relief	0.7	0.7	0.5	0.5	0.6	0.5
Overall balance after grants	-3.2	-4.1	-4.8	-5.1	-5.2	-5.1
Adjustment to cash 3/	-0.2	-0.2	0.0	0.0	0.0	0.0
Financing	3.5	4.3	4.8	5.1	5.2	5.1
Foreign (net)	3.8	3.1	4.2	3.9	4.5	4.7
Foreign loans	4.2	4.2	5.1	4.7	5.1	5.4
Program (including basket loans) 2/	1.9	1.9	1.8	2.5	2.8	3.0
Project	2.3	2.3	3.3	2.3	2.3	2.4
Amortization	-0.4	-1.1	-0.9	-0.8	-0.7	-0.7
Domestic (net)	-0.4	1.3	0.6	1.1	0.8	0.5
Bank financing	-0.7	0.8	0.3	1.1	0.8	0.5
Nonbank financing	0.3	0.5	0.3	0.0	0.0	0.0
Amortization of parastatal debt	0.0	-0.1	-0.1	0.0	-0.1	-0.1
Privatization proceeds	0.1	0.1	0.1	0.1	0.0	0.0

Sources: Ministry of Finance and Fund staff projections.

1/ Fiscal year: July-June.

2/ Basket funds are sector-specific accounts established by the government for channeling donor support to fund specific activities in different sectors.

3/ Unidentified financing (+)/expenditure (-). Includes expenditure carryover from the previous fiscal year.

4/ Defined as a ratio (in percent) of gross grant and loan inflows to the sum of total expenditures and amortization payments.

5/ Defined as a ratio (in percent) of current expenditures to a sum of program grants and loans (including basket funding).

6/ Including contigent liabilities, largely consisting of non-guaranteed parastatal debt.

Table 4. Tanzania: Summary Accounts of the Bank of Tanzania, December 2004 - June 2006
(In billions of shillings, unless otherwise indicated; end of period)

	2004	2005						2006	
	Dec	March		June		Sep.	Dec.	March	June
	Act.	Prog.	Act.	Prog.	Est.	Proj.	Proj.	Proj.	Proj.
Net foreign assets	1,825	1,987	1,771	1,804	1,756	2,027	2,198	2,056	1,943
Net international reserves	1,864	2,026	1,810	1,844	1,795	2,066	2,237	2,095	1,982
(in millions of U.S. dollars)	1,787	1,747	1,639	1,589	1,662	1,913	2,071	1,940	1,835
Medium- and long-term foreign liabilities	-39	-40	-39	-40	-39	-39	-39	-39	-39
Net domestic assets	-857	-1,003	-794	-776	-727	-894	-963	-806	-641
Credit to government (net, excl. liquidity paper)	-412	-200	-276	-180	-160	-290	-415	-300	-120
Liquidity paper (sterilized T-Bills)	-454	-657	-511	-450	-603	-640	-613	-604	-632
Other items (net)	8	-146	-7	-146	35	36	65	98	111
Reserve money	968	984	977	1,028	1,028	1,133	1,235	1,250	1,302
Currency outside banks	664	682	645	701	696	785	857	854	905
Bank reserves	304	302	332	327	332	348	378	396	397
Currency in banks	64	63	83	63	63	63	65	65	65
Deposits	240	239	249	265	269	285	313	331	332
Required reserves (calculated) 1/	187	206	206	220	223	247	265	276	288
Excess reserves (calculated)	53	32	43	45	46	38	48	55	43

Sources: Bank of Tanzania; and Fund staff estimates and projections.

1/ Calculated as reserve requirement times banks' deposits minus half of bank cash in vault.

Table 5. Tanzania: Monetary Survey, December 2004 - June 2006
(In billions of shillings, unless otherwise indicated; end of period)

	2004	2005						2006	
	Dec	March		June		Sept	Dec	March	June
	Act.	Prog.	Act.	Prog.	Est.	Proj.	Proj.	Proj.	Proj.
Net foreign assets	2,490	2,712	2,485	2,500	2,350	2,647	2,814	2,725	2,636
Net domestic assets	358	348	640	715	889	924	1,021	1,212	1,479
Domestic credit	852	1,273	1,116	1,433	1,378	1,398	1,459	1,666	1,959
Credit to government (net)	-208	79	-31	175	122	21	-22	80	286
Credit to nongovernment sector	1,060	1,194	1,147	1,258	1,256	1,377	1,481	1,586	1,672
Other items (net)	-493	-925	-476	-718	-489	-475	-438	-454	-480
M3	2,848	3,060	3,125	3,215	3,239	3,570	3,835	3,937	4,115
Foreign currency deposits	797	937	912	931	880	1,037	1,058	1,112	1,118
M2	2,051	2,123	2,212	2,283	2,359	2,534	2,777	2,825	2,997
Currency in circulation	664	682	645	701	696	785	857	854	905
Deposits (in Tanzania shillings)	1,387	1,440	1,567	1,582	1,662	1,748	1,920	1,970	2,092
Memorandum items:									
M3 growth (12-month percent change)	19.3	23.5	26.1	23.5	24.4	27.7	34.6	26.0	27.0
Foreign currency deposits (12-month percent change)	19.5	30.1	26.6	24.8	17.9	27.0	32.8	21.9	27.0
M2 growth (12-month percent change)	19.2	20.8	25.9	23.0	27.1	28.0	35.4	27.7	27.1
Credit to nongovernment sector (12-month percent change)	29.7	40.8	35.3	30.2	30.0	34.1	39.7	38.3	33.2
Reserve money (12-month percent change)	23.5	22.5	21.7	28.4	28.5	31.2	27.6	27.9	26.6
Currency/M3 (in percent)	23.3	22.3	20.6	21.8	21.5	22.0	22.3	21.7	22.0
Reserve money multiplier (M3/reserves)	2.9	3.1	3.2	3.1	3.1	3.1	3.1	3.1	3.2
Velocity of money (M3; average)	4.5	...	...	4.3	4.4	...	4.1	...	3.9
Velocity of money (M3; end-period)	4.2	...	...	3.9	4.0	...	3.6	...	3.5

Sources: Bank of Tanzania; and Fund staff estimates and projections.

Table 6. Tanzania: Balance of Payments, 2003/04-2007/08
(In millions of U.S. dollars, unless otherwise indicated)

	2003/04	2004/05	2004/05	2005/06	2005/06	2006/07	2007/08
	Act.	Prog.	Est.	Prog	Proj.	Proj.	Proj.
Current account	-620.3	-647.3	-629.9	-784.9	-937.7	-947.1	-1,017.1
Trade balance	-980.5	-1,203.2	-1,117.4	-1,227.6	-1,438.6	-1,500.9	-1,525.9
Exports, f.o.b.	1,174.5	1,288.8	1,456.4	1,458.6	1,708.9	1,921.8	2,160.0
Traditional	214.9	245.0	341.2	290.4	409.5	452.8	500.4
Nontraditional	959.6	1,043.9	1,115.2	1,168.2	1,299.4	1,469.0	1,659.6
Imports, f.o.b	-2,155.0	-2,492.0	-2,573.8	-2,686.2	-3,147.5	-3,422.7	-3,685.9
Services (net)	-128.8	-144.7	-173.3	-124.5	-160.6	-156.3	-194.0
Income (net)	-68.1	-32.3	-49.6	-31.9	-62.0	-94.3	-114.5
Of which: interest payments due	-124.5	-87.1	-90.5	-76.1	-102.9	-134.1	-149.3
Of which: interest on public debt	-80.4	-69.9	-69.9	-56.1	-67.9	-69.1	-74.3
Of which : interest on central government debt	-74.0	-66.2	-66.2	-50.5	-64.8	-62.2	-66.9
Current transfers (net)	557.1	732.9	710.3	599.1	723.4	804.4	817.3
Of which: official transfers	550.9	724.8	733.8	614.4	713.0	869.4	902.3
Of which: program grants	338.3	501.9	534.0	388.6	507.9	638.0	661.6
HIPC Initiative relief grants	71.8	79.0	62.3	79.0	64.9	83.9	86.7
Capital account	348.6	329.6	340.6	325.0	543.5	560.0	585.0
Of which: project grants	310.0	289.3	302.0	290.0	496.0	525.0	550.0
Financial account	635.3	538.0	580.7	714.6	567.6	711.2	778.2
Direct investment	478.0	263.0	495.0	300.0	510.0	582.0	645.0
Portfolio investment	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment	157.3	275.0	85.7	414.6	57.6	129.2	133.2
Of which : government scheduled amortization	-108.0	-123.2	-123.2	-112.7	-119.2	-109.6	-121.0
Of which: central government amortization	-97.1	-118.5	-103.0	-101.4	-113.2	-98.6	-108.9
Errors and omissions	-201.2	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	162.4	220.2	291.3	254.7	173.4	324.1	346.1
Financing	-162.4	-220.2	-291.3	-254.7	-173.4	-324.1	-346.1
BoT reserve assets (increase, -)	-207.6	-179.5	-259.1	-201.5	-110.2	-254.9	-268.4
Use of Fund credit	-3.1	-40.8	-32.2	-53.2	-63.2	-59.2	-57.7
Exceptional financing	48.3	0.0	0.0	0.0	0.0	-10.0	-20.0
Change in arrears (increase +) 1/	48.3	0.0	0.0	0.0	0.0	-10.0	-20.0
Debt rescheduled	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:							
Gross official reserves (BoT)	1,878.0	2,057.6	2,137.2	2,259.1	2,247.4	2,502.3	2,770.7
In months of imports of goods and services (next year)	6.0	6.8	5.9	7.1	5.7	5.8	6.6
Current account deficit (as percent of GDP)							
Excluding official current transfers	-11.0	-12.6	-11.2	-11.6	-12.4	-11.7	-11.0
Including official current transfers	-5.8	-5.9	-5.2	-6.6	-7.0	-6.3	-6.1
World Oil Price (U.S. $/barrel) 2/	33.3	40.6	42.1	40.5	45.1	42.4	40.4
Aid dependency 2/	12.2	13.5	13.8	12.4	14.0	14.5	14.1
Net aid flows (as a percent of GDP)	10.9	11.7	12.2	11.0	12.6	13.3	12.9
Direct foreign investment (as percentage of GDP)	4.5	2.4	4.1	2.5	3.8	3.9	3.9
Nominal GDP	10,693.7	10,914.6	12,019.1	11,923.3	13,387.0	14,932.5	16,680.9

Sources: Tanzanian authorities; and Fund staff estimates and projections.

1/ Arrears are on non-Paris Club official and commercial debt subject to rescheduling and currently under negotiation. Projection assumes these will clear once agreements are reached.

2/ Program and Project assistance (BOP coverage) as percentage of GDP.

Table 7. Tanzania: Disbursements of Program Assistance, 2003/04 - 2005/06 1/

(In millions of U.S. dollars)

	2004/05							2005/06				2003/04	2004/05		2005/06
	Act.	Prog.	Act.	Prog.	Act.	Prog.	Est.	Proj.	Proj.	Proj.	Proj.	Act.	Prog.	Est.	Proj.
	Sep.	Dec.	Dec.	Mar.	Mar.	Jun.	Jun.	Sep.	Dec.	Mar.	Jun.	FY	FY	FY	FY
Grants	288.3	121.4	184.5	57.8	43.0	42.3	18.1	316.8	140.1	36.1	14.9	338.3	501.9	534.0	507.9
Multilateral	128.6	0.0	26.5	0.0	0.0	0.0	0.0	47.1	0.0	0.0	0.0	71.6	128.6	155.1	47.1
EU PRBS grants 2/	38.3	0.0	0.0	0.0	0.0	0.0	0.0	47.1	0.0	0.0	0.0	39.0	38.3	38.3	47.1
World Bank	90.3	0.0	26.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	32.6	90.3	116.8	0.0
Bilateral	159.7	121.4	158.0	57.8	43.0	42.3	18.1	269.7	140.1	36.1	14.9	266.7	373.3	378.9	460.9
PRBS 2/	122.0	70.7	72.5	38.4	14.2	0.0	11.4	215.0	57.9	6.7	0.0	192.7	231.1	220.2	279.5
Sweden	15.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	17.8	0.0	0.0	13.1	15.8	15.8	17.8
Netherlands	0.0	18.1	18.1	16.9	0.0	0.0	0.0	0.0	13.5	0.0	0.0	31.5	35.0	18.1	13.5
Ireland	0.0	0.0	0.0	7.0	6.5	0.0	0.0	13.5	0.0	0.0	0.0	10.3	7.0	6.5	13.5
United Kingdom	81.9	33.0	38.8	0.0	0.0	0.0	0.0	163.5	0.0	0.0	0.0	100.4	114.9	120.7	163.5
Norway	11.4	2.8	3.2	0.0	0.0	0.0	0.0	13.2	3.3	0.0	0.0	13.6	14.2	14.6	16.5
Finland	2.2	0.0	1.7	0.0	0.0	0.0	0.0	5.4	0.0	0.0	0.0	1.8	2.2	3.9	5.4
Denmark	0.0	10.8	10.7	3.1	2.7	0.0	0.0	9.0	1.8	0.0	0.0	11.0	13.9	13.4	10.8
Switzerland	0.0	6.0	0.0	0.0	5.0	0.0	0.0	5.2	0.0	0.0	0.0	0.0	6.0	5.0	5.2
Germany	6.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	6.7	0.0	6.1	6.2	6.2	6.7
Japan	4.5	0.0	0.0	0.0	0.0	0.0	0.0	5.2	0.0	0.0	0.0	0.4	4.5	4.5	5.2
Canada	0.0	0.0	0.0	11.4	0.0	0.0	11.4	0.0	21.6	0.0	0.0	4.4	11.4	11.4	21.6
Sectoral baskets	37.7	50.8	85.5	19.4	28.8	42.3	6.7	54.8	82.2	29.4	14.9	74.0	142.2	158.7	181.3
Belgium	0.0	0.0	5.4	0.0	0.0	0.0	0.0	0.0	5.4	0.0	0.0	18.4	0.0	5.4	5.4
Canada	0.0	0.0	0.0	1.9	18.0	9.5	0.0	2.5	4.1	0.0	11.6	0.0	11.4	18.0	18.2
Denmark	6.8	10.3	9.5	0.0	0.6	0.0	0.0	16.9	0.0	1.2	0.0	9.5	15.5	16.9	18.1
EU	0.0	1.9	17.9	0.0	0.0	26.7	0.0	0.0	8.7	4.1	0.0	0.0	28.6	17.9	12.8
Finland	0.5	1.5	0.6	0.0	0.0	0.0	0.0	6.9	0.0	2.6	0.0	2.6	1.5	1.1	9.5
Ireland	4.8	1.8	2.1	3.6	2.2	0.0	0.0	10.1	0.1	0.0	0.0	6.0	10.2	9.1	10.2
Netherlands	13.6	0.0	23.3	0.0	0.0	0.0	0.0	0.9	28.2	0.0	0.0	9.4	9.3	36.9	29.1
Norway	2.1	4.0	4.0	6.9	2.2	0.0	0.0	2.3	9.9	4.7	0.0	8.1	11.5	8.2	16.9
Sweden	7.3	12.1	8.1	1.3	0.9	4.4	0.0	0.0	21.5	0.0	0.0	5.8	25.1	16.3	21.5
Switzerland	2.6	1.5	1.3	0.0	0.7	0.0	0.0	0.1	0.6	0.0	0.0	3.7	4.1	4.6	0.7
United Kingdom	0.0	14.4	8.8	2.2	3.8	0.0	6.7	10.9	0.3	15.3	1.8	0.0	16.6	19.3	28.3
Germany	0.0	2.6	3.4	2.6	0.0	0.0	0.0	4.2	1.7	1.5	1.5	7.9	5.2	3.4	8.9
Japan	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.5	0.0	0.0	0.0	0.0	0.0	0.5
Italy	0.0	0.0	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.0	0.0
France	0.0	0.7	0.8	0.7	0.4	0.7	0.0	0.0	1.2	0.0	0.0	0.0	2.0	1.2	1.2
Others	0.0	0.0	0.3	0.0	0.0	1.0	0.0	0.0	0.0	0.0	0.0	2.7	1.0	0.3	0.0
Loans	62.0	38.0	123.0	39.0	1.4	70.0	44.0	125.6	175.0	29.1	0.0	204.4	207.2	230.4	329.7
Multilateral	62.0	38.0	123.0	39.0	1.4	70.0	44.0	125.6	175.0	29.1	0.0	204.4	207.2	230.4	329.7
World Bank 3/	62.0	38.0	123.0	39.0	1.4	70.0	44.0	50.0	175.0	29.1	0.0	145.7	207.2	230.4	254.1
World Bank Loan	60.2	21.0	0.0	21.0	0.0	0.0	44.0	0.0	175.0	0.0	0.0	143.9	102.2	104.2	175.0
World Bank Basket Loans	1.9	17.0	123.0	18.0	1.4	70.0	0.0	50.0	0.0	29.1	0.0	1.8	105.0	126.3	79.1
African Devlopment Bank	0.0	0.0	0.0	0.0	0.0	0.0	0.0	75.6	0.0	0.0	0.0	58.7	0.0	0.0	75.6
Bilateral	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total program assistance	350.4	159.4	307.5	96.8	44.4	112.3	62.1	442.4	315.1	65.2	14.9	542.8	709.0	764.4	837.7
Cumulative from beginning of fiscal year	350.4	500.0	657.9	596.8	702.3	709.0	764.4	442.4	757.6	822.8	837.7	...	...	...	...
Memo items															
Total including HIPC/interim assistance	365.8	178.6	320.9	118.0	58.6	131.5	81.3	460.7	329.3	83.5	29.1	614.5	788.0	826.7	902.5
Of which: HIPC	15.4	19.2	13.4	21.2	14.2	19.2	19.2	18.3	14.2	18.3	14.2	71.8	79.0	62.3	64.9
IMF	2.0	2.6	2.6	2.8	2.5	2.6	2.6	2.5	2.5	2.5	2.5	11.7	10.1	9.8	10.0
IDA	9.0	15.9	10.1	13.0	9.1	16.0	16.0	11.0	11.5	11.0	11.5	46.4	55.4	44.2	45.0
AfDB	4.4	0.2	0.2	4.4	2.1	0.1	0.1	4.8	0.1	4.8	0.1	13.5	9.5	6.8	9.9
Others	0.0	0.5	0.5	1.0	0.5	0.5	0.5	0.0	0.0	0.0	0.0	0.2	4.0	1.6	0.0

Sources: Tanzanian authorities; and donors.

1/ Fiscal year: July-June.

2/ Poverty reduction budget support.

3/ Including loan baskets.

Table 8. Tanzania: Status of HIPC Initiative Agreements by Creditor

	Debt Relief in nominal terms (US$ mil.)	Agreement to provide relief beyond HIPC?	Comments
Multilateral Creditors			
IMF	120	n/a	Provided grants through PRGF-HIPC Trust fund.
AfDB/AfDF	190.7	n/a	Debt service reduction by 80% annually until debt relief delivered.
IDA/IBRD	1,157.10	n/a	Debt service relief of 69.1 and 63.6 percent on debts outstanding at end-june 1999 and 2001, respectively.
IFAD	24.5	n/a	Reduction of 100% of debt -service due.
BADEA	14.7	n/a	Concessional rescheduling of the debt and reduced interest rate.
OPEC	9.8	n/a	Concessional loans and restructuring of existing debt.
NDF	3.2	n/a	Contribution to HIPC initiative trust fund , to pay 100% debt service.
EADB	0.6	n/a	Reduced interest rate and extension of repayment period.
EU	37.9	n/a	Provided grants at the completion point to pay off outstanding loans.
Paris Club Creditors			
Austria	31.3	Yes	Bilateral Agreement for PC VII was signed on May 7, 2002.
Belgium	74.3	No	Bilateral Agreement for PC VII was signed on November 29, 2002.
Brazil	-	No	Reminder letter to submit draft agreement for PC VII sent May 19, 2004. Awaiting reply.
Canada	31.1	Yes	Bilateral Agreement for PC VII was signed on October 16, 2002.
France	89.9	Yes	Bilateral Agreement for PC VII was signed on March 6, 2003.
Germany	60.6	Yes	Bilateral Agreement for PC VII was signed on April 29, 2003.
Italy	132.0	Yes	Bilateral Agreement for PC VII was signed on May 7, 2002.
Japan	108.9	n.a.	Bilateral Agreement signed on March 2, 2004 has cancelled 100% of ODA loans. Not yet offered debt relief on commercial and part of bilateral (Japanese Food Agency) debts.
Norway	11.1	Yes	Bilateral Agreement for PC VII was signed on December 5, 2002.
Netherlands	99.1	Yes	Bilateral Agreement for PC VII was signed on March 17, 2002.
Russia	69.6	No	Bilateral Agreement for PC VII was signed on July 18, 2003.
U.K.	129.2	Yes	Bilateral Agreement for PC VII was signed on July, 2002.
United States	21.3	Yes	Bilateral Agreement for PC VII was signed on July 4, 2002.
Non-Paris Club Bilateral Creditors			
Algeria	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Angola	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Bulgaria	15.1	No	Bilateral Agreement was signed on December 12, 2003.
China	37.7	n.a.	15 interest-free loans maturing 31 Dec 1999 cancelled.
Czech Republic	-	No	The debt has been assigned to Lazard.
Egypt	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Hungary	-	No	In active negotiations.
India	19.7	No	Bilateral Agreement signed on September 14, 2004 has cancelled all intergovernmental loans.
Iran	-	No	In active negotiations.
Iraq	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Kuwait	31.8	n.a.	Signed bilateral agreement on March 8, 2003. Rescheduled 9 pre-CD loans.
Libya	-	No	In active negotiations.
Romania	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
UAE	-	No	In active negotiations.
Yugoslavia	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Zambia	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Zimbabwe	-	No	Diminimus Clause

Source: Bank of Tanzania

Table 9. Tanzania: Millennium Development Goals

	1990	1995	2001	2002
1. Eradicate extreme poverty and hunger	2015 target = halve 1990 $1 a day poverty and malnutrition			
Population below $1 a day (percent)	..	19.9	..	..
Poverty gap at $1 a day (percent)	..	4.8	..	..
Percentage share of income or consumption held by poorest 20 percent	..	6.8	..	..
Prevalence of child malnutrition (percent of children under 5)	28.9	30.6	29.4	..
Population below minimum level of dietary energy consumption (percent)	35	49	43	..
2. Achieve universal primary education	2015 target = net enrollment to 100			
Net primary enrollment ratio (percent of relevant age group)	51.4	47.7	54.4	..
Percentage of cohort reaching grade 5 (percent)	78.9	81.3	..	..
Youth literacy rate (percent ages 15-24)	83.1	87.1	91.1	91.6
3. Promote gender equality	2015 target = education ratio to 100			
Ratio of girls to boys in primary and secondary education (percent)	95.5	96.7	100.3	..
Ratio of young literate females to males (percent ages 15-24)	86.5	90.7	94.8	95.3
Share of women employed in the nonagricultural sector (percent)	33.1	..	..	..
4. Reduce child mortality	2015 target = reduce 1990 under 5 mortality by two-thirds			
Under 5 mortality rate (per 1,000)	163	164	165	165
Infant mortality rate (per 1,000 live births)	102	103	104	104
Immunization, measles (percent of children under 12 months)	80	78	83	89
5. Improve maternal health	2015 target = reduce 1990 maternal mortality by three-fourths			
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	1,500	..
Births attended by skilled health staff (percent of total)	43.9	38.2	35.8	..
6. Combat HIV/AIDS, malaria, and other diseases	2015 target = halt, and begin to reverse, AIDS and other major			
Prevalence of HIV, female (percent ages 15-24)	..	..	8.1	..
Contraceptive prevalence rate (percent of women ages 15-49)	9.5	18.4	25.4	..
Number of children orphaned by HIV/AIDS (thousands)	..	..	810	..
Incidence of tuberculosis (per 100,000 people)	..	..	344	362.7
Tuberculosis cases detected under Direction of Trade Statistics (percent)	..	61	47	43.1
7. Ensure environmental sustainability	2015 target = various			
Forest area (percent of total land area)	45	..	43.9	..
Nationally protected areas (percent of total land area)	..	15.6	15.6	29.8
GDP per unit of energy use (PPP dollars per kg oil equivalent)	1.1	1.2	1.4	..
CO2 emissions (metric tons per capita)	0.1	0.1	0.1	..
Access to an improved water source (percent of population)	38	..	68	..
Access to improved sanitation (percent of population)	84	..	90	..
Access to secure tenure (percent of population)	..	..	..	..
8. Develop a Global Partnership for Development	2015 target = various			
Youth unemployment rate (percent of total labor force ages 15-24)	..	..	..	..
Fixed-line and mobile telephones (per 1,000 people)	3.1	3.3	17.1	24.1
Personal computers (per 1,000 people)	..	1.7	3.6	4.2
General indicators				
Population (millions)	25.5	29.6	34.5	35.2
Gross national income (billions of U.S. dollars)	4.8	4.9	9.4	9.7
GNI per capita (U.S. dollars)	190	160	270	290
Adult literacy rate (percent of people ages 15 and over)	62.9	69.2	76	77.1
Total fertility rate (births per woman)	6.3	5.7	5.3	5.0
Life expectancy at birth (years)	50.1	48.5	44.4	43.1
Aid (percent of GNI)	28.8	17.1	13.7	13.2
External debt (percent of GNI)	158.6	144.7	72.2	77.6
Trade (percent of GDP)	50.1	59.3	39.2	40.3

Source: http://www.developmentgoals.org

July 14, 2005

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. de Rato:

LETTER OF INTENT
AND MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

1. On behalf of the Government of the United Republic of Tanzania I hereby transmit the attached Memorandum of Economic and Financial Policies (MEFP) which reviews recent economic developments and progress in the implementation of the 2004/05 programme supported by the PRGF arrangement, and policies that Government intends to pursue for 2005/06 and the medium term.

2. Satisfactory progress was achieved and the programme has remained on track; all quantitative performance criteria were observed. The structural performance criteria and benchmarks are also on track, except for the performance criteria regarding submission to Parliament of the amendments to the Bank of Tanzania Act and the Banking and Financial Institutions Act.[1] This could not be completed by the scheduled date due to longer than expected consultations with Zanzibar and a tight legislative agenda, and will now be completed in July 2005. In this regard, we are seeking waivers of the non-observance of the structural performance criteria, and conclusion of the fourth review under the PRGF arrangement, and the consequent disbursement of the fifth tranche in an amount equivalent to SDR 2.8 million.

3. Implementation of the newly promulgated National Strategy for Growth and Reduction of Poverty (NSGRP, or MKUKUTA in Kiswahili), which sets economic growth, social well being of the population, and good governance and accountability as the pillars of the country's development agenda, will commence in 2005/06. In this regard, the Government remains committed to maintaining macroeconomic stability, including monetary and fiscal policies, as well as structural reforms particularly in the areas of domestic resource mobilization, strengthening of the financial sector, and improving governance. By implementing the measures set forth in the attached MEFP, the Government can achieve these objectives in coherence with the programme. The Government will continue to provide the Fund with the required information to assess progress in implementing the programme

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[1] The finalized Financial Sector Reform Implementation Action Plan was submitted to Government in June rather than end-May as envisaged in the benchmark.

and will also consult with the Fund on the adoption of any measures that may be appropriate at the initiative of either Tanzania or the Fund.

4. The Government of Tanzania intends to make the contents of this letter and those of the attached MEFP available to the public and authorizes its publication on the IMF website, together with Fund staff report on the fourth review under the PRGF, once the Executive Board completes the review.

Yours sincerely,

/s/
Basil P. Mramba (MP)
Minister for Finance

Attachment: Memorandum of Economic and Financial Policies.

MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES FOR 2005/06 AND THE MEDIUM TERM

I. Recent Economic Developments and Progress Under the Programme:

1. Substantial progress has been achieved in Tanzania's macroeconomic performance under the PRGF programme. During the calendar year 2004 6.7 percent growth in real GDP was attained compared to 6.3 percent previously projected, and an outturn of 5.7 percent in 2003. The higher than expected GDP growth stemmed almost entirely from the agriculture sector following favourable weather conditions and the recovery of some commodity prices. The annual rate of inflation (based on the newly revised CPI index) dropped from 4.3 percent at end-June 2004 to 4.0 at end-April 2005, mainly because of the weather related recovery in food production.

2. The fiscal performance for 2004/05 has remained broadly in line with the programme with overall budgetary performance being broadly in line with the budget estimates. Revenue collections for the year are estimated to have been slightly above the budget estimate, and more than 20 percent higher than in 2003/04, primarily on account of higher collections from VAT and income taxes as well as sharply higher non-tax revenue.

3. With regard to expenditure, there has been an improvement in overall execution by the spending units in 2004/05. Total recurrent expenditure is estimated at Tsh 2,608 billion in line with the budget estimates, while estimated development expenditure was Tsh 898 billion, slightly above budget because of higher foreign financing. Estimated net domestic financing of the budget is Tsh 79 billion, or about half of the programme target of Tsh 157 billion.

4. The Government has completed a review of various tax laws with a view to updating them in the coming year, including rationalisation of the administration provisions of different tax laws as part of the ring-fencing agenda. The main laws reviewed include The Tanzania Revenue Authority Act, 1995; The Value Added Tax Act, 1997; The Stamp Duty Act, 1972; The Road Toll Act, 1985; The Airport Service Charge Act, 1962. In addition, the TRA has continued with implementation of the reform initiatives stipulated in its Corporate Plan for 2003/04-2007/08 with support from various stakeholders including East AFRITAC of the IMF. A complete quality assurance review of the Customs and Excise Department reforms under the TRA's second corporate plan was completed in June 2005 as envisaged. This includes updating the action plan that focuses on post-clearance auditing and compliance. Following a transfer of 100 additional taxpayers to the Large Taxpayers Department last year, a further expansion of the Department has brought the number to 278 at end-June 2005. This will be accompanied by consolidation of the department's capacity through recruitment of staff with the requisite skills.

5. As a way to strengthen Treasury functionality and improve its expenditure management, the Government has introduced measures to curb the accumulation of expenditure commitments at year end, which had led to huge expenditure floats in the past

and impaired fiscal flexibility for executing first quarter budgets. Closer monitoring of the expenditure float will involve building capacity for improved cash management and the projections of monthly expenditure requirements by MDAs.

6. Public debt continues to be an area of focus on the basis of the National Debt Strategy (NDS). Recent developments in this area include the adoption by the National Debt Management Committee (NDMC) of a capacity building plan for the various institutions to fulfill the obligations specified in the NDS in collaboration with the Macroeconomic and Financial Management Institute (MEFMI) and as part of the Public Financial Management Reform Programme (PFMRP). The Government Loans, Guarantees and Grants Act of 1974 incorporating the changes introduced in 2003 has been distributed to all MDAs with a circular describing its effect in clear language. Enforcement of the legislation will be ensured through regular meetings of the relevant committees to advise the Minister for Finance on developments, including applications for new loans and public guarantees.

7. Progress was also made in the implementation of the PFMRP and includes the identification of core activities for each component as well as the processes, outcome and output indicators, and a structure for monitoring, reporting and controlling performance. The PFMRP has been mainstreamed into the budget to ensure consistency between strategic plans and budgets.

8. Substantial progress has been made in the procurement area by enacting a new law, The Public Procurement Act 2004, which has decentralised all tendering functions and established a Public Procurement Regulatory Authority.

9. A steady inflow of official foreign funds to the budget during 2004/05, coupled with HIPC debt relief, and an increase in exports of both goods and services, resulted in a considerable build-up of liquidity in the economy and subsequent pressure in liquidity management. The Bank of Tanzania continued to exercise vigilance in its monetary policy actions so as to keep the reserve money programme on track. The Bank of Tanzania continued to manage liquidity using domestic instruments (i.e. Government securities, and repurchase agreements) while complementing with sale of foreign exchange when appropriate. On the fiscal front, strong revenue collections that exceeded targets in most of the months in the period under review helped to contain reserve money within targets. The above measures enabled the Bank to observe the targets for reserve money throughout the year.

10. Consistent with the increase in demand for financing of the expansion in economic activities in the country, credit to the private sector increased by about 30 percent during the year ending June 2005, in line with the programme projection for 2004/05. The strong growth of private sector credit was sustained in part by the increased number of credit-worthy clients taking advantage of relatively favourable negotiated cost of borrowing in the domestic market. Also, the ongoing efforts by the Government to improve the business environment have influenced expectations of positive investment returns and therefore stimulated demand for private sector credit.

11. The tightened monetary policy stance of the Bank of Tanzania in response to high liquidity led to an upward pressure on interest rates. The overall weighted average yield for Treasury bills went up from 7.8 percent in June 2004 to 8.4 percent in March 2005. In line with the Treasury bill rate, the lending rate moved upwards from 14.2 percent in June 2004 to 15.6 percent in March 2005. Whilst, the weighted average time deposit rate stood at 4.3 percent in June 2004, it moved only slightly up to 4.5 percent in March 2005, and savings rate remained at around 2.5 percent throughout the year.

12. During the period under review, balance of payments developments were characterized by substantial growth in both imports and exports. The external accounts improved as a result of large inflows of external assistance and growth in the mining exports, a recovery in traditional exports and tourism receipts. On an annual basis, the current account deficit is estimated at $630 million, marginally below the programme target and virtually unchanged from the previous fiscal year. Exports are estimated to have increased to $1,456 million from $1,174 million in the previous year, whereas estimated imports rose to $2,574 million, up from about $2,155 million the previous year.

13. A steady inflow of foreign assistance, coupled with HIPC debt relief, resulted in the increase in official gross reserves to $2,137 million from about $1,878 million at end-June 2004, which is equivalent to about 7 months of 2004/05 estimated imports of goods and non-factor services. The nominal exchange rate of the shilling to the U.S. dollar depreciated slightly from Tsh 1,107 at end-June 2004 to Tsh 1,124 at end-May 2005.

14. During the year, the Government continued negotiations with both Paris and non-Paris Club bilateral creditors for debt relief on terms comparable to those under the Enhanced HIPC framework. As at end-June 2005, total debt relief received from Paris Club VII arrangement stood at an estimated $2.5 billion. The countries that offered debt relief are Austria, Belgium, Canada, France, Germany, Italy, Norway, the Netherlands, United Kingdom, USA, Russia and Japan. The U.K. offered additional relief this year of 10 percent of debt service obligations to IDA and ADB. Efforts are under way to have the remaining bilateral agreements signed with Brazil and other Japanese agencies namely EID/MITI and the Japanese Food Agency. With regard to Non-Paris Club members, only Bulgaria, India and Kuwait had offered debt relief in line with the HIPC framework. Bulgaria extended debt relief by canceling debt amounting to $15.1 million, and India offered debt relief by canceling all of its intergovernmental loans amounting to $19.7 million. Kuwait rescheduled its debt amounting to $31.8 million under terms that provided debt relief equivalent to 90 percent cancellation in NPV terms. Meanwhile, China offered debt relief by canceling debts worth $37.7 million. Meanwhile, dialogue is continuing with Abu Dhabi Fund, Hungary, Libya and Iran.

15. The Government has made substantial progress in the areas related to Private Sector Development (PSD). A major study on a new PSD strategy is under way and is scheduled to be completed by November 2005. This work will benefit from inputs from a Diagnostic Trade Integration Study (DTIS) currently being carried out by the World Bank. The reform

work in this area will increase the long-term growth potential of the economy and support poverty reduction through increased incomes. A coherent Monitoring and Evaluation (M&E) system for BEST, SME policy and PSD strategy is being developed and is expected to be institutionalized by November 2005. The Government has continued to mobilise resources and it is envisaged that the implementation of SME policy priority projects will start by November 2005. Reforms in the business licensing system have continued and the Draft Business Activities Registration Bill has been prepared which will eventually lead to the repeal of the Business Licensing Act of 1972.

16. The Government continues with its efforts to promote good governance in line with the NSGRP and the National Anti-Corruption Strategy and Action Plan (NACSAP). Quarterly reports are being prepared depicting progress made in the implementation of the MDAs' anti-corruption plans. Following broad consultations with stakeholders, proposals to amend the Anti-Corruption Law are in process. In addition, the Government is taking broad measures to strengthen the Good Governance Coordination Unit (GGCU) in the President's Office through, among others, increasing the number of staff and enhancing training.

17. The Government remains committed to implement the Public Service Reform Programme (PSRP) aiming at improving public service delivery so as to contribute to economic growth and poverty reduction. The reform strategy has continued to focus on attracting and retaining better qualified staff and strengthening human resource capacity in order to sustain the overall Government reform programmes. This will be achieved through the Government's long-term plan of capacity building as well as pay reform which is performance-oriented. A study is underway to establish a detailed analysis of the nature of and trends in employment allowances, and employment growth in order to make specific recommendations that would be consistent with improved rationality and an accelerated pace of salary enhancement within an affordable wage bill.

II. Economic Policy for 2005/06 and the Medium Term Strategy

A. The MKUKUTA and Overview of Medium-Term Economic Objectives

18. The recently adopted MKUKUTA charts in broad strokes, for the next five years, Tanzania's policy direction towards rates of broad-based economic growth of 8-10 percent per annum, and the attainment of the Millennium Development Goals. The MKUKUTA improves on the approach of the recent years' PRS in so far as it is organized around three clusters of outcomes: Growth and Reduction of Income Poverty; Improved Quality of Life and Social Well-Being; and Good Governance and Accountability. Thus, policy design and all government activities are being determined with respect to their contribution to achieving specific targets within these clusters. At the same time, the framework takes into account inter-sectoral linkages and synergies and pays more attention to cross-cutting issues, namely HIV/AIDS, gender, environment, employment, governance, children, youth, elderly, disabled and human settlement. By comparison with the PRS, it also gives more emphasis to economic growth in poverty reduction.

19. The emphasis on equitable economic growth translates into particular attention to stimulating private investment, developing infrastructure, building human capacity and a competitive economy. The MKUKUTA provides entry points for stakeholder participation in its implementation, starting out with a process where all levels and sectors of the government administration (i.e. including each MDA and the Local Government Authorities) are required to indicate how their policy interventions will contribute to achieving goals in the respective three clusters. In order to support rising household income and reduce income disparities, policy interventions in the following areas are also geared to boost district and regional economic growth: agriculture, roads, lands, energy, trade, tourism, mining, private sector environment—with emphasis on SMEs, establishing special economic zones, and formalizing property and business ownership. Improvement in the quality of life and social well being is to be realized through more equity and quality in the delivery of social services, including education, health, nutrition, water, sanitation, and shelter. Policy reforms concerning the third cluster, governance and accountability, focus on creating well functioning and fair justice and anti-corruption systems, and facilitating public access to information on laws, policies, and policy implementation (including public finances).

B. Real Sector

20. Strong growth is expected to continue across all sectors of the economy leading to overall economic growth of 6.9 percent in real terms in 2005 and, supported by the continued structural reforms and infrastructure investment, accelerating further to 7.5 percent over the medium term. Assuming normal rainfall, growth in agriculture is expected to remain strong, at around 6 percent a year in 2005-06 and over the medium-term, supported by the provision of extension services, facilitated access to agricultural inputs, and the continued reform efforts aimed at improving rural infrastructure and the availability of credit. Tanzania's mining sector received a boost in 2004 following Tanzania's ranking in the top ten list of global locations for mining investments by the mining industry's authoritative Annual World Risk Survey and growth should remain robust. Strong expansion is expected in 2005-06 in the manufacturing sector, agro-processing, trade, and construction. In the area of infrastructure development, Tanzania will undertake rural and peri-urban electrification projects involving different components of the power sector; improve the rail network and rehabilitate the ports through providing specialized equipment for handling containers and their removal into new customs inspection areas. Growth in tourism-related activities is expected to remain buoyant over the forecast period although further rapid expansion of the sector will be constrained by the limited park and accommodation capacity.

21. Inflation is expected to remain at an average of about 4 percent in 2005-06 and over the medium term. Although there are indications of potential food shortages in a few regions of the country that did not receive adequate rainfall during the short rains season, measures are being taken to distribute foodstuffs from the strategic grain reserve and from surplus to deficit areas thus dampening the pressure on food prices.

C. Fiscal Policy and Public Resource Management

22. In its preparations for the 2005/06 budget, the Government has been guided by two objectives, maintaining macroeconomic stability and translating the policies stipulated in the MKUKUTA into the budget. The newly developed Strategic Budget Allocation System (SBAS) has ensured this strategic linkage, with the central government budget allocating about 48 percent of total funds for the implementation of the MKUKUTA to the cluster of Growth and Poverty Reduction, about 44 percent to Quality of Life and Social Well-Being, and about 8 percent to Governance and Accountability. MKUKUTA-related funding accounts for about 54 percent of central government budget allocations. Over time, as work on the full costing of the MKUKUTA progresses, the Government's Medium-Term Expenditure Framework is expected to translate comprehensively policy objectives into programmes, targets and activities. Nevertheless, already today, the expenditure programmes are driven by policy priorities and disciplined by budget realities, such as institutional capacity and resource constraints. In order to mitigate these constraints, the Government will press ahead with its ongoing programmes of strengthening public administration systems and domestic resource mobilization.

23. The Government's budget for 2005/06 envisages an increase in domestic revenue, and higher domestic financing with a concomitant increase in expenditures. Domestic revenue collection for 2005/06 is expected to reach at least 14.3 percent of GDP. The envisaged 0.7 percent of GDP increase in comparison to FY 2004/05 reflects: (i) the full-year effect of the introduction of the new Income Tax Act (ITA); (ii) the impact of tax administration reforms on VAT and income tax revenues (in particular related to the Large Taxpayer Department(LTD)); (iii) the graduation of a number of tax-exempted companies into the tax bracket, and (iv) increased non-tax revenue associated with coming into stream of gas-related projects. It will also be bolstered by the ongoing comprehensive tax reform programme as described below.

24. The overall expenditure level is budgeted to increase by 3.3 percentage points of GDP in 2005/06. Wages and salaries are projected to increase to 4.7 percent of GDP, consistent with our Public Service Reform Programme (PSRP) aiming at improving public service delivery so as to contribute to economic growth and poverty reduction. The Government's reform strategy, developed in consultation with major development partners, has continued to focus on attracting and retaining better qualified staff and strengthening human resource capacity in order to sustain the overall government reform programmes. The budget for goods and services shows a sharp increase, from 12.8 percent to 14.4 percent of GDP. However, as noted below, it is expected that actual outlays under this item will be lower. Development expenditure is budgeted to increase by 1.2 percent of GDP to 8 percent of GDP, especially reflecting higher infrastructure investment. Despite the significant levels of external support for investment, it is still not sufficient to meet the substantial demand for public investment in our country. Externally financed assistance therefore needs to be supplemented by domestic financing in order to enhance the productive capacity of the

economy. Our ongoing efforts to improve expenditure management and efficiency, and for greater involvement of local governments, are discussed below.

25. The revenue and expenditure estimates noted above would lead to an overall budget deficit equivalent to 14 percent of GDP, or 6.5 percent of GDP after grants, with domestic financing equivalent to 2.6 percent of GDP. However, we believe the outturn will be markedly lower. As always, the budget is prepared on a cautious basis and Tanzania has almost always over-performed against the programme's domestic financing targets through both higher revenue and tight control of expenditure. Moreover, noting the importance of expanding spending on infrastructure, we have requested additional support from our development partners. In any event, we will continue to strike a balance in the demand for domestic resources from the public sector to ensure that it does not crowd out productive private sector activities. To this end we are firmly committed to limit domestic financing to no more than Tsh 164 billion, or 1.1 percent of GDP. If necessary, the expenditure constraint would be mainly in the area of scaling back the significant increase in goods and services included in the budget.

26. In cognizance of the need to strengthen development and eventually to reduce external dependency, the Government will continue to enhance domestic resource mobilization. Further strengthening of tax administration will be in line with the TRA Corporate Plan, in particular: (i) reorganizing of the TRA along functional lines, and strengthening the LTD, with emphasis on making self-assessment fully functional, enhancing audit capacity, and further expanding its coverage of the LTD; and (ii) improving services to taxpayers. To enable additional taxpayers to obtain all tax services they need under one roof, it is expected that new centers in 15 additional districts will be established. We are also developing an Action Plan, to be completed by June 2006, to establish a single department with responsibility for all domestic taxes.

27. Efforts to streamline customs are continuing, including: (i) continued application of risk management tools in the customs administration; (ii) enhancing the post-clearance audit and verification unit; (iii) transmitting master manifests from arriving vessels directly to customs; and (iv) creating an intelligence unit at customs. Moreover, with technical support from the World Customs Organization, we are conducting a Time Release study to determine how the clearance process can be further improved. Moreover, the Government is working with other EAC members to harmonize the implementation of customs administration practices and procedures in line with the Customs Union Protocol. To increase the efficiency of post-clearance audit, we plan to increase the number of staff in this section from the current 14 to 32 by end-March 2006 (structural benchmark). Also, by end-January 2006, we plan to integrate the destination inspection programme with custom procedures to rationalize processes and tasks at the Dar es Salaam custom offices (structural benchmark).

28. The Government's focus remains on improving expenditure management and greater involvement of local government agencies (LGAs) in expenditure execution as instruments for reducing poverty. To this end, the Government will continue to implement expenditure management reforms along several tracks. First, concerning the linkages between the

MKUKUTA and the budget, the following steps will be taken: (i) more comprehensive costing of the MKUKUTA interventions; (ii) developing a budget-linked monitoring and reporting system for the MKUKUTA targets; and (iii) strengthening the Integrated Financial Management System (IFMS) by linking the new budget allocation system (SBAS) with the accounting and control system (EPICOR). Second, the increasing devolution of spending to lower levels of government will need to be accompanied by the following efforts in capacity building: (i) at the stage of working with budget guidelines, the LGAs will need to be fully integrated into the budget preparation process, through both direct allocations from the central government budget and reconciliation of their own budget plans with the MKUKUTA and the MTEF; (ii) at the stage of monitoring of spending execution, through the technical support programs of the Accountant General's office, help set up integrated reporting systems that facilitate spending control; and (iii) recognizing the need for closer supervision of the budget process of LGAs, efforts will be strengthened to obtain detailed monthly expenditure reports before releasing further funds to LGAs. The Government will give high priority to these improvements, given that 19 percent of the recurrent expenditures and 4 percent of the development expenditures of the central government budget are to be transferred to local authorities via grants.

29. The Government will also continue to address other issues of expenditure management. In order to avoid problems arising from a large carry-over of payment obligations into the start of a new budget year, the Government will monitor closely adherence to new guidelines that limit the commitment period for MDAs towards the end of the fiscal year. It will also tackle shortcomings in projecting monthly expenditure requirements, which have complicated liquidity management. In this context, it will examine whether a quarterly or monthly budget allocation would be better for expenditure and liquidity management (currently priority sectors operate under a quarterly system while other sectors receive monthly allocations). As far as recording of donor-funded project spending is concerned, there has been significant progress, as more development partners have agreed to lodge funds in the exchequer system instead of in decentralized project accounts. Nonetheless, in-kind project support still poses recording problems. Lastly, the Government has requested assistance from EAST AFRITAC for reviewing the Public Finance Act 2001 and related regulations. The objectives are to realign the Act with other legislation that has been updated in recent years, and to review the organizational structure of the Ministry of Finance.

30. As discussed among government, development partners, and stakeholders in the recent Public Expenditure Review, there is a clear need to strengthen internal and external audit of public expenditure. Parliament was called upon to play a stronger role in scrutiny of reallocations and enforcement of expenditure controls. To this end, the Government will strengthen the capacity of the National Audit Office, including facilitating more expeditious access to records, so that the reports on the audited budgets reach Parliament within the deadline stipulated by the law.

D. External Sector

31. The external sector is expected to continue benefiting from increased exports due to solid growth in the mining and manufacturing sectors, and a strong performance of traditional exports. The opening of a new gold mine this year will support continued strength in non-traditional export growth in the coming fiscal year. Expanded road infrastructure, the abolition of many local taxes and facilitated access to inputs for production are expected to continue to contribute to high growth in traditional exports volume. A benign environment for commodity prices should also contribute to the sector's recovery. On the import side, high oil prices and fast growth of imports of intermediate and capital goods, stemming from the Government's initiatives on infrastructure projects and transport for fertilizers, are expected to widen the trade deficit.

32. Developments in the trade balance will be financed by increased inflows in current transfers and the financial account. External aid financing is estimated to continue to increase in both grants and loans to reach 14 percent of GDP in the coming fiscal year. Increased net inflows to the balance of payments are projected to result in an overall international reserves position of around 6.2 months of imports of goods and non-factor services. Given the comfortable level of reserves, the BOT will continue to rely more heavily on foreign exchange sales to ease any consequent pressures on liquidity.

33. With regard to exchange rate management, the Government believes the real exchange rate is broadly in line with fundamentals. While moderate movements around the current level are expected, the Government is conscious of the fact that any excessive future depreciations or appreciations could hamper macroeconomic stability. Hence, the BOT will limit its interventions in the foreign exchange market to facilitate liquidity management and smoothing any short-run excessive fluctuations in the exchange rate.

34. The Government will persist in pursuing active negotiations with pending creditors for debt relief agreements under HIPC comparable terms. On the trade front, the Government is working within the framework of the EAC and SADC. Further progress in harmonization of any remaining conflicts within and outside the regional trade blocks is anticipated along with increased intra-regional trade in the coming years.

E. Monetary Policy

35. Monetary policy for 2005/06 will be directed towards ensuring that growth in monetary aggregates is consistent with the objectives of low inflation and higher economic growth, while maintaining sufficient official foreign reserves. Reflecting the ongoing expansion of financial intermediation, velocity is expected to continue to decline. Consistent with the expected increase in money demand, the BOT will target annual M3 growth of 27.0 percent, which would allow a further increase of credit to the private sector of about 33.2 percent. In line with the above objectives, the BOT will target a reserve money increase of

26.6 percent. We are committed to adjusting our policies as appropriate to meet these targets and objectives, which are fully consistent with the programme supported by the PRGF.

36. To meet reserve money targets, the BOT will continue to sterilize the liquidity injected through inflows of donor support to the budget and maturing debt instruments by offering adequate monetary policy instruments for rolling over the maturing securities and mopping up the excess liquidity in the economy, including through sales of foreign exchange. The BOT recognizes the tradeoffs involved in the mix of sterilization instruments. The absorption of excess liquidity through open market operations can lead to short-and medium-term increases in interest rates, while sterilization through foreign exchange sales can result in possible appreciation of the exchange rate, and loss of competitiveness. In light of these tradeoffs, the BOT will continue to sell foreign exchange in the IFEM to complement open market operations in liquidity management and reduce pressure on interest rates on Treasury bills.

37. We recognize the challenges in implementing our monetary programme, particularly in light of the upward pressure on liquidity emanating from rising capital and aid flows. In support of the BOT's efforts to adequately forecast and manage those pressures, we will continue to pursue reforms to improve existing monetary policy instruments and to undertake policy-oriented research to enhance the efficacy of monetary policy implementation, as well as to improve liquidity forecasting. On the latter point, we will continue to strengthen capacity and policy coordination, including urging ministries to further strengthen their efforts to share information with the BOT on their planned expenditures. The Government recognizes the potential risks to inflation from higher M3 growth, but is confident that our inflation and economic growth objectives will be met, given continued strong demand for credit in productive sectors of the economy and other favourable conditions such as the ample supply of labor. We are committed to closely monitoring the economy for any signs of higher inflationary pressure.

F. Financial Sector Reform

38. During 2005/06 and over the medium term, the Government will implement Tanzania's comprehensive second generation Financial Sector Reform Programme (FSRP), which builds on the recommendations of the FSAP. The programme, which aims to optimise financial sector contribution to investment and growth of the economy, focuses on objectives in nine sectors, namely: policy framework (including legal reforms); banking supervision; financial markets; pension funds; insurance; microfinance; employment in the financial sector; land issues; and long-term development financing. The plan was finalized and submitted to Government in June 2005 rather than in May as envisaged in the structural benchmark under the PRGF, to allow additional time to incorporate input from the Bretton Woods Institutions, development partners, and other stakeholders. It is expected that the Inter-Institutional Committee for the FSRP will oversee broad implementation of the plan, with technical and financial support from development partners.

39. Our near-term priority is to put in place the Bank of Tanzania Act and Banking and Financial Institutions Act (BFIA). The critical importance of this legislation for updating the legal framework is discussed in more detail in our letter of intent of February 10, 2005. The two acts will modernize the regulatory and supervisory framework and capacity of the Central Bank, and cement in law the current operating practices of the BOT, while enhancing accountability of the BOT to the Government. Our reforms in this area are consistent with best practices of the legal and operational framework for the financial sector in the region. The amendments to the BOT Act will include a strengthening of the Board's role as the BOT's decision-making body, a strengthening of the transparency and accountability of the Bank for conduct of monetary policy, and an increase in the number of Deputy Governors. The amendments have been approved by cabinet and the Government will submit them to Parliament for first reading by end-July 2005.

40. In addition, the Government will take steps to ensure that the impact of costs of liquidity management, including interest on liquidity paper, do not influence monetary policy. The Government will protect the BOT's profitability during 2005/06 and beyond through direct payment of interest costs on liquidity paper which exceeds 15 percent of BOT's revenue.

41. The preferred bidder for the partial privatization of the National Microfinance Bank (NMB) was approved and announced by Government in April 2005, a structural performance criterion under the PRGF programme. The final negotiations with the preferred bidder will be concluded shortly. The Government is also pursuing the restructuring of the Tanzania Postal Bank, as part of our ongoing strategy to further boost competition and efficiency in the sector.

42. As noted in our letter of February 10, 2005, the Government is undertaking efforts to further improve the availability of medium-term credit to key sectors of the economy. The World Bank has been providing assistance in this area. To this end, the Government is taking or encouraging initiatives in three areas. First, the Government will soon launch a Development Finance Guarantee Facility (DFGF), to be managed initially by the BOT, which will provide partial government guarantees to commercial banks for their loans to development- and export-oriented projects. The DFGF scheme will have a governance and operating structure consistent with the following principles: (i) operate on market principles, be appropriately funded from the budget, and protect public resources; (ii) include strong and transparent governance; and (iii) provide for appropriate risk-sharing with commercial banks with a maximum share of risk to the Government of 50 percent. With a view to starting the scheme on a prudent basis, we will limit the Government's initial exposure under the DFGF to T Sh 120 billion (about 0.8 percent of GDP), not including a credit guarantee already in place.

43. Second, the Government hopes to facilitate creation of a privately owned and managed long-term financing facility (LTFF) that would channel funds from nonbanks or banks and potentially development partners (without government guarantee) to be on-lent to commercial banks on a long-term basis. The commercial banks would be fully responsible

for repayment of the loans, and the Government will explicitly state that there will not be any government guarantee under the LTFF, and that participation of all parties involved would be on a fully voluntary basis.

44. Third, the Government will transform the Tanzania Investment Bank into a Development Finance Institution (DFI). The DFI will channel multilateral and bilateral donor funds and government seed money voted in the budget, but not take any new deposits from the public other than its credit customers. The DFI would not raise any funds under government guarantee, other than concessional funds from donors and will operate with strong governance structures.[1] The Government is receiving advice from the World Bank on best practices in this area.

45. To help maintain high standards and public confidence in the DFGF and the DFI, and generally to promote transparency and good governance, the Government will ensure that both facilities are subject to an annual independent operational audit to verify that the funds are being used for the purposes intended and that proper governance procedures have been followed. While we believe these schemes can play a positive role in the near-term, we expect that the acceleration of structural reforms in the financial sector will ensure that these schemes will eventually diminish substantially.

46. Consistent with the FSRP plan, the Government will advance reforms in the pension fund sector. The system is currently solvent, though with low overall coverage of the population, and it plays an important role in the financial sector. To address potential weaknesses, the inter-agency committee on financial sector reforms will submit to Government a proposed unified legal and regulatory framework for all pension funds, along with investment guidelines by June 2006. The World Bank is expected to provide technical assistance in this regard. We expect this effort, particularly the development of investment guidelines, to facilitate the channeling of pension funds' resources into longer term lending through commercial banks.

G. Other Structural Reforms

47. The Government is actively pursuing governance and business environment reforms in a number of areas. As noted above, a draft new Anti-Corruption Law prepared by the Law Reform Commission is being reviewed by Government. In order to provide a comprehensive framework for the effective prosecution of incidents of corruption.and to facilitate convictions and recovery of assets from prosecutions, the new law contains provisions that would allow the Prevention of Corruption Bureau unfettered access to information and evidence deemed necessary to conduct investigations as well as provisions for forfeiture and seizure of assets. The provisions contained in the new draft Law would be in line with

[1] For the definition of nonconcessional loans, see para. 9 of the Technical Memorandum of Understanding attached to the Government's letter of July 22, 2004.

Tanzania's obligations under the UN Convention Against Corruption, the African Union Convention on Preventing and Combating Corruption, and the SADC Protocol Against Corruption which the Parliament ratified in 2004. Cabinet approval of the new Anti-Corruption Law is expected by April 2006 and will be a structural benchmark of the programme.

48. Consistent with the structural benchmark in the PRGF programme, draft anticorruption strategies and action plans for all Local Government Authorities were prepared and submitted to the Good Governance Coordination Unit (GGCU) in June 2005, with implementation starting in 2005/06 The Government will introduce, on a pilot basis, the mechanism for complaints and grievances to deal with unethical conduct of civil servants in two MDAs in November 2005, and extend the mechanism to 10 MDAs by November 2006 and roll it out to all MDAs by November 2007.

49. A draft bill on Business Activities Registration and Reform of the Regulatory Licensing System has been prepared and is expected to be submitted to Parliament in July 2005. To establish a well functioning, transparent, and efficient business registration system, the Government is undertaking additional actions including the harmonization of mandatory sectoral regulatory licenses, and will prepare the necessary regulations upon enactment of the Business Activities Registration Law. The Government has approved the Strategic Plan for the Implementation of the Land Laws that will operationalize the Land and Village Land Acts. The implementing mortgage regulations for the Act were approved on June 30, 2005.

50. A review of the crop boards has been undertaken and a strategy for the implementation of the Crop Board Reform Study was adopted by Government in June 2005. Under the strategy, cash crop levies will be abolished with the Government assuming direct funding of the boards, and the Crop Board Acts will be amended to streamline crop board functions and to provide a clearer delineation of public and private functions in the areas of market regulation, product quality, and input markets. The Government will also consider options to reduce and rationalize the regulatory fees imposed by various self-financing government regulatory agencies on private businesses that hamper their development. In this regard, the Government will consider whether the regulatory bodies could be funded through the budget and not through the imposition of regulatory fees as a source of revenue.

51. The Government continues to monitor closely the developments in the energy sector, with a view to avoiding power shortages or escalation of the cost of energy. In this connection, the Government is considering options for restructuring the long-term debt of TANESCO, and is discussing the feasibility of another gas-to-electricity project with private sector participation in southern Tanzania. To create the environment conducive to further private sector participation, the Electricity, Water and Utilities Regulatory Authority (EWURA) has been established and the Electricity Act is being reviewed. Recruitment of key staff for EWURA is under way.

Table 1. Tanzania: Quantitative Performance Criteria and Benchmarks Under the Poverty Reduction and Growth Facility Arrangement, March 2005 - June 2006

	2005					2006	
	March		June	Sep.	Dec.	March	June
	Performance Criteria	Actual	Benchmark	Performance Criteria	Indicative Targets	Indicative Targets	Indicative Targets
Net domestic financing of the government of Tanzania (ceiling) 1/ 2/	48	-81	157	-101	-144	-42	164
Accumulation of budgetary arrears (ceiling; indicative target only)	0	0	0	0	0	0	0
Net domestic assets of the Bank of Tanzania (ceiling; indicative target only) 2/	-769	-885	-776	-894	-963	-806	-641
Reserve money (ceiling)	984	977	1,028	1,133	1,235	1,250	1,302
Net international reserves of the Bank of Tanzania (floor) 3/	1,545	1,639	1,589	1763	1921	1790	1685
Accumulation of external payments arrears (ceiling) 4/	0	0	0	0	0	0	0
Contracting or guaranteeing of external debt on nonconcessional terms (ceiling)	0	0	0	0	0	0	0
Memorandum item:							
Foreign program assistance (grants and loans) 1/	596	702	709	442	758	823	838

Note: For precise definitions of the aggregates shown and details of the adjustment clauses, see the technical memorandum of understanding (TMU) attached to the government's letter of July 22, 2004.

1/ Cumulative from the beginning of the fiscal year (July 1).

2/ To be adjusted upward for the Tanzania shilling equivalent of any shortfall in foreign program assistance from the amounts shown in the memorandum item. Figures are different from BoT (NDA) in the monetary authorities' accounts, as they are adjusted for the program exchange rate.

3/ To be adjusted downward for any shortfall in foreign program assistance from the amounts shown in the memorandum item.

4/ Continuous performance criterion; excludes arrears on debt-service payments pending the conclusion of debt-rescheduling agreements.

Table 2. Tanzania: Structural Performance Criteria and Benchmarks Under the Poverty Reduction and Growth Facility Arrangement, January 2005-June 2005

Measure	Date of Implementation	Status
Tax policy and administration		
Expand the coverage of the Large Taxpayer Department to 250 taxpayers. 1/	End-June 2005	Observed.
Complete the quality assurance review of the Customs and Excise Department reforms under the TRA's second corporate plan, including an updating of the action plan focusing on post-clearance auditing and compliance. 1/	End-June 2005	Observed.
Submit to parliament an amendment of the Tanzania Investment Act, to limit the applicability of fiscal stability clauses to at most 5 years. 1/	End-February 2005	Observed.
Financial sector reform		
Issue final bid instructions for the sale of the National Microfinance Bank (NMB). 2/	End-January 2005	Observed.
Government approval and announcement of preferred bidder for National Microfinance Bank (NMB). 2/	End-June 2005	Observed.
Submit to Parliament amendments to the Bank of Tanzania Act and the Banking and Financial Institutions Act. 2/	End-April 2005	Delayed. Waivers requested. Submission expected in July 2005.
Finalize and submit to government the Financial Sector Reform Implementation Action Plan. 1/	End-May 2005	Met with slight delay.
Governance		
Draft anti-corruption strategies and action plans to be completed for all Local Government Authorities and submitted for final government approval. 1/	End-June 2005	Observed.
Publicizing of the list of companies, individuals, and NGO's that have received tax exemptions each quarter under the Treasury voucher scheme. 1/	Quarterly	Observed.

1/ Structural benchmark.
2/ Performance criterion.

Table 3. Tanzania: Structural Performance Criteria and Benchmarks Under the Poverty Reduction and Growth Facility Arrangement, July 2005-June 2006

Measure	Date of Implementation
Tax policy and administration	
Integrate the destination inspection program with customs procedures at all customs offices in the Dar es Salaam region as described in paragraph 27 of the MEFP. 1/	End-January 2006.
Increase the number of staff in the post-clearance audit section of customs to 32 as described in paragraph 27 of the MEFP. 1/	End-March 2006.
Financial sector reform	
Limit Government guarantees under the three medium-term credit facilities as described in paragraphs 42-44 of the MEFP. 2/	Continuous.
Inter-agency committee on financial sector reform will submit to government a proposed unified legal and regulatory framework for all pension funds, and investment guidelines, as described in paragraph 46 of the MEFP. 1/	End-June 2006.
Governance	
The government will ensure that the instruments establishing the Development Finance Guarantee Facility and Development Finance Institution require an annual independent operational audit to verify that the funds are being used for the purposes intended and that proper governance procedures have been followed, as indicated in paragraph 45 of the MEFP. 1/	End-March 2006.
Cabinet approval of the new Anti-Corruption Law, as described in paragraph 47 of the MEFP. 1/	End-April 2006.
Publish the list of companies, individuals, and NGO's that have received tax exemptions each quarter under the Treasury voucher scheme. 1/	Quarterly.

1/ Structural benchmark.
2/ Performance criterion.

Tanzania: Relations with the Fund
(As of May 31, 2005)

I. Membership Status: Joined 09/10/62; Article VIII

II. General Resources Account:	SDR million	Percent Quota
Quota	198.90	100.00
Fund holdings of currency	188.90	94.97
Reserve position in Fund	10.00	5.03
III. SDR Department:	SDR million	Percent Allocation
Net cumulative allocation	31.37	100.00
Holdings	0.04	0.11
IV. Outstanding Purchases and Loans:	SDR million	Percent Quota
Poverty Reduction and Growth Facility	260.56	131.00

V. Financial Arrangements:

Type	Approval date	Expiration date	Amount approved (SDR million)	Amount drawn (SDR million)
PRGF	08/16/2003	08/15/2006	19.60	11.20
PRGF	04/04/2000	08/15/2003	135.00	135.00
PRGF	11/08/1996	02/07/2000	181.59	181.59

VI. Projected Obligations to Fund (without HIPC assistance)
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2005	**2006**	**2007**	**2008**	**2009**
Principal	23.73	46.32	46.61	42.89	36.65
Charges/interest	1.68	1.85	1.61	1.39	1.19
Total	25.41	48.17	48.22	44.28	37.84

Projected Obligations to Fund (with Board-approved HIPC assistance)
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2005	**2006**	**2007**	**2008**	**2009**
Principal	19.92	40.43	39.32	35.70	31.59
Charges/interest	1.68	1.85	1.61	1.39	1.19
Total	21.59	42.29	40.93	37.08	32.78

VII. Implementation of HIPC Initiative:

	Enhanced framework
Commitment of HIPC assistance	
Decision point date	Apr 2000
Assistance committed (NPV terms)[1]	end-June 1999
Total assistance (US$ million)	2,026.00
Of which: Fund assistance (SDR million)	88.95
Completion point date	11/21/01
Delivery of Fund assistance (SDR million)	
Amount disbursed	88.95
Interim assistance	26.68
Completion point balance	62.27
Additional disbursement of interest income[2]	7.45
Total disbursements	96.40

VIII. Safeguards Assessments:

Under the Fund's safeguards assessment policy, Bank of Tanzania (BoT) was subjected to an assessment with respect to the PRGF arrangement, which was approved on August 16, 2003 and is scheduled to expire on August 15, 2006.

A safeguards assessment of the BoT was completed on December 5, 2003 and concluded that whereas the bank had a relatively strong internal control environment, some vulnerabilities existed, notably in the external audit and financial reporting areas. Staff proposed recommendations are reported in Country Report No. 04/58. The BoT has implemented most of the recommendations of the safeguards assessment.

IX. Exchange Arrangements:

The currency of Tanzania is the Tanzania shilling. The official exchange rate is determined on the basis of the rate established in the interbank market for foreign exchange. The middle rate in terms of the U.S. dollar, the intervention currency, was T Sh 1,123 per U.S. dollar as

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[1] Net present value (NPV) terms at the decision point under the enhanced framework.

[2] Under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative, an additional disbursement is made at the completion point corresponding to interest income earned on amounts committed but not disbursed during the interim period, calculated using the average return (during the interim period) on the investment of resources held by, or for, the benefit of the PRGF-HIPC Trust.

of end-May 2005. The exchange system is free of restrictions on the making of payments and transfers for current international transactions.

X. Article IV Consultation:

The most recent Article IV consultation was concluded on August 6, 2004 (Country Report No. 04/285).

XI. Technical Assistance, 2001–05:

Department	Date	Form	Purpose
Fiscal Affairs	March 2001	Mission	Fiscal decentralization
	May 2001	Short-term consultant	Translation of government accounts and operationalization to the standard classifications
	October 2001	Mission	Report on Observance of Standards and Codes (ROSC) fiscal transparency module and preparation of an assessment and action plan for tracking poverty-reducing expenditure
	2001–02	Long-term consultant	Strengthening of fiscal analysis at the Ministry of Finance
	October 2002	Mission	Tax administration
	2002–03	Long-term consultant	Public expenditure management
	Mar.–May 2003	Peripatetic advisor	Tax administration
	April 2003	Mission	Inspection and tripartite review
	June–Sep. 2003	Long-term consultant	Public expenditure management
	Sep.–Oct. 2003	Peripatetic advisor	Tax administration
	Oct 2003	Mission	Tax administration
	November 2003	Multicountry mission	EAC tax harmonization
	April 2004	Mission	Customs administration
	July 2004	Peripatetic advisor	Tax administration
	July 2004	Mission	Public Expenditure Management Assessment and Action Plan
	September 2004	Mission	Review of mining taxation
	September 2004	Mission	Tax administration (Zanzibar)
	April 2005	Mission	Customs administration
Legal	Oct. 21–Nov. 2, 2002	Mission	Income tax law
	March 17–April 3, 2003	Mission	Income tax law
	Sept. 15–27, 2003	Mission	Income tax law
	June 6–13, 2004	Mission	Income tax law
	July 2004	Mission with MFD	Central and commercial bank legislative reform
	July–November 2004	Desk review	Foreign Exchange Act, Evidence

			Act, Bills of Exchange Ordnance, National Payment System bill, Electronic Transactions bill
Monetary and Financial Systems	March 2001	Mission	Monetary policy operations
	June 2001	Mission	Public debt and domestic market management
	2001–2002	General Advisor	General advice to the BoT
	Feb. 2003	Mission	Pre-FSAP mission
	May 2003	Mission	FSAP
	November 2003	Mission	FSAP follow-up workshop
	March 2004	Mission	Accounting and banking supervision
	June 2004	Mission	BoT accounting
	July 2004	Mission	Central and commercial banking legislation reform with LEG
	August 2004	Mission	Financial sector reform/FSAP follow-up
	November 2004	Mission	BoT accounting
	December 2004	Mission	Second FSAP follow-up workshop
	May 2005	Mission	Financial sector reform/FSAP follow-up
Statistics	May 2002	Mission	Balance of payments statistics
	2002–03	Long-term consultant	Multisector statistics
	October 2002	Mission	Data ROSC
	June 2003	Mission	Government finance statistics course
	January 2005	Mission	Monetary statistics

XII. Resident Representative:

Ms. Lelde Schmitz has been the Senior Resident Representative since January 2005.

Tanzania: Relations with the World Bank Group

Partnership in Tanzania's Development Strategy

The government of Tanzania's development strategy is set forth in its Poverty Reduction Strategy Paper (PRSP) and further refined in the first, second, and third progress reports, which were endorsed by the Bank's Board on November 27, 2001, May 29, 2003 and June 2, 2004, respectively. The PRSP focuses on three main areas of outcomes. The first is a reduction in the breadth and depth of income poverty. The outcome targets include a reduction in basic needs poverty and food poverty, with a particular focus on rural areas, where poverty is most prevalent. The second area is that of improving the quality of life and social well-being. More specifically, this entails improving human capabilities, enhancing longevity and survival, and social well-being (social inclusion and personal security), improving nutrition, and containing extreme vulnerability (mainly through safety nets). The third broad area is an environment conducive to development that can be sustained. This environment encompasses macroeconomic stability and good governance. The Government of Tanzania is finalizing the new PRSP (National Strategy for Growth and Reduction of Poverty commonly referred to under its Swahili acronym as MKUKUTA), in consultation with stakeholders, including development partners and civil society. The central objective of the MKUKUTA is to achieve faster, more equitable, and sustainable growth. It also stresses governance and accountability in the use of public resources and monitoring and evaluation to enhance the strategy's outcome-oriented focus.

Bank Group Strategy

The Bank's Board approved the current Country Assistance Strategy (CAS) for Tanzania on June 15, 2000. The World Bank is in to process of preparing a new Tanzania Joint Assistance Strategy (TJAS) together with other development partners drawing on the MKUKUTA to ensure alignment with the government's strategy. The TJAS is expected to be presented to the Board in FY2006. The focus of the current CAS is on higher economic growth, poverty reduction, and institutional reforms to improve governance. It conforms with the government's main strategy of adherence to macroeconomic stability, increased private sector participation in the economy, a renewed emphasis on rural development, and an improved delivery of social services. It also supports the government's desire to enter into new relationships with its development partners, based on the phased switching from projects to programs for more effective and efficient use of aid resources.

The Bank is providing support for the implementation of the Poverty Reduction Strategy through a series of Poverty Reduction Support Credits and Grants (PRSC). The first PRSC (total US$132 million, of which US$32 million in grants) was approved by the Bank's Board on May 29, 2003. The operation has been prepared in close collaboration with 11 other donors, who provide financial assistance through the Poverty Reduction Budget Support (PRBS) facility, using a joint performance assessment framework and a common review process. The focus of the PRSC/PRBS is on scaling up pro-poor growth, especially through a focus on rural development and improvements in the business environment. The

PRSC/PRBS also supports strengthening public expenditure management and public service delivery, especially in the priority sectors for poverty reduction, and putting in place a system to ensure that sectoral programs are accountable for their results. The second phase of the PRSC (PRSC-2; US$150 million, of which US$90 million in grants) was approved by the IDA Board on July 29, 2004. PRSC 3 is scheduled to go to the Board in early FY06. The implementation of policy reforms agreed upon under the PRSC is supported by a series of technical assistance and investment projects. These include project support to improve tax administration, reform the public sector, and develop the financial sector, including rural finance and microfinance.

In the social sectors, the Bank has approved adjustment lending operations for primary education between October 2001 and October 2004 and, most recently, secondary education (US$150 million each). The objectives include improving education, expanding school access, and increasing school retention at the primary and secondary levels. Bank support in this area has already facilitated a significant increase in school enrollment rates. The Bank contributes to the health sector multidonor “basket fund,” which supports reforms of the sector and provides funding for nonwage expenditures. A multisector HIV/AIDS project supports Tanzania’s efforts to reduce HIV transmission and mitigate the adverse consequences of AIDS. In the water sector, one project supports technical, commercial, and financial rehabilitation of the water supply and sanitation services in Dar es Salaam. Another project supports access to improved and sustained water and sanitation services in rural communities in Tanzania. The objective of the IDA-funded Tanzania Social Action Fund (TASAF) is to increase and enhance the capacities of communities and other stakeholders to prioritize, implement, and manage sustainable development initiatives and, in the process, improve socioeconomic services and opportunities. The Bank’s Board approved the Tanzania Second Social Action Fund (US$150 million) on November 30, 2004, as a follow-up to continue with the successful outcomes from TASAF-1.

In the agriculture sector, the Bank supports policy reforms through analytical work and the policy dialogue under the PRSC. The Bank also supported the country’s efforts to strengthen research and extension services from January 1998 to June 2004. A Participatory Agricultural Development and Empowerment Project Credit was approved by the Bank’s Board in May 2003 to support investments in appropriate technologies to reduce soil fertility decline. A Forest Conservation and Management Project assists the government in policy implementation, in particular by developing a framework for the long-term sustainable management and conservation of Tanzania's forest resources. Another project, covering Tanzania, Uganda, and Kenya, aims at improving management of the Lake Victoria ecosystem.

Efforts to improve Tanzania’s infrastructure are supported through projects in the road and railway sectors, as well as through an urban rehabilitation project. In April 2004, the Bank’s Board approved a credit in the amount of US$122 million to (1) upgrade strategic road links, (2) enhance road management capacity, and (3) improve the operations of Tanzanian Railways (TRC and TAZARA). The policy dialogue focuses on the preparation of a new

Road Act, which will provide the basis for strengthening the policy and institutional framework for road development and maintenance.

In the power sector, the Bank has helped the government implement the Power Sector Restructuring Program. It has encouraged the government to develop the domestic gas market and to generate lower-cost power through the Songo Songo Gas Development and Power Generation Project. Since 2003, an extended drought has caused electricity load-shedding in Tanzania's predominantly hydropower system. The Bank's Board approved an Emergency Power Supply Credit in the amount of US$45 million in June 2004.

Another recently approved project is the Local Government Support Project (US$52 million), which aims to strengthen fiscal decentralization, improve accountability in the use of local government resources, and improve the management of intergovernmental transfer systems. In addition, the project's objectives are to increase access to infrastructure and services in unplanned areas of Dar es Salaam and improve revenue performance for sustainable operations and maintenance.

The IFC's committed portfolio in Tanzania as of April 2005, stood at US$24 million. IFC's strategy for Tanzania has five focus areas: Building the financial market; Private investment in infrastructure; Small and medium size enterprise development; Tourism development; Privatization. In the micro, small, and medium enterprise sector, a joint IDA/IFC program is expected to go to the Board in FY2006. MIGA's outstanding portfolio in Tanzania, as of March 31, 2005, consists of one contract of guarantee for the Bulyanhulu gold mine, with a gross exposure of USD 75.8 million and a net exposure of USD 17.7 million.

Tanzania joined the World Bank Group in 1962. Beginning with an IDA credit for education in 1963, a total of 138 credits, 7 grants and 27 loans, totaling US$5.4 billion (US$5.1 billion from IDA) have been provided to Tanzania. Total disbursements amounted to US$4.4 billion as of April 30, 2005 (US$3.9 billion from IDA, US$355.6 million from the IBRD, and US$2.7 billion IDA grants). Currently, the portfolio comprises 23 active projects, with commitments of US$1.6 billion in all major sectors and an undisbursed balance of US$925 million.

Statement of Loans, Credits, and Grants (As of April 30, 2005; in U.S. dollars)

	IBRD	IDA Credits	IDA Grants	Total
Original Principal	361,030,400	4,784,469,393	274,400,000	5,419,899,793
Cancellations	5,477,944	231,622,023	0	237,099,967
Disbursed	355,552,456	3,897,916,330	182,169,644	4,435,638,430
Undisbursed	0	822,414,625	102,582,385	924,997,010
Repaid	355,903,982	396,433,973	0	752,337,955
Due	-441,526	3,842,480,538	0	3,842,039,012
Exchange Adjustment	441,526	0	0	441,526
Borrower Obligation	0	3,842,480,538	0	3,842,480,538

Source: World Bank Group

Bank-Fund collaboration in specific areas

The IMF and World Bank staffs maintain a close collaborative relationship in supporting the government's structural reforms. As part of its overall assistance to Tanzania—through lending, country analytic work, and technical assistance—the Bank supports policy reforms in the following areas in collaboration with the Fund:

- **Public expenditure management.** Improvements in public expenditure management have been one of the top priorities of the Tanzanian government since 1995. The Bank, the Fund, and other donors have worked closely to provide the government the needed support for institutional and policy reforms. While the Fund is leading the dialogue on fiscal policy, the Bank is focusing on strategic resource allocation and operational efficiency of public expenditures. In the area of overall fiscal policy, the reduction of domestically financed deficits has resulted in sustained macroeconomic stability over the past five years. To enhance strategic resource allocation and operational efficiency, the Bank is supporting a government-led, participatory public expenditure review/medium-term expenditure framework (MTEF) process. This effort that has supported the strengthening and opening up of the budget process as well as the allocation of resources to pro-poor priority areas. In addition to process, support, and analytical work in this area, the Bank is also supporting policy reforms through the PRSC. Another area of Bank involvement is the fiscal decentralization process through analytical work and the Local Government Support Project. The Bank and the Fund collaborate closely to support institutional budget and expenditure management reforms. The annual, Bank-led Public Expenditure and Financial Assessment Report (PEFAR), the first of which was issued in May 2005, serves as the main instrument for the donor community to assess progress in these areas. A joint Bank-IMF assessment of capacity to track poverty-reducing expenditure have all noted the improvements in public financial management and fiduciary systems in recent years. The Bank also prepared a Country Procurement Assessment Report, which provides an agenda for strengthening procurement systems in Tanzania.

- **Tax policy and administration reform.** The Bank and the Fund have, over the past few years, cooperated closely to support the government's efforts to modernize the tax system and to enhance the domestic revenue collection. While the Fund has taken the lead in reforms and adjustments of tax policy, the Bank has taken the lead in reforms to strengthen tax administration. As a result, the ratio of revenue to GDP ratio has increased in recent years, an outcome that is important to Tanzania's efforts to improve public service provision and fully finance the implementation of the poverty reduction strategy.

- **Financial sector reforms.** Tanzania has instituted far-reaching reforms in the financial sector. The Bank and the Fund have been working closely to support these policy reforms. In addition to contributing to the policy dialogue, the Bank has provided significant technical assistance for financial sector reforms. This includes two financial institution development projects that support, respectively, the withdrawal of the government from banking and nonbanking financial institutions and the strengthening of financial sector supervision. Successful outcomes of these reforms include the privatization of Tanzania's largest bank and the entry of a fairly large number of international banks into the Tanzanian market. Other areas of Bank involvement include the reform of the capital and securities authority, reform of pension systems, and liberalization of capital accounts. Through a separate project, the Bank supports the development of rural and microfinance services. A joint Bank-Fund Financial Sector Assessment was completed in June 2003.

- **Public service reform and improved service delivery.** In recent years, the government of Tanzania, with support from the Bank and other donors, has launched a number of major initiatives to improve performance and increase accountability, transparency, and integrity in the public sector. These include (i) the Public Service Reform Program (PSRP); (ii) the Local Government Reform Program; (iii) the Public Finance Management Reform Program; (iv) the National Anti-Corruption Strategy and Action Plans for Tanzania; (v) the National Framework on Good Governance, delineating a comprehensive approach to improve governance; (vi) the establishment of a Good Governance Coordination Unit (GGCU) in the president's office; and (vii) the launch of the Legal Sector Reform Program. Among these reforms, the PSRP has played a central role since its objective is to improve the accountability, transparency, and resource management of service delivery. The reforms are closely linked with other major reforms in public finance and decentralization. The PSRP aims at transforming the public service into a service that has the capacity, systems, and culture for client orientation and continuous improvement. Cooperation between the Bank and the Fund covers those areas where public sector reform has a direct impact on fiscal stability and public sector financial management.

- **Trade reforms.** The Bank and the Fund are working closely to assist Tanzania in establishing a pro-growth trade framework. Within the context of the Integrated Framework, the Bank is leading the preparation of a Diagnostic Trade Integration Study, which is currently being finalized. While the Fund is focusing on reforms of the tariff regime, the Bank is focusing on trade expansion though its regional trade facilitation project. The Bank is also involved at the regional level in the dialogue on trade reforms in the context of the East African Community.

World Bank Senior Country Economist: Robert Utz (202-473-0612)

Tanzania: Statistical Issues

The Tanzanian authorities cooperate fully in providing available data to Fund missions in a timely manner. Moreover, Tanzania's economic and financial database is adequate for surveillance and program-monitoring purposes, but remains weak despite considerable technical assistance and progress in some areas. Tanzania has few statistical publications and no fully articulated publication policy. Only limited data are reported for Zanzibar. The authorities are committed to improving the production and dissemination of macroeconomic and socio-demographic statistics in the framework of the General Data Dissemination System (GDDS). In October 2000, a GDDS multisector statistics mission assessed Tanzania's statistical systems and provided guidance on statistical practices and development in the areas of national accounts, price, foreign trade, balance of payments, fiscal, monetary, and socio-demographic data. Tanzania's GDDS metadata were initially posted on the IMF's Dissemination Standards Bulletin Board (DSBB) in July 2001 and last updated in May 2004 and January 2005. A mission to prepare the data module for a Report on the Observance of Standards and Codes (data ROSC) was completed in October 2002, and the report was published in March 2004.

National accounts

National accounts statistics are prepared by the National Bureau of Statistics (NBS) on the basis of data collected by its regional offices and by other government entities. But the data sources for compiling the estimates by expenditure category, the external sector data, and the indicators used to extrapolate benchmark production levels are deficient. These deficiencies impede the accurate estimation of the savings-investment relationship. To improve the quality of the national accounts, the authorities, with help from donors, are changing the base year of the national accounts to 2001 from 1992. It is expected that the new series, using data from the recent agricultural census and the 2000/01 household budget survey, will be published in the 2005/06 fiscal year.

Prices

The NBS compiles a monthly consumer price index (CPI) based on consumer expenditure in 20 urban centers. Since mid-May 1996, data have been reported within three weeks of the end of the month. In September 2004, the authorities began publishing the new CPI (retroactive to January 2003) using new weights calculated from the 2000/01 household budget survey data. Key changes are a reduction of the weight given to food from 71 percent to 56 percent and an expansion of the number of products. In addition, the authorities plan to publish regional price indices and expand the producer price index series.

Government finance statistics

Although the authorities provide Fund missions with monthly data on central government revenue, expenditure, and financing on a timely basis, the underlying concepts differ from international standards in the treatment of lending minus repayments and transfer payments. Despite improvements in the recording of government transactions, discrepancies remain between revenue and expenditure data, on the one hand, and financing data, on the other. The discrepancies are related to the lack of a fully integrated set of accounts and the delineation of the public sector and its sub-sectors. More specifically, discrepancies are due to different sources used for these data, and timing and coverage differences. The coverage of the central government sector in the fiscal data are different from that in the monetary data. Following the creation by the Ministry of Finance, with donor assistance, of a database of donor-funded projects in 2001/02 (July-June), the amount of foreign-financed projects reported by and channeled through the budget has increased significantly. No information is yet provided on the financial position of local governments, although the authorities stated their intention to produce these reports.

The government has completed the computerization of its accounting system for budgetary units, which the authorities indicate would allow resumption of reporting in the *Government Finance Statistics (GFS) Yearbook*. However, the computerized accounting system does not yet provide details about donor funded development expenditure and has not yet been extended to cover the extra-budgetary units. The authorities regularly report data for inclusion in the IFS.

Monetary statistics

Tanzania's existing monetary statistics are broadly adequate for policy and analysis purposes. Nevertheless, the October 2002 data ROSC and January-February 2005 monetary and financial statistics missions determined that the quality of monetary statistics was compromised by various methodological problems. In particular, the latter mission identified the following shortcomings: (a) an exclusion of savings banks from the institutional coverage of monetary survey, (b) an arbitrary application of the residency criterion by the commercial banks, (c) an inadequate subdivision of the resident sector data, (d) misclassification of certain accounting data between statistical aggregates, (e) discrepancies between reported interbank positions, (f) a non-transparent treatment of repurchase agreements, and (g) key information gaps in the bank reporting system. It was also found that international reserves data included certain assets that did not qualify as reserve assets.

To address these problems, the mission recommended that the Bank of Tanzania: (i) extend the institutional coverage of monetary statistics to include the postal bank and other savings banks, (ii) instruct commercial banks to classify accounts according to the client's properly determined residency status, (iii) use a more detailed scheme for sectorizing resident sector data, *in accordance with the Monetary and Financial Statistics Manual*, (iv) reclassify the misclassified accounting data and ensure construction of accurate statistical aggregates, (v) resolve discrepancies between reported interbank positions, (vi) treat repurchase agreements with commercial banks as a new financial instrument for providing or taking loans, and (vii) modify the bank reporting system to introduce certain additional sectors that are needed for collecting the currently missing information. The mission also recommended that the coverage of international reserves be redefined to include only those foreign assets that can provide ready external financing.

Balance of payments statistics

Foreign trade data are prepared by Fund staff missions on the basis of customs data from the BoT, which in turn are compiled by the Tanzania Revenue Authority (TRA) based on customs records. A balance of payments statistics mission in May 2002 found that there continued to be a significant under-recording of trade and that information on invisible transactions was sparse. The authorities have acknowledged these problems in their response to the data ROSC report published in March 2004 and have indicated that the BoT plans to commission a joint study by the NBS and the TRA to determine the magnitude of under-recorded trade and design an appropriate method of estimation. This study is expected to take place in 2005/06. Partial international investment position data are reported to STA.

Tourism revenue is estimated on the basis of foreign exchange records of the international transactions reporting system (ITRS). However, a tourism survey was recently introduced, and the results are expected to be released in 2005/06. The authorities intend to use the survey results to improve the reporting of revenue (preliminary estimates of tourism receipts are already being used for estimates and projections in the BOP statistics).

Information on official grant and loan receipts is prepared by Fund staff through contacts with official agencies. The data on current and capital transfers (grants) are estimates, based in part on data provided by the Ministry of Finance and, in part, on United Nations Development Program projections. Disaggregation of the data has improved, but more work is needed here and in the coverage and periodicity of data.

Data on private capital flows are presently quite weak. While some information on private banking sector flows can be derived from the monetary survey, other private capital flows are not adequately captured through ITRS records and are largely reflected in "errors and omissions." However, the authorities have made commendable progress in collecting information on certain integral components. In 1999, the BOT introduced the Private Capital Flows Survey, designed to capture information on foreign direct investment (FDI) inflows. However, the survey has only been formally conducted, in 1999 and in 2001. The survey asks investors to report committed and projected (for the near future) FDI flows. The BOT generally follows-up with informal contacts with selected investors for the purpose of maintaining up-to-date information until the next survey is conducted. The final report on the 2001 survey is expected by end-2005, but a preliminary series for FDI inflows has been incorporated in the BOP statistics.

Data on the gross and net official reserves of the BoT are provided monthly with a short lag and are available to the Fund more frequently on request . Similarly, data on the foreign assets and liabilities of the banking system are provided with relatively short lags.

Significant improvements in the quality of external debt data have been made in the context of the creditor reconciliation exercise under the HIPC Initiative. At present, all multilateral and Paris Club debts (accounting for about 80 percent of total external debt) have been fully reconciled. However, little progress has been made in reconciling debt owed to other bilateral and commercial creditors. Information on external debt not guaranteed by the public sector, mostly private sector debt, is also limited and not captured in a timely manner.

TANZANIA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE AS OF JUNE 28, 2005

	Date of latest observation	Date received	Frequency of data[6]	Frequency of reporting[6]	Frequency of publication[6]	Memo Items: Data Quality – Methodological soundness[7]	Memo Items: Data Quality Accuracy and reliability[8]
Exchange Rates	June 2005	June 2005	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	May 2005	June 2005	M	M	M		
Reserve/Base Money	May 2005	June 2005	D	D	M		
Broad Money	May 2005	June 2005	M	M	M		
Central Bank Balance Sheet	May 2005	June 2005	M	M	M	LO, LO, LO, LO	LO, O, O, O, LO
Consolidated Balance Sheet of the Banking System	May 2005	June 2005	M	M	M		
Interest Rates[2]	May 2005	June 2005	M	M	M		
Consumer Price Index	May 2005	June 2005	M	M	M	O, LO, O, LO	LNO, LNO, LNO, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	...	...	...	...	...	LNO, LNO, LNO, LO	LO, O, O, LO, O
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	Mar 2005	May 2005	M	M	Q		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Mar 2005	May 2005	M	M	A		
External Current Account Balance	Mar 2005	May 2005	A	A	A	LO, LO, LO, LO	LO, LNO, O, LNO, LNO
Exports and Imports of Goods and Services	2003	May 2004	A	A	A		
GDP/GNP	2004	May 2005	A	A	A	LO, LO, LO, LO	LNO, LNO, O, LO, LO
Gross External Debt	Mar 2005	May 2005	M	M	A		

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).
[7] Reflects the assessment provided in the data ROSC published March 23, 2004 and based on the findings of the mission that took place during October 2002 for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning (respectively) concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).
[8] Same as footnote 7, except referring to international standards concerning (respectively) source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.

External Debt Sustainability[1]

Tanzania's debt outlook remains solid, contingent on the continuation of Tanzania's reform efforts and sustained strong economic performance. However, vulnerabilities arise from Tanzania's aid dependency and the limited diversification of exports. As a result of the concessional nature of new borrowing and HIPC relief as well as the strong export performance in recent years[2], the NPV of external debt is currently around 20 percent of GDP and 120 percent of exports, while debt service is around 7 percent of exports. All indicators are below the indicative debt-burden thresholds (Table 1).[3, 4]

The baseline scenario assumes that Tanzania's marked improvements in economic performance in the recent past will be sustained and hence is more optimistic than the 10-year historical scenario (Table 2)**.** In particular, the baseline scenario assumes higher real GDP and export growth rates and higher levels of donor assistance and Foreign Direct Investment relative to the past 10 years.

The bound tests reveal that significant threats for debt sustainability would result from a year of poor export performance or, to a lesser extent, a reversal of Tanzania's economic performance to historical levels. (Table 2). Export value growth at one historical standard deviation below the baseline for 2005 would result in an increase in the NPV of debt to exports ratio above the indicative threshold of 200 for roughly the following three years. The exercise highlights the importance of strengthening and diversifying Tanzania's export sector to reduce its vulnerability to weather and terms of trade shocks. The bound tests also reveal that if the economy and exports were to grow at the average growth rates experienced during the past ten years, both the NPV of debt-to GDP ratio and the debt service-to-exports ratio would increase over the projection period. This underlines the need to sustain and deepen reforms, including improvements in the business environment, agricultural policies, and infrastructure investment.

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[1] This DSA was prepared by Fund and Bank staff under the Interim Guidance for Debt-Sustainability Assessments in Low-Income Countries (LIC DSA) (www.imf.org for details).

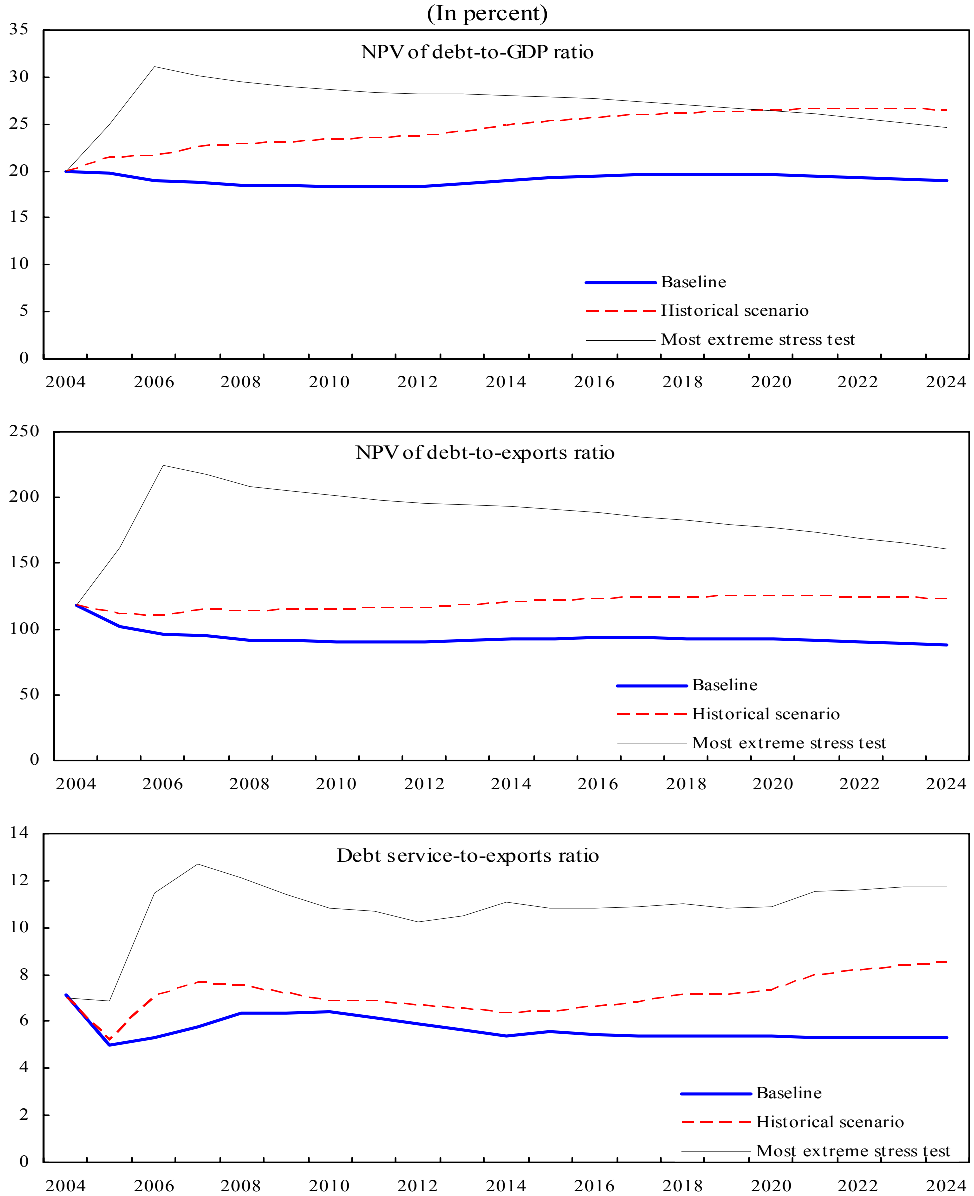
[2] The scenario assumes relief in HIPC comparable terms for all creditors with which there are pending agreements. See Table 7 of the staff report.

[3] As specified by the World Bank's Country Policy and Institutional Assessment Index, Tanzania is classified as a "Strong Performer". As such, the thresholds are: 200 percent of NPV of debt to exports ratio, 50 percent of NPV of debt to GDP ratio and 25 percent of debt service to exports ratio.

[4] Total public sector debt—including domestic debt—remains sustainable with the NPV of public debt and debt service at 230 and 10 percent relative to revenues. The indicative ratios are 300 and 35, respectively.

Given that Tanzania breaches the indicative threshold for LIC DSA on the NPV of debt-to exports ratio under the "stress test" scenario and that both the NPV of debt-to-export ratio and the debt service-to-export ratio increase under the historic scenario, staff classifies Tanzania as "moderate risk" as described in the Fund-Bank interim guidance for debt distress assessments. In addition, Tanzania's dependency on foreign aid makes it also highly vulnerable to a significant decline in donor grants. If the share of grant financing in total were to decline from the current levels of about 50 percent to 30 over the projection period (equivalent to a decline of about 1 percentage point of GDP), the behavior of debt indicators would reinforce the classification of "moderate risk" of debt distress as specified in the guidance.

Figure 1. Tanzania: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2004-2024
(In percent)



Source: Staff projections and simulations.

Table 1. Tanzania: External Debt Sustainability Framework, Baseline Scenario, 2001-2024 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Estimate	Projections								
	2001	2002	2003			2004	2005	2006	2007	2008	2009	2004-09 Average	2014	2024	2010-24 Average
External debt (nominal) 1/	**73.8**	**55.9**	**59.5**			**63.2**	**56.9**	**49.7**	**42.2**	**42.4**	**42.9**		**45.1**	**43.1**	
Of which: public and publicly guaranteed (PPG)	73.7	55.8	59.1			62.8	56.2	48.9	41.6	42.1	42.7		45.1	43.1	
Change in external debt	-4.9	-18.0	3.6			3.7	-6.2	-7.3	-7.4	0.2	0.5		-0.2	-0.2	
Identified net debt-creating flows	-1.9	-2.7	-4.6			-2.4	-2.6	-1.0	-1.0	-0.8	-0.8		-1.0	-1.2	
Noninterest current account deficit	**4.6**	**3.0**	**1.8**	**5.7**	**3.7**	**5.1**	**4.5**	**5.8**	**5.3**	**5.2**	**5.3**		**5.5**	**5.8**	5.6
Deficit in balance of goods and services	7.4	7.3	6.8			9.8	10.2	11.3	10.5	10.0	10.3		11.4	15.1	
Exports	15.2	15.2	16.7			16.9	19.3	19.7	19.7	20.1	20.2		20.6	21.6	
Imports	22.6	22.6	23.5			26.7	29.5	31.0	30.2	30.1	30.4		32.0	36.7	
Net current transfers (negative = inflow)	-4.5	-4.2	-4.8	-5.6	3.4	-4.9	-5.6	-5.1	-5.1	-4.7	-4.6		-5.2	-4.8	-4.9
Other current account flows (negative = net inflow)	1.6	-0.2	-0.3			0.2	-0.1	-0.4	-0.2	0.0	-0.5		-0.6	-4.5	
Net FDI (negative = inflow)	**-4.2**	**-3.8**	**-4.4**	**-3.5**	**1.6**	**-4.2**	**-3.9**	**-3.9**	**-3.8**	**-3.8**	**-3.9**		**-4.1**	**-4.7**	-4.3
Endogenous debt dynamics 2/	**-2.3**	**-1.9**	**-2.0**			**-3.3**	**-3.2**	**-2.9**	**-2.5**	**-2.2**	**-2.2**		**-2.4**	**-2.3**	
Contribution from nominal interest rate	0.7	0.8	0.6			0.4	0.7	0.8	0.8	0.7	0.7		0.5	0.5	
Contribution from real GDP growth	-4.3	-4.4	-3.0			-3.6	-3.9	-3.7	-3.3	-2.9	-2.8		-2.9	-2.8	
Contribution from price and exchange rate changes	1.3	1.6	0.4			…	…	…	…	…	…		…	…	
Residual (3-4) 3/	**-3.0**	**-15.2**	**8.2**			**6.1**	**-3.6**	**-6.3**	**-6.4**	**1.0**	**1.3**		**0.8**	**1.0**	
Of which: exceptional financing	-2.8	-2.6	-0.1			-0.4	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
NPV of external debt 4/	...	...	20.4			20.3	20.4	19.7	19.4	18.8	18.7		19.1	18.9	
In percent of exports	...	...	122.5			119.7	105.9	100.4	98.3	93.7	92.5		92.5	87.4	
NPV of PPG external debt	**...**	**...**	**20.1**			**19.9**	**19.7**	**19.0**	**18.7**	**18.5**	**18.4**		**19.0**	**18.9**	
In percent of exports	...	...	120.2			117.7	102.2	96.5	95.1	91.9	91.3		92.2	87.4	
Debt service-to-exports ratio (in percent)	32.5	25.4	10.0			9.2	9.5	9.2	8.9	8.1	7.6		5.7	5.3	
PPG debt service-to-exports ratio (in percent)	32.5	25.4	8.3			7.1	5.0	5.3	5.7	6.3	6.4		5.4	5.3	
Total gross financing need (billions of U.S. dollars)	0.5	0.3	-0.1			0.3	0.3	0.5	0.5	0.5	0.5		0.7	1.4	
Non-interest current account deficit that stabilizes debt ratio	9.5	21.0	-1.8			1.4	10.7	13.1	12.7	5.0	4.8		5.7	6.0	
Key macroeconomic assumptions															
Real GDP growth (in percent)	5.7	6.2	5.7	4.4	1.5	6.7	6.9	7.2	7.3	7.5	7.3	7.2	7.0	7.0	7.0
GDP deflator in US dollar terms (change in percent)	-1.6	-2.2	-0.7	3.2	9.5	2.8	4.9	4.0	4.0	1.8	1.4	3.1	1.4	1.4	1.4
Effective interest rate (percent) 5/	1.0	1.2	1.1	1.5	0.6	0.7	1.2	1.5	1.7	1.8	1.7	1.4	1.3	1.3	1.3
Growth of exports of G&S (US dollar terms, in percent)	9.5	4.5	14.8	5.9	12.9	11.3	27.7	13.8	11.8	11.8	9.0	14.2	9.0	9.0	9.0
Growth of imports of G&S (US dollar terms, in percent)	3.2	3.9	9.2	2.3	12.9	24.9	23.5	17.2	8.9	9.0	10.0	15.6	8.0	10.0	9.9
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	55.2	54.8	48.5	50.2	49.4	49.1	51.2	46.7	46.6	47.2
Memorandym item:															
Nominal GDP (billions of US dollars)	9.4	9.8	10.3			11.3	12.7	14.1	15.8	17.2	18.8		28.2	63.8	

Source: Staff simulations.

1/ Includes both public and private sector external debt.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
4/ Assumes that NPV of private sector debt is equivalent to its face value.
5/ Current-year interest payments devided by previous period debt stock.
6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2. Tanzania: Sensitivity Analyses for Key Indicators of Public and Publicly Guaranteed External Debt, 2004-24
(In percent)

	Estimate	Projections						
	2004	2005	2006	2007	2008	2009	**2014**	2024
NPV of debt-to-GDP ratio								
Baseline	20	20	19	19	18	18	**19**	19
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2005-24 1/	20	21	22	23	23	23	**25**	26
A2. New public sector loans on less favorable terms in 2005-24 2/	20	21	21	22	22	23	**27**	32
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2005-06	20	20	21	20	20	20	**21**	20
B2. Export value growth at historical average minus one standard deviation in 2005-06 3/	20	23	26	25	25	24	**24**	21
B3. US dollar GDP deflator at historical average minus one standard deviation in 2005-06	20	22	24	23	23	23	**24**	23
B4. Net non-debt creating flows at historical average minus one standard deviation in 2005-06 4/	20	22	22	22	22	21	**21**	20
B5. Combination of B1-B4 using one-half standard deviation shocks	20	25	31	30	29	29	**28**	25
B6. One-time 30 percent nominal depreciation relative to the baseline in 2005 5/	20	28	27	26	26	26	**27**	26
NPV of debt-to-exports ratio								
Baseline	118	102	97	95	92	91	**92**	87
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2005-24 1/	118	111	110	115	113	114	**120**	122
A2. New public sector loans on less favorable terms in 2005-24 2/	118	108	107	111	111	115	**133**	149
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2005-06	118	102	97	95	92	91	**92**	87
B2. Export value growth at historical average minus one standard deviation in 2005-06 3/	118	161	224	217	208	205	**193**	161
B3. US dollar GDP deflator at historical average minus one standard deviation in 2005-06	118	102	97	95	92	91	**92**	87
B4. Net non-debt creating flows at historical average minus one standard deviation in 2005-06 4/	118	112	114	112	107	106	**103**	91
B5. Combination of B1-B4 using one-half standard deviation shocks	118	152	194	188	180	177	**167**	140
B6. One-time 30 percent nominal depreciation relative to the baseline in 2005 5/	118	102	97	95	92	91	**92**	87
Debt service ratio								
Baseline	7	5	5	6	6	6	**5**	5
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2005-24 1/	7	5	7	8	7	7	**6**	9
A2. New public sector loans on less favorable terms in 2005-24 2/	7	5	7	7	7	7	**7**	10
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2005-06	7	5	6	7	6	6	**5**	6
B2. Export value growth at historical average minus one standard deviation in 2005-06 3/	7	7	11	13	12	11	**11**	12
B3. US dollar GDP deflator at historical average minus one standard deviation in 2005-06	7	5	6	7	6	6	**5**	6
B4. Net non-debt creating flows at historical average minus one standard deviation in 2005-06 4/	7	5	7	7	7	6	**6**	7
B5. Combination of B1-B4 using one-half standard deviation shocks	7	6	10	11	11	10	**10**	10
B6. One-time 30 percent nominal depreciation relative to the baseline in 2005 5/	7	5	6	7	6	6	**5**	6
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	46	46	46	46	46	46	**46**	46

Source: Staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import lelvels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Statement by the IMF Staff Representative
July 29, 2005

This statement describes developments since the staff report was issued on July 18, 2005. These developments do not change the thrust of the staff appraisal.

The amendments to the BoT Act and the Banking and Financial Institutions Act were submitted to parliament on July 18, 2005, thus meeting the end-April performance criteria.

Recent data indicate that economic and financial developments remained broadly in line with the program. The 12-month inflation rate at end-June 2005 remained in line with expectations at 4.2 percent, (compared with 4.3 percent at end-June 2004). Provisional data indicate that the end-June indicative target for reserve money was missed by Tsh 2 billion (two tenths of one percent) due to a delay in posting an end-June repurchase agreement with a commercial bank.

Press Release No. 05/177
FOR IMMEDIATE RELEASE
July 29, 2005

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fourth Review Under Tanzania's PRGF Arrangement and Approves US$4.1 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the fourth review of Tanzania's economic performance under a three-year Poverty Reduction and Growth Facility (PRGF) arrangement (see Press Release No. 03/127.) The completion of the review enables a further release of an amount equivalent to SDR 2.8 million (about US$4.1 million) under the arrangement, and will bring the total disbursements under the program to the equivalent of SDR 14.0 million (about US$20.2 million.)

Following the Executive Board's discussion on Tanzania's economic performance, Mr. Agustín Carstens, Deputy Managing Director and Acting Chair, stated:

"The Tanzanian authorities are to be commended for sustaining strong economic performance through market-oriented policies within an appropriate macroeconomic framework. The authorities will need to build on the recent success by maintaining sound policies and steadily pursuing key structural reforms and capacity building to remove key impediments to growth and make meaningful progress on poverty reduction. Sustained reform efforts to stimulate private-sector led growth will be needed, particularly in such areas as infrastructure, access to the financial sector, improving the business environment, trade facilitation, and governance.

"The authorities' decision to scale back the planned rapid expansion of government spending under the 2005/06 budget is commendable in view of the need to limit net domestic budget financing and reduce the risk of crowding out productive private sector activity. It will be important to protect priority and poverty-related spending while avoiding divergences between the program and budget expenditure levels, as they undermine the budget process and transparency. The authorities are committed to strengthening public expenditure management and addressing weaknesses in the budget preparation and execution process.

"Mobilizing domestic resources and raising the revenue-to-GDP ratio through better tax administration will provide resources for key expenditures for development and poverty alleviation, and reduce the dependence on foreign aid. In this regard, it will be essential to further enhance the operation of the VAT and income tax departments, further strengthen the Large Taxpayers Department, and continue efforts to streamline customs administration.

“The Bank of Tanzania’s monetary program is consistent with the growth and inflation objectives. The authorities deserve credit for their management of liquidity pressures that arise from high aid inflows and continue to present challenges to monetary policy. The Bank of Tanzania should continue to exercise vigilance and to use a full range of tools available for liquidity management and sterilization operations.

“The authorities’ efforts to develop the financial sector will benefit from the new financial sector reform plan. It is important that the government maintain its cautious and prudent approach to several new initiatives to facilitate medium-term lending and investment in the context of improving the availability of medium-term credit to key sectors of the economy. Specifically, maintaining strong governance and strict limits on government exposure under the Development Finance Guarantee Facility and the planned Development Finance Institution will be critical.

“Efforts should continue to reach debt relief agreements with non-Paris Club creditors under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative,” Mr. Carstens said.

The PRGF is the IMF's concessional facility for low-income countries. PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent and are repayable over 10 years with a 5 ½-year grace period on principal payments.

Statement by Peter Ngumbullu, Executive Director for United Republic of Tanzania and John Mafararikwa, Senior Advisor to Executive Director
July 29, 2005

Introduction

1. Tanzania, made significant progress in the reform agenda in the past decade and remains politically committed to strengthen and maintain macroeconomic policy performance and stability, deepening of structural reforms and implementation of the new PRS; the National Strategy for Growth and Reduction of Poverty, which emphasizes economic growth, social well-being, improved governance and accountability as the cornerstones for addressing the country's development challenges and meeting the MDGS. As the country heads towards the parliamentary and presidential elections at the end of October 2005, measures are being taken to ensure that balloting will be free, fair and peaceful. The new government is expected to continue with the political commitment to the country's peace and stability, implementation and maintenance of strong economic reform agenda within a sound macroeconomic framework and address the main issues of poverty reduction, key structural reforms, strengthening of institutional capacity as well as enhancing efforts towards mobilization of domestic resources, an essential element for reduction in aid dependency in the medium- and long- term.

2. The Tanzanian authorities would like to thank the Board and Management of the Fund for the continued support and assistance given to the country's reform agenda. They also thank the Fund Staff for the quality report prepared on Tanzania.

Recent Economic Developments and Program Performance

3. Tanzania's economy continued to benefit from the momentum of sustained macroeconomic achievements under the PRGF program, with real GDP growth reaching 6.7 percent during 2004, up from 5.7 percent recorded in 2003. Inflation declined from 4.3 percent recorded in June 2004 to 4.0 percent at end May 2005, following a rebound in food production, buoyed by good weather. During fiscal year 2004/05, fiscal performance continued to be strong, with revenue collections, surpassing the annual target, and above last fiscal year's collections by 20 percent, reflecting improved tax administration. Expenditure was broadly in line with budget estimates, except for slightly higher than projected development spending, financed from higher than projected external support. The government has also completed a review of various tax laws, with the intention of updating them in the coming year. The authorities completed the second corporate plan for the Tanzania Revenue Authority (TRA) in June 2005 as planned, and its implementation is expected to further improve the efficiency of the authority in revenue collection and administration.

4. The authorities continue to implement measures, aimed at further reducing the scope of public debt under the Public Financial Management Reform Program (PFMRP). The National Debt Management Committee (NDMC) recently adopted the national capacity

building plan, which will provide a basis for enhancing capacity in debt management, and government has distributed to all ministries and independent departments the amended Government Loans, Guarantees and Grants Act together with a circular, clarifying key amendments of the act and their application. Similarly, the new Procurement Law of 2004, which decentralizes the government tendering process, has been widely distributed. The authorities continued to negotiate with its creditors for debt relief, for terms comparable with those agreed under the enhanced HIPC framework. Efforts are underway to have bilateral agreements signed with Brazil and other Japanese agencies. They also thank non-Paris club countries, which offered debt relief to Tanzania in line with the HIPC framework, and discussions continue with remaining creditors.

5. On monetary policy, the Bank of Tanzania continued to exercise vigilance in its monetary policy operations, keeping liquidity in the economy at programmed levels. Credit to the private sector continued its upward trend, increasing by about 30 percent during 2004/05, following improved business climate in the economy and growth in the number of credit worthy borrowers.

6. The external current account deficit stabilized at last year's level as both imports and exports grew substantially. Large inflows of foreign assistance, recovery in traditional exports, higher receipts from tourism and increased mineral exports contributed to the improvement in the external account.

7. The government has continued to further its efforts to enhance good governance, by taking comprehensive measures to strengthen the Good Governance Coordination Unit (GGCU). These measures are part of the National Strategy for Growth and Reduction of Poverty (NSGRP), commonly referred to as MKUKUTA in Kiswahili and the National Anti-Corruption Strategy and Action Plan (NACSAP). Notwithstanding these impressive achievements, particularly in maintaining macroeconomic stability, structural reforms and improved private sector environment, the Tanzanian authorities are aware that many challenges remain. Poverty remains widespread, while the budget continues to be donor dependent. The government remains committed to measures that will address the remaining problems in the economy, as specified in its economic policy framework for 2005/06 and beyond.

Economic Policies for 2005/06 and the Medium Term

8. The recently adopted new PRS (MKUKUTA) spells out Tanzania's policy direction in the coming five years, which mainly focuses on the attainment of the MDGs. The MKUKUTA improves on the PRS, by building its strategy around clusters of outcomes, taking into account inter-sectoral linkages and synergies. The strategy puts more emphasis on growth for poverty reduction, through policy interventions in key areas. All sectors of the economy are expected to continue to experience strong growth, with real GDP growth reaching 6.9 percent during 2005. Growth is expected to be driven mainly by agriculture, which is the mainstay of the Tanzanian economy, supported by other important sectors, especially mining, tourism and infrastructure. Over the medium term, GDP growth is expected to reach 7.5 percent. To attain this objective, the government

will remain committed to the reform agenda, while implementing prudent fiscal, monetary and structural polices.

Fiscal Policy

9. The 2005/06 budget drew its guidance from the MKUKUTA, while focusing on the objective of maintaining macroeconomic stability. The strategic linkage between the budget and the MKUKUTA was facilitated by the newly developed Strategic Budget Allocation System (SBAS). The authorities continue to work towards ensuring that over time, as work on full costing of the MKUKUTA is attained, the government's Medium–Term Expenditure Framework will translate comprehensively the policy objectives into program targets and activities. As a step forward, the expenditure programs in the current budget are already driven by policy priorities within available and budgeted resources. The authorities continue to implement measures that will strengthen public administration systems and domestic resource mobilization.

10. The government envisages an increase in domestic revenue, to reach 14.3 percent of GDP during 2005/06. The increase will be driven by the full one year impact of the implementation of the new Income Tax Act, improved tax administration following tax reforms at the TRA, graduation of a number of tax exempted companies into the tax net and increased revenue from new gas related projects. The Tanzanian authorities fully recognize the need to strengthen internal revenue capabilities and finally reduce donor dependency. The government will therefore continue to strengthen tax administration, streamline customs procedures and improve expenditure management.

Monetary Policy

11. Monetary policy will continue to be directed towards maintaining appropriate level of liquidity in the economy to ensure that inflation remains low, while foreign reserves remain at sufficient level. In this connection, the Bank of Tanzania (BOT) will continue to sterilize liquidity arising from high donor inflows, through appropriate mix of Treasury bill sales and foreign exchange interventions. Moreover, the BOT will continue to improve its techniques for liquidity forecasting and maintain close policy collaboration with the government.

12. The financial sector, an important channel for monetary policy transmission, will also continue to be strengthened. The authorities will implement Tanzania's comprehensive second generation of the Financial Sector Reform Program (FSRP), which builds on the recommendations of the second FSAP. The program's aim is to optimize financial sector contribution to investment and growth. The authorities intend to amend the main banking laws, namely, the Bank of Tanzania Act and the Banking and Financial Institutions Act, to provide greater autonomy to the central bank while enhancing its transparency and accountability and strengthen bank suspension.

Structural Policies

13. The government will actively focus its policies towards enhancing good governance and improving the business environment. The Anti-Corruption Law is currently being reviewed by the government and is expected to be passed by Parliament by April 2006. The Law will grant greater operational autonomy to the Prevention of Corruption Bureau in investigating cases related to corruption, in line with Tanzania's obligations under the UN Convention Against Corruption, the African Union Convention on Preventing and Combating Corruption and the SADC Protocol Against Corruption.

14. In order to establish a well functioning, transparent and efficient business registration system, the government is preparing a Bill to be submitted to Parliament soon. Given the importance of the energy sector to the economy, the government is considering options for restructuring the electricity company, TANESCO with the objective of increasing its operational efficiency and reducing long term debt to sustainable level.

Conclusion

15. Tanzania has over the decade consistently implemented broad based policy reforms, which have resulted in sustained high level of growth. The authorities will continue to implement policies aimed at deepening these reforms. They recognize that over 80 percent of Tanzanians reside in rural areas, and their future livelihood hinges on transforming agriculture and improving rural infrastructure and therefore more efforts and resources need to be redirected to effectively correct these imbalances. It is for this reason that the new PRS (MKUKUTA) will put more emphasis on attaining sustainable growth levels necessary for improvement in social well-being of the majority of Tanzanians.