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United Republic of Tanzania: Second Review Under the Policy Support Instrument—Staff Report; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Tanzania

In the context of the second review under the Policy Support Instrument for Tanzania, the following documents have been released and are included in this package:

- the staff report for the Second Review Under the Policy Support Instrument, prepared by a staff team of the IMF, following discussions that ended on October 9, 2007, 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 December 7, 2007. 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 December 21, 2007 updating information on recent developments.

- a Press Release summarizing the views of the Executive Board as expressed during its December 21, 2007 discussion of the staff report that completed the review.

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

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

Poverty Reduction Strategy Paper—Annual Implementation Report—Joint Staff Advisory Note
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*

*Also included in Staff Report

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

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

UNITED REPUBLIC OF TANZANIA

Second Review Under the Policy Support Instrument

Prepared by the African and Policy Development and Review Departments
(In consultation with other departments)

Approved by David Nellor and Michael T. Hadjimichael

December 7, 2007

Discussions were held in Dar es Salaam on September 25-October 9, 2007. The staff team comprised Roger Nord (head), David Dunn, Yuri Sobolev (all AFR), Niko Hobdari (PDR), and Alejandro Hajdenberg (FAD). The mission met with the Minister of Finance, Mrs. Meghji, the Permanent Secretary of Finance, Mr. Mgonja, the First Deputy Governor of the Bank of Tanzania, Prof. Ndulu, other senior officials, and representatives of the private and international communities. Mr. Robinson, the Fund's senior resident representative in Dar es Salaam, and Mr. Masawe, senior advisor to the Executive Director, participated in the discussions.

Executive Summary

The staff recommends completion of the second review. All quantitative assessment criteria were met with the exception of the ceiling on reserve money, which was breached by a small margin. The Bank of Tanzania has since taken corrective action. The request for an electricity tariff increase (structural assessment criterion) was made with a three month delay. One of four structural benchmarks was implemented; the others are being implemented with delays.

Economic performance remains strong and the outlook is positive. Economic growth is on track to exceed 7 percent, government revenue is buoyant, and international reserves are ample. However, inflation has trended higher and remains above the Bank of Tanzania's target.

Significant portfolio inflows put pressure on liquidity management during mid-2007, but have since abated. Reserve money growth still exceeded program targets through September, despite large sterilization operations by the Bank of Tanzania, which put upward pressure on T-bill yields. The key to regaining monetary control is to reduce reliance on government securities sales for liquidity management in favor of more foreign exchange sales. The Bank of Tanzania has taken steps in this direction, allowing the exchange rate to appreciate modestly, and reserve money growth has moderated. T-bill yields have also begun to decline.

The 2007/08 budget targets ambitious increases in both revenue and expenditure. Revenue has performed strongly so far and foreign assistance has been ample and front-loaded. But to safeguard the domestic financing objective the authorities need to be ready to respond flexibly should revenue flag later in the year. Further strengthening public financial management is critical to ensure that public resources are used effectively, including in priority areas such as education and infrastructure.

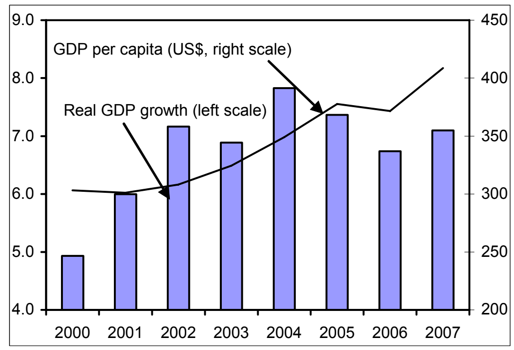
Swifter structural reforms could further boost economic growth. Private sector development requires the business environment to improve further. Second-generation financial sector reforms should be accelerated by reducing key legal bottlenecks, particularly related to landownership, and addressing the weak capacity of the judicial system. Prudential supervision needs to be geared toward overseeing a fast-growing and diversifying financial system. The first priority should be to strengthen the regulatory framework for nonbank financial institutions, especially pension funds, which are growing rapidly.

Sound governance and strong public accountability are key to sustained high growth. The welcome initiatives to strengthen governance need to be implemented decisively, including through an expeditious and thorough follow-up to the special audit of the EPA account at the BoT.

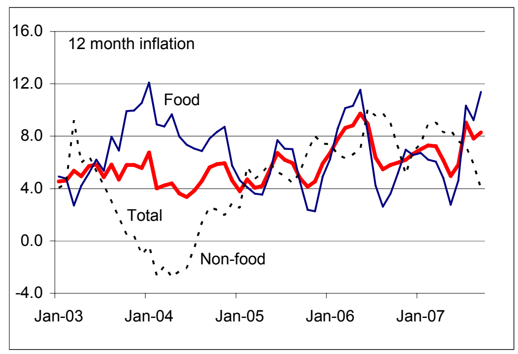
I. Growth Remains Strong, But Inflation Has Trended Higher

1. **Fueled by a rebound in agriculture and improved electricity supply, economic growth reached 6.7 percent in 2006/07 and is on track to exceed 7 percent in 2007/08.**[1] The mining, tourism, and manufacturing sectors continued to drive economic growth, supported by continued rapid credit expansion. Inflation, however, continued to trend slightly above the authorities' 5 percent target, reaching 6.3 percent in 2006/07. The overall fiscal deficit on a cash basis, after grants, fell to 5 percent of GDP in 2006/07, thanks mainly to a strong revenue performance.[2] A surge in imports, particularly capital goods and fuel, resulted in a widening of the external current account deficit. However, despite delays in the disbursement of foreign assistance, gross international reserves rose to US$2.3 billion (4.5 months of imports) as foreign direct investment and other capital inflows increased (Figures 1-3).

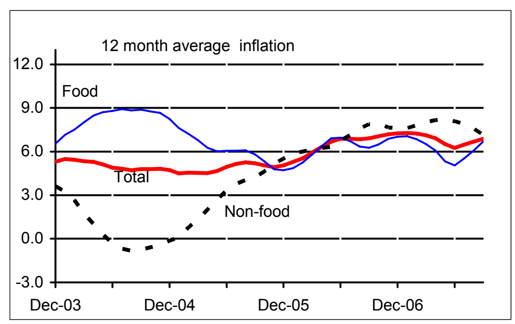
Tanzania has achieved high growth...



... with relatively low inflation.



But inflation has trended higher since 2005.



Sources: Tanzanian National Bureau of Statistics

2. **In mid-2007, significant portfolio capital inflows put pressure on liquidity management.** An estimated US$200–250 million of foreign capital entered Tanzania in April–July.[3] To sterilize the resulting excess liquidity, the BoT issued additional T-bills,

[1] The fiscal year is July-June. National accounts are compiled only on a calendar year basis; fiscal year GDP is estimated by interpolation. The National Bureau of Statistics intends to begin publishing quarterly GDP data soon, which will allow fiscal year GDP to be calculated more accurately.

[2] All ratios to GDP reflect the revised national accounts data, which were published in July 2007. The revised GDP series is based on SNA93; nominal levels are about 10 percent higher.

[3] The inflows were likely motivated by the high yields on government securities. However, because nonresidents are not allowed to hold government securities directly, the inflows increased nonresident (shilling) time deposits in commercial banks, which in turn invested in government securities. Since August, such inflows appear to have abated, but no significant outflows have been observed.

containing annual reserve money growth in 2006/07 to 29 percent, only slightly above target. However, yields on T-bills climbed to 18.1 percent in June from 12.5 percent in April[4].

3. **In the first quarter of 2007/08, fiscal performance was strong, but inflationary pressures intensified.** Government revenue remained on track to reach the program objective at year-end—an increase of 1.5 percentage points to 16 percent of GDP. Moreover, donor budget support was frontloaded, with about 80 percent being disbursed in the first quarter, which allowed government deposits in the BoT to build. The BoT, however, continued to face problems mopping up the excess liquidity created by both public and private inflows and reserve money remained above the program path in the first quarter. Inflation reached 8.3 percent in September (year-on-year), with price increases mainly stemming from higher transportation and distribution costs after the budget raised taxes on fuels and as the pass-through of prices of imported petroleum products continued.

4. **After continuing to depreciate in most of 2007, the exchange rate recently reversed course.** In the face of capital inflows, the Bank of Tanzania relied heavily on government securities to mop up liquidity and was a net buyer, rather than seller, of foreign exchange. As a result, the nominal exchange rate of the shilling did not appreciate, in contrast to currencies in nearby countries with similar capital inflows.[5] Starting in August, the Bank of Tanzania resumed net foreign exchange sales and reduced its reliance on government securities for liquidity management. The shilling in September-October appreciated by about 4.5 percent in nominal effective terms (Figure 4).

5. **The reform program supported by the PSI was broadly on track** (Text table)**.** All quantitative assessment criteria but one for end-June 2007 were met. The ceiling on reserve money was exceeded by a small margin (0.3 percent). Structural reforms advanced, though at a slower pace than envisaged. In particular, the request for an electricity tariff increase (structural assessment criterion) was submitted in October rather than in July 2007 as originally planned.[6]

6. **Given the relatively minor slippages against the targets and the corrective actions taken, staff recommends the approval of waivers for the nonobservance of the two assessment criteria and completion of the review**.

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[4] For background, see "Tanzania: High and Volatile Government Securities Yields in Country Report No. 07/246," Box 2.

[5] Staff analysis at the time suggested some scope for appreciation. - See Box 3 on competitiveness in Tanzania in Country Report No. 07/246 for more detail.

[6] Under its regulations, the independent regulator must rule on TANESCO's request for a 40 percent tariff within 84 days (by early 2008).

Tanzania: Summary Performance under the PSI[1]

Measure	Scheduled Date of Implementation	Status	Corrective Action
Quantitative Assessment Criteria			
• Ceiling on net domestic financing	June	Observed	
• Average reserve money target	June	Not observed	Increased foreign exchange sales to reduce reliance on government securities
• Floor on net international reserves	June	Observed	
• Non-accumulation of arrears	Continuous	Observed	
• Limit on nonconcessional borrowing	Continuous	Observed	
Structural Assessment Criteria and Benchmarks			
• Submit request for an aggregate electricity tariff increase based on full cost recovery.[2]	End-July 2007	Not Observed Submission of request for tariff increase was deemed compliant by the regulator in October 2007.	Decision by the regulator on tariff increase due by early January 2008.
• Unified legal and regulatory framework and investment guidelines for pension funds.	End-September 2007	Partly implemented Draft proposal prepared, but yet not submitted to Government.	Proposal must be harmonized with the proposal to amend the Social Security Act to be submitted to Government by end-February 2008.
• Cash Management Unit (CMU) in the Accountant General's Department and Cash Management Committee (CMC) to produce rolling cash flow forecast and liquidity management plan.	Continuous, beginning end- July 2007	Partly implemented CMU and CMC established, but 3-month cash flow projection and liquidity management plan delayed.	CMU will produce cash flow projections quarterly by end-March 2008; the CMC will meet frequently for liquidity management planning.
• Customs and Excise Department to develop a risk management strategy/plan.	End-September 2007	Implemented	
• Complete the special audit of the NBC-EPA debt in accordance with the agreed terms of reference.	End-October 2007	Implemented with delay Audit completed in late-November.	Authorities will make public the main findings of the special audit and will follow up as appropriate.

[1] For full detail see Tables 1 and 2 in Appendix I.
[2] Assessment Criterion.

II. POLICY DISCUSSIONS AND PROGRAM FOR THE REMAINDER OF 2007/08

7. **Discussions focused on three main challenges:** (i) regaining monetary control and returning inflation to the BoT's target path, (ii) containing fiscal risks as the 2007/08 budget is implemented and safeguarding the objective of zero net domestic financing; and (iii) accelerating structural reforms to raise the economy's growth potential.

Monetary and Exchange Rate Policies

8. **Strengthening monetary control is the key to reducing inflationary pressures and reining in high and volatile T-bill rates.** To that end, the BoT intends to follow a three-pronged strategy that would (MEFP ¶28-¶32)

- bolster its operations in the government securities markets. Key steps include better liquidity forecasting; more coordination between the BoT's policy-making and financial markets departments; and measures to increase competition in the T-bill auctions;
- rely more on sales of foreign exchange to systematically mop up liquidity, while allowing greater exchange rate flexibility; and
- expand BoT communications with markets, including by issuing policy statements after the Monetary Policy Committee meets each month and regularly publishing assessments of the Tanzanian economy.

9. **Since September 2007, the BoT has stepped up its foreign exchange sales and reduced its reliance on issuing government securities.** In a statement after the September meeting of the Monetary Policy Committee, the BoT reemphasized its primary objective of maintaining price stability. Since then, yields on government securities have retreated from very high levels and the nominal exchange rate has appreciated. The BoT also announced that it will move from weekly to fortnightly T-bill auctions by January 2008, a step aimed at encouraging secondary market activity and increasing competition in the primary auctions. Improved discipline by the BoT in sticking with preannounced volumes and maturity structures in the primary auction has already enhanced this competition and contributed to falling yields.

10. **Looking ahead, better liquidity forecasting will be key to improving monetary management.** In this regard, strengthening the forecasting ability of the Cash Management Committee, which convenes the Bank of Tanzania and the Ministry of Finance, will be critical. More accurate forecasts are a prerequisite for extending the period between T-bill auctions, as well as the BoT to shift from targeting monetary aggregates to targeting inflation in the medium term. The staff will work with the BoT to prepare the ground for such a shift.

11. **The BoT is committed to a flexible exchange rate policy, in the context of using foreign exchange sales as a primary tool for mopping up liquidity generated by donor-supported government spending.** In line with recommendations by Fund staff, the BoT is

taking steps to conduct its sales of foreign exchange for sterilization operations more systematically to minimize the impact on the interbank market. Other interventions would be limited only to maintaining an orderly market.[7]

Fiscal Policy

12. **Sound government financing will continue to anchor macroeconomic stability, even while public spending increases substantially to meet pressing social and infrastructural needs** (MEFP ¶22-¶27). To limit the impact on domestic demand, the government targets zero net domestic financing of the government budget.[8] The 2007/08 budget provides for a 34 percent increase in expenditure financed by more improvement in revenue performance (from 14.5 to 16.0 percent of GDP) and a sharp increase in donor support (from 9 to 12 percent of GDP) in 2007/08. The spending increase reflects priorities in the poverty reduction strategy (MKUKUTA) and is concentrated in development expenditure, especially infrastructure, education, and health. About half the revenue increase is likely to result from specific measures; the remainder would stem from further improvements in revenue administration, notably at the level of large taxpayers. While domestic revenue has performed well so far, risks remain; to safeguard the domestic financing objective, the authorities will prepare a prioritized expenditure plan for use should revenue fall short of expectations.

13. **Improvements in revenue administration and public financial management (PFM) would ensure effective use of public resources in support of economic growth.** To further enhance the performance of the Tanzania Revenue Authority, measures will extend the gains achieved through the large taxpayer department to medium-sized taxpayers, promote electronic tax filing, and improve customs processes. The government also plans to review tax expenditures, nontax revenue collection, and the fiscal regime in the mining sector with a view to further broaden the tax base over the medium term. Tanzania's PFM systems compare favorably with other African countries', but reforms have slowed (Box 1). Following a recent review, the PFM Reform Program, supported by a well-coordinated group of donors, is being updated and will focus on strategically allocating resources and ensuring value for money in budget execution. Priorities supported by the Fund through East AFRITAC are to improve cash management and expenditure tracking.

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[7] The 2007 Annual Report on Exchange Arrangements and Exchange Restrictions modified the classification of Tanzania's exchange rate policy to "managed floating with no predetermined path for the exchange rate" from "freely floating", beginning in April 2007.

[8] The program contains an adjustor, which allows for domestic financing up to the equivalent to US$150 million (just under 1 percent of GDP) should foreign budget assistance fall short of target (see the Technical Memorandum of Understanding, Appendix I).

14. **Looking ahead, Tanzania's hard-won fiscal stability is subject to several risks.** In particular, government guarantees, such as that provided for the recent syndicated loan by domestic financial institutions to TANESCO (T Sh 250 billion, equal to about 1 percent of GDP), and credit guarantee schemes, operated by the Bank of Tanzania on behalf of the government, could give rise to future liabilities. Moreover, the government is considering expanding the use of public public-private partnerships (PPPs) in the area of infrastructure. The staff stressed that in evaluating the use of PPPs, value for money must be a top criterion; a strong legal and regulatory framework and the ability to assess fiscal risks are also essential. A regular report on fiscal risks, prepared as part of the annual budget documentation, would be a useful tool.

Structural Reforms to Raise Potential Economic Growth

15. **Private sector development and continued productivity growth are the keys to further accelerating economic growth.** Foreign direct investment has averaged over 4 percent of GDP in recent years, and foreign investor interest in Tanzania is rising. But despite improvements, the business environment still compares unfavorably to many fast-growing economies in Africa and elsewhere (Box 2). The government is implementing a wide range of reforms to strengthen the business environment (MEFP ¶15-¶16). The PSI-supported program focuses on reforms in three areas: the energy sector; the financial sector, and governance and public accountability. The government is also taking steps to improve transportation infrastructure, which is one of the key binding constraints on private sector development.

16. **A sizable tariff increase is needed to restore the financial viability of TANESCO, the state-owned electricity company** (MEFP ¶17-¶18). As part of its financial recovery plan, a proposal to increase the tariff 40 percent is pending with EWURA, the independent regulator. Moreover, the government is pursuing broader reforms in the power sector so that energy is produced and distributed more efficiently and reliably. In particular, it is discussing a new Electricity Act that would promote competition and attract greater private investment to the sector.

17. **Second-generation financial sector reforms aim at further improving access to financial services and strengthening prudential supervision** (MEFP ¶33). Bottlenecks in the legal framework, particularly for landownership, and the weak capacity of the judicial system are being addressed, which would facilitate collateralized lending. Commercial bank balance sheets remain sound (Table 6). But prudential supervision needs to be geared increasingly toward overseeing a fast-growing and diversifying financial system. More also needs to be done to introduce risk-based supervision of commercial banks. A near-term priority is to strengthen the regulatory framework for nonbank financial institutions, especially pension funds, which are growing rapidly. The authorities are preparing a unified legal and regulatory framework for the financial supervision of pension funds, including investment guidelines, as part of the forthcoming proposal to amend the Social Security Act.

18. **Improving public accountability would improve the use of public resources and create a more enabling business environment.** The strengthening of the Prevention and Combating of Corruption Bureau, the creation of the Public Procurement Regulatory Authority, and the publication of procurement audit reports of 20 procuring entities are important steps toward building greater government accountability.[9] As Tanzania further exploits its natural resources, it will be important to ensure strong governance in the sector; transparency, including subscribing to international standards such as the Extractive Industries Transparency Initiative, would advance this goal.

19. **To address allegations of improprieties in the operation of the EPA account managed by the Bank of Tanzania, the government has launched a special audit, conducted by an international auditor** (MEFP ¶35). The audit report was completed in late November and submitted to the authorities. Once finalized, which is expected by end-December, the authorities intend to publish the main findings of the report and are committed to implementing the appropriate remedial measures. The staff will discuss these measures with the authorities in the context of the third review, which is expected to take place in the firsty quarter of 2008.

III. PSI PROGRAM MONITORING FOR 2007/08

20. **The PSI-supported program will be monitored through the quantitative and structural assessment criteria, indicative targets, and benchmarks specified in Tables 1 and 3 of Appendix I.** The third and fourth reviews will be based on quantitative assessment criteria for the end-December 2007 and end-June 2008 test dates, respectively, including proposed modifications to assessment criteria. That is, the floor on net international reserves would be revised upwards to reflect the strong overperformance in 2006/07; and the ceiling on average reserve money would be raised by a small amount to reflect a minor adjustment in the forecast for the final quarter of the fiscal year. Quantitative indicative targets were also set for end-March 2008. Conditionality in key areas of the structural reform agenda includes progress in revenue mobilization, public financial management, and financial sector reform.

IV. STAFF APPRAISAL AND RISKS

21. **Tanzania's economic performance continues to be strong and its growth prospects are good.** But there is scope for even higher growth as Tanzania taps into the opportunities of global integration. This will require attracting more investment, particularly foreign direct investment, which in turn will require strengthening public infrastructure as well as institutions and governance.

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[9] The improvement in procurement practices was reflected in the latest PEFA assessment, which rates Tanzania "B," two grades higher than in the previous year.

22. **In the near term, policies will need to address two main risks.** First, average inflation is running above the BoT's target, and underlying inflation is rising. Monetary policy needs to be active rather than reactive to keep inflation at modest levels. Second, the ambitious revenue and expenditure targets for 2007/08 pose potential risks for budget implementation. Careful planning would need to ensure that spending can be adjusted if domestic revenue falls short.

23. **Swifter structural reforms could further boost economic growth.** Private sector development requires the business environment to improve further. Second-generation financial sector reforms should be accelerated by reducing key legal bottlenecks, particularly related to landownership, and addressing the weak capacity of the judicial system. Prudential supervision needs to be geared toward overseeing a fast-growing and diversifying financial system. The first priority should be to strengthen the regulatory framework for nonbank financial institutions, especially pension funds, which are growing rapidly.

24. **Strengthening governance and public accountability are critical to ensure that public resources are used more effectively and create an environment conducive to private sector development.** Momentum on public financial management reforms needs to be regained. In particular, cash management needs to be strengthened and the development of a functional classification of expenditure to improve expenditure tracking needs to be accelerated. More broadly, the welcome efforts to strengthen governance need to be implemented decisively, including through an expeditious and thorough follow-up to the special audit of the EPA account at the BoT.

25. **The authorities' economic program faces some risks.** The government budget remains dependent on donor budget support. Steps to ensure more predictable longer-term aid, such as enhanced donor coordination under the Joint Assistance Strategy for Tanzania, have facilitated budget execution, but the authorities need to be able to respond flexibly if domestic revenue or donor support falls short. The Multilateral Debt Relief Initiative has lowered Tanzania's debt burden and created more fiscal space. However, there is a need for vigilance, notably with regard to government guarantees and other contingent liabilities, to ensure value for money and sound public finances in the long run. An insufficient tariff increase for TANESCO would not only pose some fiscal risks, but could also discourage private investment in the electricity sector.

26. **Staff recommends the completion of the second review of Tanzania's program under the PSI.** Based on the relatively minor slippages and the corrective actions taken, staff recommends the approval of waivers for the nonobservance of two assessment criteria: the end-June 2007 ceiling on average reserve money and TANESCO's submission of an application for increased electricity tariffs by end-July 2007.

Box 1. Tanzania: Public Financial Management Reforms

Public financial management (PFM) reforms in Tanzania are articulated in the PFM reform program (PFMRP). The second stage of the PFMRP, launched in 2004 and still under way, is organized around the 10 major components of PFM. The PFMRP also provides a framework to coordinate the activities of the development partners supporting PFM reforms in Tanzania, including the Fund and the World Bank. The PFMRP is currently under revision with the objective of raising its effectiveness, notably by strengthening its links with other PFM instruments.

Thanks to sustained reforms, Tanzania has one of the most solid PFM systems in sub-Saharan Africa. In particular, the budget preparation, process has been strengthened through enhanced macroeconomic programming, development of a medium-term expenditure framework (MTEF), and increased orientation of the budget toward government priorities. In budget execution, strengths include an advanced information financial management system (IFMS) and the establishment of a treasury single account. Substantial progress has also been made toward channeling external aid through the budget, strengthening donor coordination, and developing a public procurement system. Finally, the framework for public scrutiny has been strengthened through regular and timely audits that are published after parliament discusses them.

Significant scope for reform remains. Priorities should include further improving budget preparation, particularly by allowing more time for strategic planning; strengthening alignment of MKUKUTA, the MTEF, and the budget; and integrating the Strategic Budget Allocation System and IFMS. Other enhancements would be to improve budget execution through enhanced cash management; strengthen fiscal monitoring by implementing a functional classification of expenditures; report regularly on MKUKUTA spending, contingent liabilities, quasi-fiscal activities, and government assets; extend reporting to the general government; and further reinforce internal and external auditing. However, there is limited staff capacity at the mid- and lower levels within the Ministry of Finance, line ministries, and local governments.

Box 2. Tanzania: Foreign Investment and the Business Environment

Foreign investors have been increasingly interested not just in Tanzania's traditional mining sector but in areas such as tourism, agriculture, and manufacturing. More investment could provide a basis for stronger growth and employment creation in the years ahead. However, actual foreign direct investment inflows, while growing steadily, have fallen short of registered interest, partly because it is difficult to do business in Tanzania.

Tanzania: Foreign Direct Investment, US$ million

	2002	2003	2004	2005	2006
Total Registered Projects	**1072**	**1590**	**1133**	**1706**	**5877**
Agriculture	50	146	72	466	533
Mining and natural resources	55	64	29	16	176
Tourism	90	121	141	227	683
Manufacturing	204	228	390	462	1243
Transport and infrastructure	25	834	214	138	1254
Construction	590	56	203	195	1248
Other	58	141	86	200	741
Total FDI inflows	**411**	**473**	**485**	**506**	**597**

Source: Tanzania Investment Center and Bank of Tanzania

Despite improving in recent years, Tanzania's business environment still compares poorly to that in other countries, including fellow East African Community (EAC) members Kenya and Uganda. Tanzania ranks 130 out of 178 economies in the World Bank's *Doing Business 2008* report.

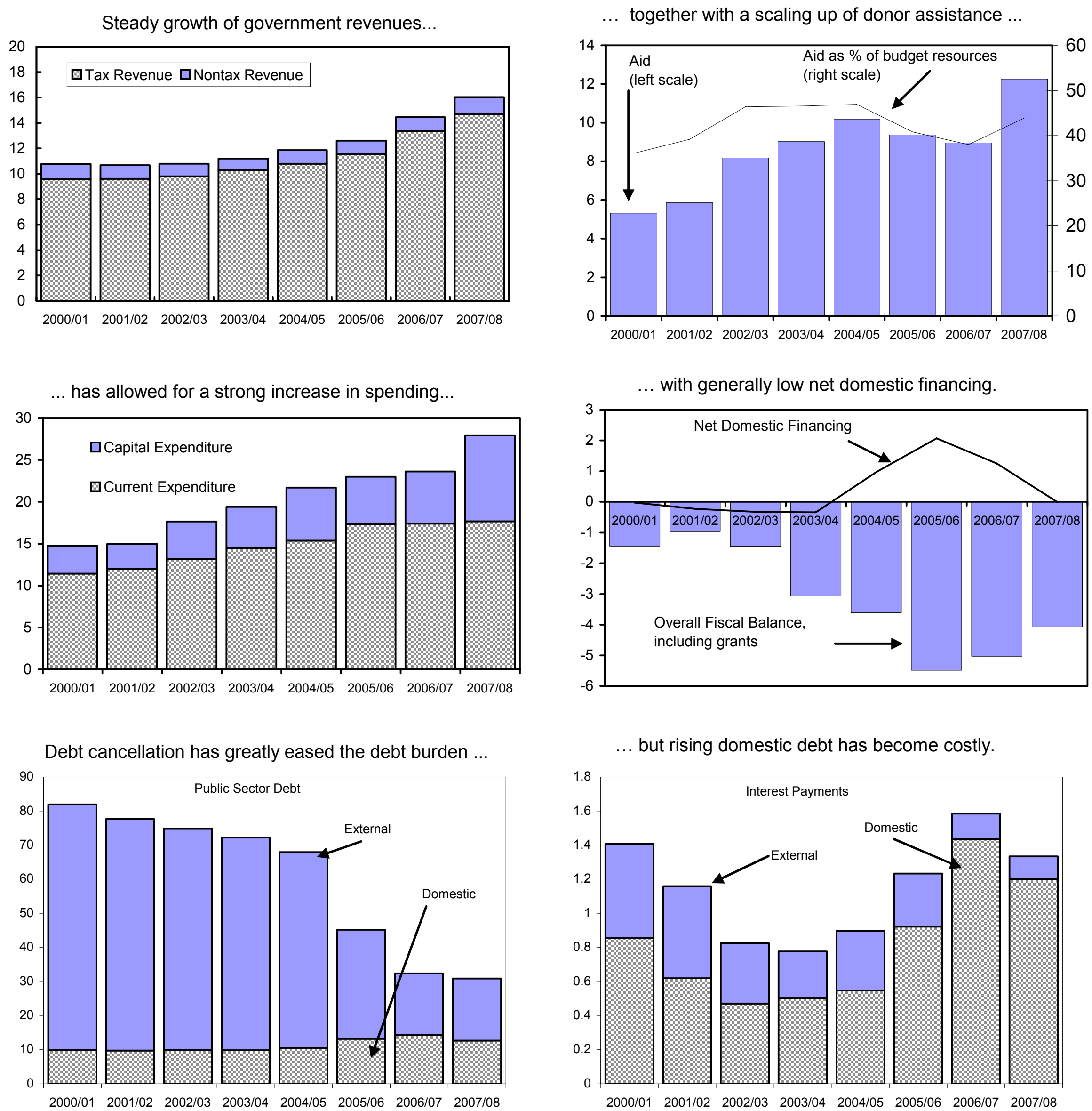
Tanzania: Ease of Doing Buisness Rank in Comparison to Selected Sub-Saharan African Economies, 2007

Mauritius	South Africa	Botswana	Kenya	Ghana	Zambia	Uganda	**Tanzania**	SSA mean	SSA median
27	35	51	72	87	116	118	**130**	133	150

Source: World Bank (www.doingbusiness.org)

Key impediments to investment in Tanzania are lack of both adequate physical infrastructure and skilled labor at vocational and managerial levels, issues that can be addressed only over time. Other barriers, however, could be readily addressed. While business registration procedures have been streamlined, a plethora of regulatory and licensing bodies finance themselves through the fees they impose on businesses (effectively serving as nuisance taxes). Implementation of the Land Laws, while ongoing, is slow, especially in rural areas, and foreclosure of land collateral on default remains difficult. The commercial dispute resolution system has been improved with the creation of commercial courts, but the judiciary is understaffed and ill-equipped, and contract enforcement decisions often stall in the general court of appeals. Within the EAC, nontariff policies and procedural impediments to trade have not been fully eliminated and continue to discourage business and trade in the region. Barriers include lack of (i) harmonized investment codes and rules of origin; (ii) joint customs border posts and uniform cargo clearance procedures; and (iii) standardized regulations, metrology, and product quality standards. Restrictions on labor mobility and unresolved double-taxation issues also stand in the way of much business activity.

Figure 1. Tanzania: Fiscal Developments, 2000/01-2007/08 *
(Percent of GDP, unless otherwise stated)

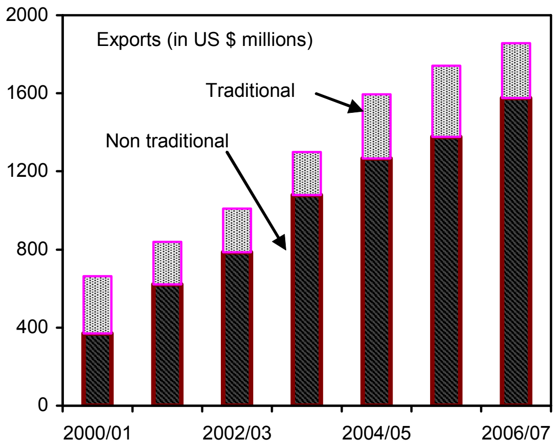


Source: Tanzanian authorities; Fund staff estimates/projections.

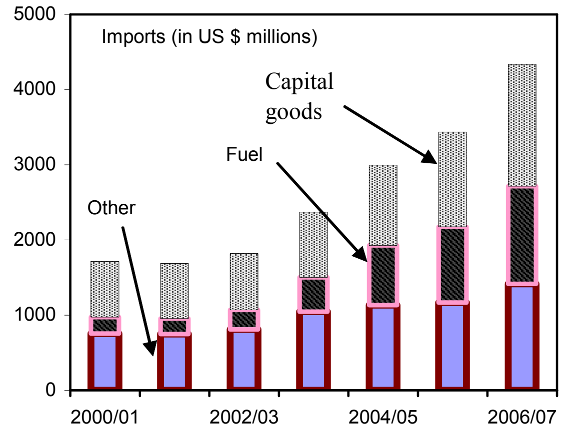
* Figures for 2007/08 are program projections.

Figure 2. Tanzania: External Sector Developments

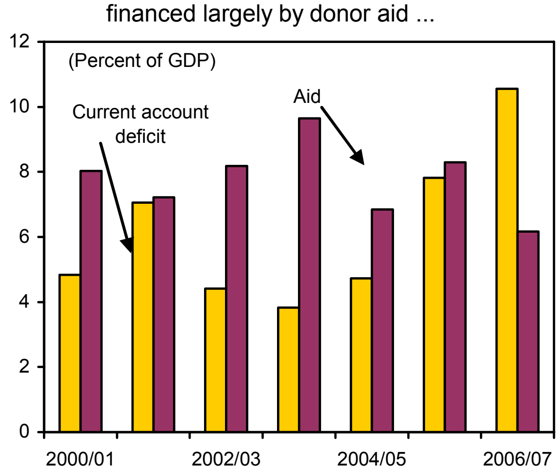
Exports have risen sharply in recent years ...



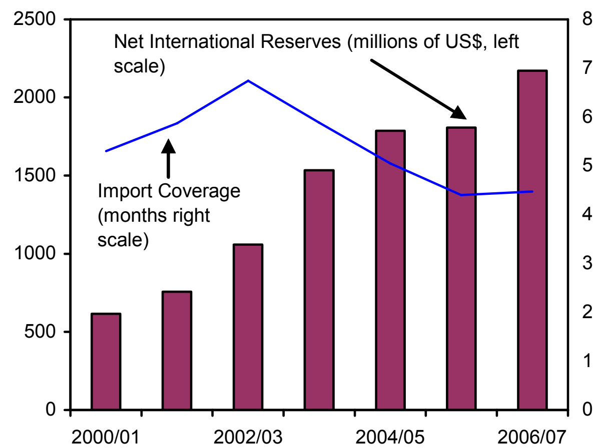
... but imports have risen even faster, driven by higher fuel costs and investment ...



... and despite a rising current account deficit financed largely by donor aid ...



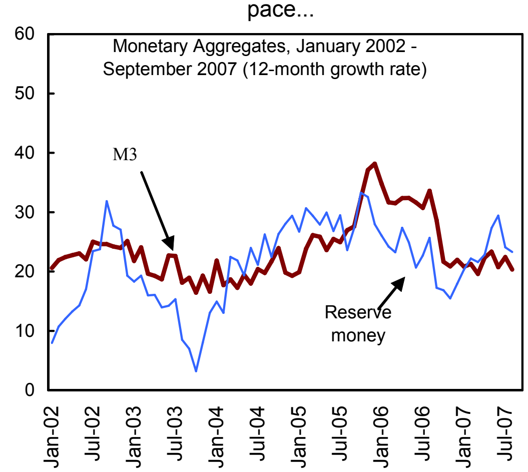
… reserves have remained ample.



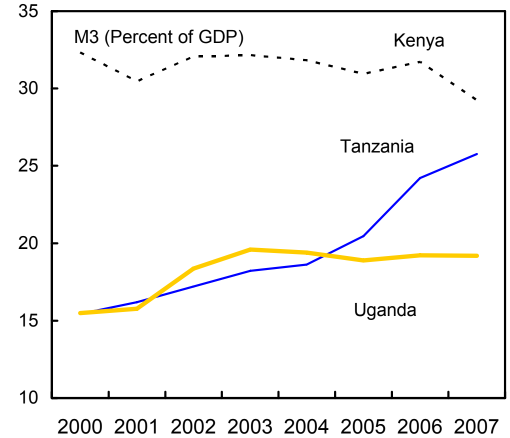
Source: Tanzania authorities; Fund staff estimates.

Figure 3. Tanzania: Monetary and Financial Developments

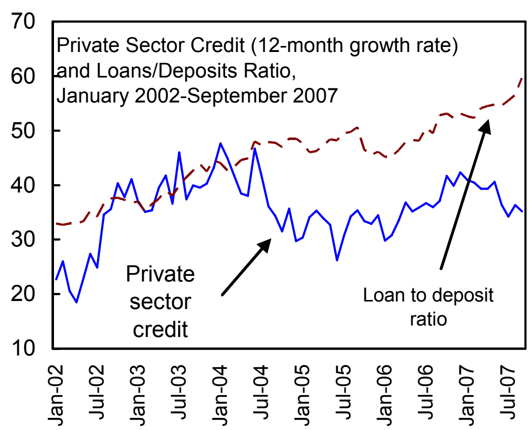
Monetary aggregates have grown at a rapid pace...



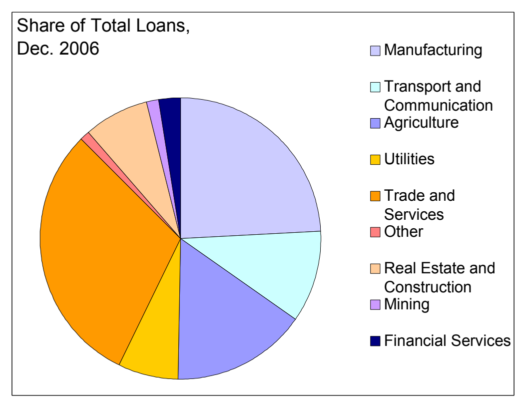
... reflecting accelerated financial deepening.



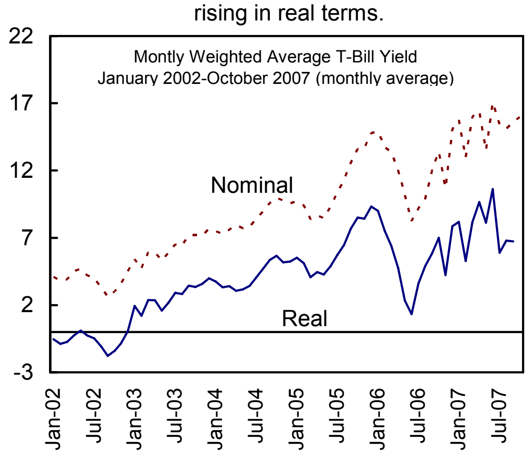
Lending is also expanding rapidly...



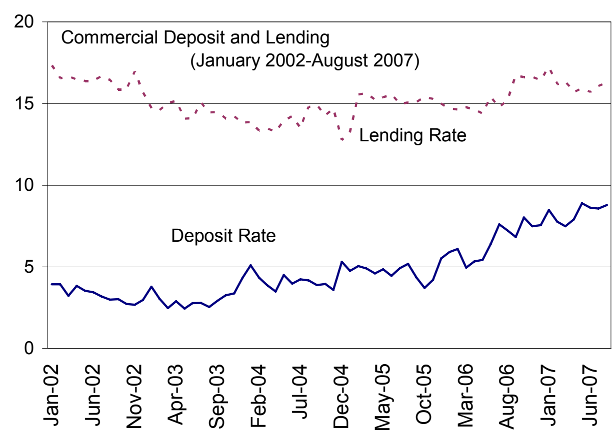
…mostly to productive sectors.



Interest rates have been volatile and rising in real terms.

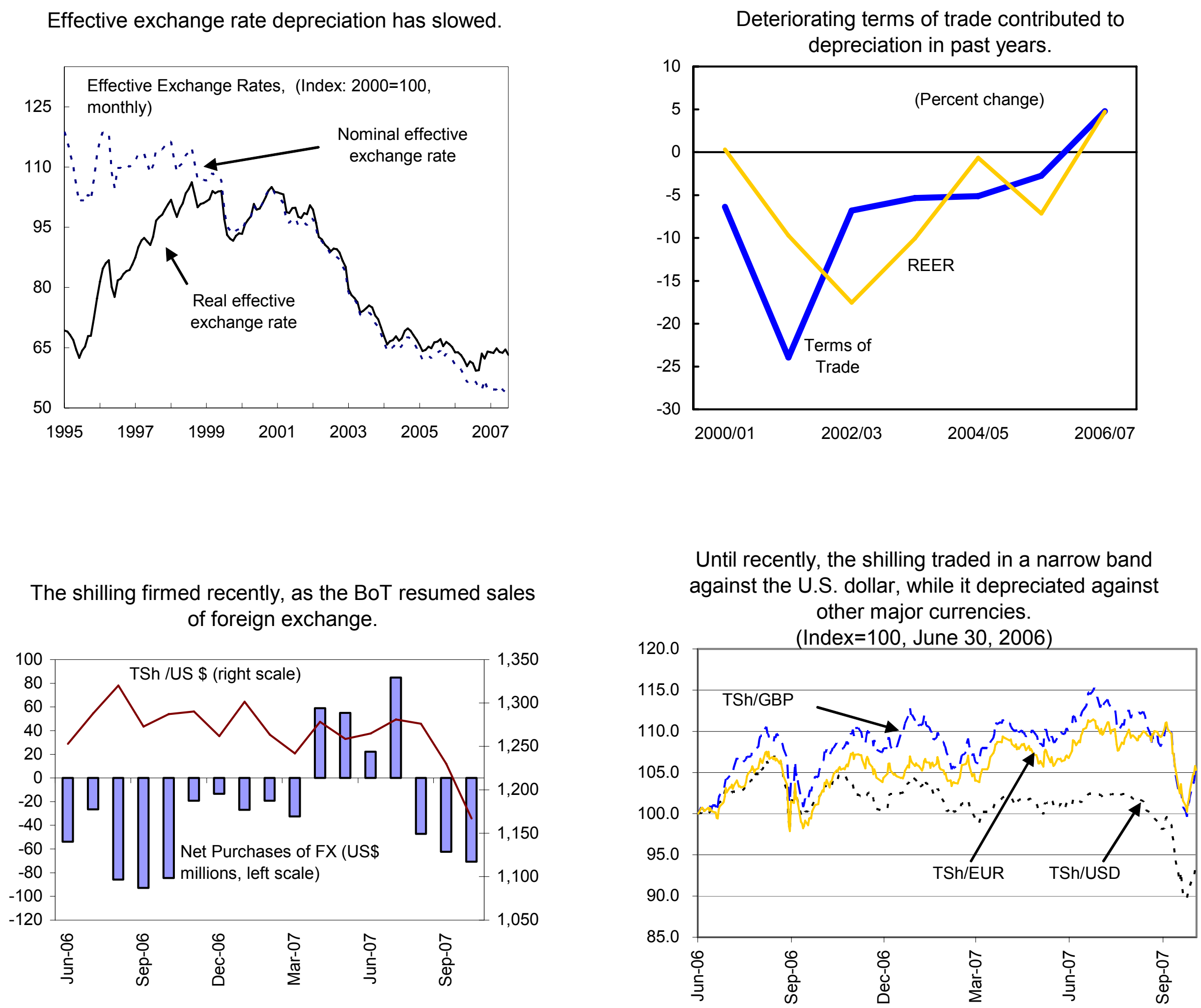


Commercial bank deposit rates have increased while the spread with lending rates has narrowed.



Source: Bank of Tanzania

Figure 4. Tanzania: Exchange Rate Developments



Source: Tanzania authorities; Fund staff estimates.

Table 1. Tanzania: Selected Economic and Financial Indicators, 2005/06-2010/11

	2005/06	2006/07		2007/08		2008/09	2009/10	2010/11
	Est.	Prog.	Prel.	Prog.	Proj.	Proj.	Proj.	Proj.
	(Annual percentage change, unless otherwise indicated)							
National income and prices								
Real GDP growth (calendar year, at market prices)[1]	7.4	6.2	6.7	7.1	7.1	7.5	7.9	8.0
Real GDP growth (fiscal year, at market prices)	7.0	6.7	6.9	7.3	7.3	7.7	8.0	8.0
Consumer prices (period average)	5.6	6.2	6.3	5.0	6.9	5.2	5.2	5.0
Consumer prices (end of period)	6.8	5.0	5.8	5.0	6.0	5.0	5.0	5.0
External sector								
Export, f.o.b (in U.S. dollars)	1,741	1,965	1,856	2,131	2,145	2,340	2,562	2,807
Imports, c.i.f. (in U.S. dollars)	-3,776	-4,368	-4,764	-5,131	-5,509	-6,079	-6,671	-7,386
Export volume	2.5	6.7	-7.1	15.0	19.6	7.1	7.4	7.6
Import volume	3.4	9.4	20.4	15.1	9.4	12.8	12.1	12.2
Terms of trade	-2.7	-8.7	4.8	1.7	-6.8	4.1	4.1	3.3
Nominal effective exchange rate (end of period; depreciation -)	-10.3	...	-4.9	...	...	...	...	...
Real effective exchange rate (end of period; depreciation -)	-7.2	...	4.8	...	...	...	...	...
Money and credit								
Broad money (M3)	31.6	24.2	20.7	21.0	21.0	…	…	…
Net foreign assets	38.5	4.8	10.6	5.4	-3.7	…	…	…
Net domestic assets	14.2	83.5	51.7	53.7	76.1	…	…	…
Credit to nongovernment sector	35.9	36.0	36.4	39.5	34.5	…	…	…
Velocity of money (GDP/M3; average)[2]	4.7	3.9	4.0	3.7	3.7	…	…	…
Treasury bill interest rate (in percent; end of period)[3]	9.3	…	16.0	…	…	…	…	…
	(Percent of GDP)[2]							
Public finance								
Revenue (excluding grants)	12.6	13.3	14.5	14.5	16.0	16.3	16.6	16.8
Total grants	5.4	7.4	5.0	7.3	7.8	7.2	6.5	6.7
Expenditure (including adjustment to cash)	23.5	25.5	24.5	25.5	27.9	27.6	27.1	27.4
Overall balance (including grants)	-5.5	-4.8	-5.0	-3.8	-4.1	-4.1	-4.0	-3.9
Domestic financing	2.1	0.4	1.3	0.0	0.0	0.0	0.0	0.0
Savings and investment[1]								
Resource gap	-8.9	-11.7	-13.9	-13.2	-14.5	-14.9	-14.7	-14.4
Investment	25.1	21.0	27.9	22.4	29.1	29.4	29.7	29.9
Government	6.0	6.8	6.0	8.0	8.4	10.2	10.0	10.1
Nongovernment[4]	19.1	14.2	21.9	14.4	20.7	19.2	19.7	19.8
Gross domestic savings	16.2	9.4	14.0	9.1	14.6	14.5	15.0	15.5
External sector								
Current account balance (excluding current transfers)	-11.3	-13.3	-14.0	-13.1	-13.7	-13.5	-13.2	-13.0
Current account balance (including current transfers)	-7.8	-9.5	-10.6	-9.7	-10.0	-9.8	-9.6	-9.5
	(Millions of U.S. dollars, unless otherwise indicated)							
Balance of payments								
Current account balance (excluding current transfers; deficit -)	-1,641	-2,022	-2,104	-2,299	-2,405	-2,666	-2,906	-3,156
Overall balance of payments (deficit -)	383	26	288	-69	43	111	189	242
Gross official reserves	1,995	2,025	2,285	1,975	2,349	2,460	2,650	2,890
In months of imports of goods and nonfactor services	4.2	4.0	4.2	3.5	3.9	3.7	3.6	3.6

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

[1] Data are on calendar year basis. For example, 2005/06 data are for calendar year 2005.
[2] Program figures for 2006/07 and 2007/08 have been adjusted to reflect the revised GDP data, which were released in September 2007. Actual and projected national accounts figures further reflect the new methodology used (SNA 1993).
[3] Weighted-average yield of 35-, 91-, 182-, and 364-day treasury bills during the month of June.
[4] Including change in stocks.

Table 2. Tanzania: National Accounts, 2006-11[1]

	2006	2006 Rev.	2007 Prog.	2007 Rev. proj.	2008 Prog.	2008 Proj.	2009 Proj.	2010 Proj.	2011 Proj.
	(Annual percentage change in real terms)								
GDP at market prices									
Nominal (billions of T Sh, calendar-year basis)	16,016	17,750	18,096	20,146	20,448	22,785	25,792	29,171	32,964
Real (percentage change)	6.2	6.7	7.1	7.1	7.5	7.5	7.9	8.0	8.0
Deflator (percentage change)	6.5	4.2	5.8	6.4	5.5	5.6	5.3	5.1	5.0
Sectoral components of GDP									
Agriculture	4.1	3.9	4.7	5.0	5.2	5.2	5.2	5.2	5.2
Industry	9.6	8.5	9.3	9.2	9.8	11.2	11.6	11.6	11.6
Services	7.2	7.7	8.5	6.7	8.4	7.3	7.8	7.9	7.9
Memorandum items:	2005/06	2005/06 Rev.	2006/07 Prog.	2006/07 Rev. proj.	2007/08 Prog.	2007/08 Proj.	2008/09 Proj.	2009/10 Proj.	2010/11 Proj.
Nominal GDP (billions of T sh, fiscal-year basis)	15,113	16,857	17,056	18,948	19,272	21,465	24,289	27,482	31,067
Nominal GDP growth	13.7	12.6	12.9	12.4	13.0	13.3	13.2	13.1	13.0
Real GDP growth	6.5	7.0	6.7	6.9	7.3	7.3	7.7	8.0	8.0
CPI inflation (average)	5.6	5.6	6.2	6.3	5.0	6.9	5.2	5.0	5.0
CPI inflation (end period)	6.8	6.8	5.0	5.8	5.0	6.0	5.0	5.0	5.0

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

Table 3. Tanzania: Central Government Operations, 2005/06-2010/11[1]
(Billions of Tanzania Shillings)

	2005/06	2006/07		2007/08			2008/09	2009/10	2010/11
	Actual	Prog.	Est.	Prog.	Budget	Rev. Proj.	Proj.	Proj.	Proj.
Total revenue	2,125	2,511	2,739	3,103	3,503	3,438	3,963	4,567	5,225
Tax revenue	1,946	2,321	2,529	2,866	3,188	3,154	3,636	4,190	4,794
Import duties	191	221	246	286	309	291	336	387	442
Value-added tax[2]	803	956	832	967	969	969	1,117	1,288	1,473
Excises[2]	262	333	520	580	657	653	753	868	993
Income taxes	554	643	714	780	827	827	953	1,098	1,257
Other taxes	137	168	219	253	427	414	477	550	629
Nontax revenue	178	191	210	237	314	284	327	377	431
Total expenditure	3,873	4,825	4,475	5,477	5,998	5,998	6,709	7,452	8,455
Recurrent expenditure	2,920	3,349	3,296	3,729	3,797	3,797	4,284	4,732	5,330
Wages and salaries	657	1,004	976	1,113	1,113	1,113	1,280	1,449	1,638
Interest payments	219	144	216	276	276	304	307	289	292
Domestic	164	122	185	240	240	274	270	247	247
Foreign[3]	55	22	31	36	36	30	37	42	44
Goods and services and transfers	2,044	2,201	2,105	2,340	2,408	2,380	2,696	2,994	3,401
of which: MDRI (IMF) related	0	53	18	0	0	7	0	0	0
Development expenditure	953	1,476	1,179	1,749	2,201	2,201	2,425	2,719	3,172
Domestically financed	296	667	504	710	1,012	1,012	1,096	1,215	1,471
of which: MDRI (IMF) related	0	230	105	204	206	206	81	0	0
Foreign financed	657	810	675	1,039	1,189	1,188	1,330	1,505	1,701
Overall balance before grants	-1,748	-2,314	-1,736	-2,375	-2,495	-2,558	-2,746	-2,885	-3,230
Grants	911	1,406	953	1,566	1,691	1,685	1,754	1,790	2,073
Program (including basket grants)[4]	507	708	591	768	800	795	899	986	1,083
Project	328	413	242	595	684	684	774	876	991
HIPC grant relief	76	2	0	0	0	0	0	0	0
MDRI (IMF) grant relief	0	283	123	204	206	206	81	0	0
Overall balance after grants	-837	-908	-783	-808	-805	-873	-991	-1,095	-1,157
Adjustment to cash[5]	-87	0	-171	0	0	0	0	0	0
Overall balance (cash basis)	-924	-908	-954	-808	-805	-873	-991	-1,095	-1,157
Financing	924	908	954	808	805	873	991	1,095	1,204
Foreign (net)	561	852	717	832	819	887	991	1,095	1,204
Foreign loans	669	882	746	896	858	946	1,056	1,168	1,286
Program (including basket loans)[4]	340	485	313	452	354	442	501	539	576
Project	329	397	433	444	504	504	555	628	710
Amortization	-108	-29	-30	-65	-40	-59	-65	-73	-82
Domestic (net)	349	67	237	0	-14	0	0	0	0
Bank financing	127	20	25	...	...	...	...	...	...
Nonbank financing	222	47	212	...	...	...	...	...	...
Amortization of parastatal debt	-19	-11	0	-23	-29	-29	0	0	0
Privatization proceeds	33	0	0	0	15	15	0	0	0
Financing Gap	0	0	0	0	0	0	0	0	0
Memorandum items:									
Treasury vouchers	24	36	36	31	...	31	31	0	0
Public domestic debt (in percent of GDP)	13.9	14.9	13.6	12	...	12.3	10.9	9.6	9.6
Ratio of recurrent expenditures to total revenues (percent)	137	133	120	120	...	110	108	104	102
Nominal GDP[6]	16,857	18,948	18,948	21,465	21,465	21,465	24,289	27,482	31,067

Table 3. Tanzania: Central Government Operations, 2005/06-2010/11[1] (concluded)
(Percent of GDP)

	2005/06	2006/07		2007/08			2008/09	2009/10	2010/11
	Actual	Prog.	Prel.	Prog.	Budget	Rev. Proj.	Proj.	Proj.	Proj.
Total revenue	12.6	13.3	14.5	14.5	16.3	16.0	16.3	16.6	16.8
Tax revenue	11.5	12.2	13.3	13.4	14.9	14.7	15.0	15.2	15.4
Import duties	1.1	1.2	1.3	1.3	1.4	1.4	1.4	1.4	1.4
Value-added tax[2]	4.8	5.0	4.4	4.5	4.5	4.5	4.6	4.7	4.7
Excises[2]	1.6	1.8	2.7	2.7	3.1	3.0	3.1	3.2	3.2
Income taxes	3.3	3.4	3.8	3.6	3.9	3.9	3.9	4.0	4.0
Other taxes	0.8	0.9	1.2	1.2	2.0	1.9	2.0	2.0	2.0
Nontax revenue	1.1	1.0	1.1	1.1	1.5	1.3	1.3	1.4	1.4
Total expenditure	23.0	25.5	23.6	25.5	27.9	27.9	27.6	27.1	27.2
Recurrent expenditure	17.3	17.7	17.4	17.4	17.7	17.7	17.6	17.2	17.2
Wages and salaries	3.9	5.3	5.2	5.2	5.2	5.2	5.3	5.3	5.3
Interest payments	1.3	0.8	1.1	1.3	1.3	1.4	1.3	1.1	0.9
Domestic	1.0	0.6	1.0	1.1	1.1	1.3	1.1	0.9	0.8
Foreign[3]	0.3	0.1	0.2	0.2	0.2	0.1	0.2	0.2	0.1
Goods and services and transfers	12.1	11.6	11.1	10.9	11.2	11.1	11.1	10.9	10.9
o/w MDRI (IMF) related	0.0	0.3	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Development expenditure	5.7	7.8	6.2	8.1	10.3	10.3	10.0	9.9	10.2
Domestically financed	1.8	3.5	2.7	3.3	4.7	4.7	4.5	4.4	4.7
o/w MDRI (IMF) related	0.0	1.2	0.6	0.9	1.0	1.0	0.3	0.0	0.0
Foreign financed	3.9	4.3	3.6	4.8	5.5	5.5	5.5	5.5	5.5
Overall balance before grants	-10.4	-12.2	-9.2	-11.1	-11.6	-11.9	-11.3	-10.5	-10.4
Grants	5.4	7.4	5.0	7.3	7.9	7.8	7.2	6.5	6.7
Program (including basket grants)[4]	3.0	3.7	3.1	3.6	3.7	3.7	3.7	3.6	3.5
Project	1.9	2.2	1.3	2.8	3.2	3.2	3.2	3.2	3.2
HIPC grant relief	0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
MDRI (IMF) grant relief	0.0	1.5	0.7	0.9	1.0	1.0	0.3	0.0	0.0
Overall balance after grants	-5.0	-4.8	-4.1	-3.8	-3.7	-4.1	-4.1	-4.0	-3.7
Adjustment to cash[5]	-0.5	0.0	-0.9	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (cash basis)	-5.5	-4.8	-5.0	-3.8	-3.7	-4.1	-4.1	-4.0	-3.7
Financing	5.5	4.8	5.0	3.8	3.7	4.1	4.1	4.0	3.9
Foreign (net)	3.3	4.5	3.8	3.9	3.8	4.1	4.1	4.0	3.9
Foreign loans	4.0	4.7	3.9	4.2	4.0	4.4	4.3	4.2	4.1
Program (including basket loans)[3]	2.0	2.6	1.7	2.1	1.6	2.1	2.1	2.0	1.9
Project	2.0	2.1	2.3	2.1	2.3	2.3	2.3	2.3	2.3
Amortization	-0.6	-0.2	-0.2	-0.3	-0.2	-0.3	-0.3	-0.3	-0.3
Domestic (net)	2.1	0.4	1.3	0.0	-0.1	0.0	0.0	0.0	0.0
Bank financing	0.8	0.1	0.1	...	...	...	...	...	...
Nonbank financing	1.3	0.2	1.1	...	...	...	...	...	...
Amortization of parastatal debt	-0.1	-0.1	0.0	-0.1	-0.1	-0.1	0.0	0.0	0.0
Privatization proceeds	0.2	0.0	0.0	0.0	0.1	0.1	0.0	0.0	0.0

Sources: Ministry of Finance; Bank of Tanzania; and Fund staff projections.

[1] Fiscal year: July-June.

[2] After program projections were finalized, the VAT on fuel products was abolished and excise tax rates on those products were i

[3] Some projected external debt obligations are under negotiation for relief with a number of creditors.

[4] Basket funds are sector-specific accounts established by the government to channel donor support to fund-specific activities.

[5] Unidentified financing (+)/expenditure (-). Includes expenditure carryover from the previous year.

[6] The nominal GDP series was revised upwards by about 10% in 2007. All ratios to GDP have been revised accordingly.

Table 4. Tanzania: Summary Accounts of the Bank of Tanzania, 2007/08
(Billions of Tanzania Shillings, unless otherwise indicated; end of period)

	2007						2008			
	Jun		Sept		Dec		Mar		Jun	
	Prog.	Prel.	Prog.	Prel.	Prog.	Proj.	Prog.	Proj.	Prog.	Proj.
Net foreign assets	2,505	2,747	2,644	3,418	2,684	3,123	2,524	2,933	2,431	2,716
Net international reserves	2,540	2,782	2,679	3,453	2,718	3,158	2,558	2,967	2,465	2,751
(Millions of U.S. dollars)	1,954	2,194	2,081	2,807	2,099	2,567	1,965	2,412	1,883	2,236
Medium- and long-term foreign liabilities	-35	-35	-35	-35	-35	-35	-35	-35	-35	-35
Net domestic assets	-832	-1,149	-859	-1,733	-759	-1,198	-558	-967	-405	-691
Credit to government	-961	-1,136	-1,082	-1,898	-1,041	-1,700	-899	-1,475	-807	-1,152
Of *which:* excluding liquidity paper	-200	-85	-487	-707	-557	-524	-348	-294	-258	-100
Other items (net)	129	-13	223	165	282	502	341	508	402	461
Of *which:* MDRI (IMF)	-149	-289	-152	-213	-102	-167	-51	-121	0	-74
Of *which:* REPOs	-35	-15	-35	-117	-35	-10	-35	-70	-35	-100
Reserve money	1,674	1,598	1,785	1,685	1,925	1,925	1,966	1,966	2,025	2,025
Currency outside banks	1,148	1,049	1,204	1,174	1,294	1,245	1,210	1,164	1,320	1,270
Bank reserves	526	549	580	511	631	680	756	802	706	755
Currency in banks	103	131	106	130	109	130	112	130	115	130
Deposits	423	418	474	381	522	550	644	672	591	625
Required reserves (calculated)1	368	348	380	363	398	406	426	427	440	436
Excess reserves (calculated)	55	69	94	17	124	144	218	245	151	189
Memorandum items:										
Stock of liquidity paper	761	1,052	595	1,191	484	1,176	551	1,181	550	1,052
Average reserve money	1,664	1,685	1,775	1,836	1,915	1,915	1,956	1,956	2,013	2,022

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, 2007/08
(Billions of Tanzania Shillings, unless otherwise indicated; end of period)

	2007						2008			
	Jun		Sep		Dec		Mar		June	
	Prog.	Prel.	Prog.	Proj.	Prog.	Proj.	Prog.	Proj.	Prog.	Proj.
Net foreign assets	3,398	3,585	3,769	4,033	3,867	3,707	3,749	3,548	3,710	3,454
Bank of Tanzania	2,505	2,747	2,644	3,418	2,684	3,123	2,524	2,933	2,431	2,716
Commercial banks	893	837	1,125	615	1,183	584	1,226	615	1,279	738
Net domestic assets	1,941	1,605	1,767	1,678	1,953	2,248	2,280	2,535	2,584	2,826
Domestic credit	2,388	2,400	2,292	2,131	2,449	2,399	2,746	2,710	3,020	3,078
Credit to government (net)	134	140	-254	-483	-404	-335	-265	-150	-105	39
Credit to nongovernment sector	2,254	2,260	2,546	2,614	2,853	2,734	3,011	2,860	3,125	3,039
Other items (net)	-447	-795	-525	-453	-496	-151	-466	-175	-436	-252
M3	5,339	5,190	5,537	5,711	5,820	5,955	6,029	6,083	6,294	6,280
Foreign currency deposits	1,651	1,652	1,823	1,720	1,916	1,794	1,985	1,832	2,073	1,891
M2	3,688	3,538	3,713	3,991	3,903	4,162	4,044	4,251	4,222	4,388
Currency in circulation	1,148	1,049	1,204	1,159	1,294	1,245	1,210	1,164	1,320	1,270
Deposits (Tanzania Sh)	2,540	2,489	2,509	2,832	2,609	2,917	2,834	3,087	2,902	3,119
Memorandum items:										
M3 growth (12-month percent change)	24.2	20.7	21.7	25.5	21.3	24.1	22.8	23.7	21.0	21.0
Foreign currency deposits (12-month percent change)	22.0	22.0	21.6	14.7	19.4	11.7	22.8	13.2	21.0	14.5
M2 growth (12-month percent change)	25.2	20.1	21.7	30.8	22.2	30.3	22.8	29.0	21.0	24.0
Credit to nongovernment sector (12-month percent change)	36.0	36.4	33.6	37.1	40.7	34.8	41.1	34.0	39.5	34.5
Reserve money (12-month percent change)	29.1	23.3	26.4	19.4	33.3	33.3	33.1	33.1	21.0	26.7
Average reserve money (12-month percent change)	27.8	29.4	24.2	28.5	23.0	23.0	23.3	23.3	21.0	20.0
Currency/M3 (in percent)	21.5	20.2	21.8	20.3	22.2	20.9	20.1	19.1	21.0	20.2
Reserve money multiplier (M3/reserves)	3.2	3.1	3.1	3.1	3.0	3.1	3.1	3.1	3.1	3.1
Velocity of money (M3; end-period)	3.2	3.9	3.3	3.5	3.1	3.4	3.4	3.7	3.2	3.6
Nonbank financing of the government (net) [1]	47	212	10	40	50	80	85	90	100	100
Bank financing of the government (net) [1]	20	25	-240	-638	-350	-474	-175	-289	-100	-100
Bank and nonbank financing of the government (net) [1]	67	237	-230	-598	-300	-394	-90	-199	0	0

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

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

Table 6: Financial Soundness Indicators, 2002–06
(Percent, end of calendar year)

	2002	2003	2004	2005	2006
Access to bank lending					
Claims on the private sector to GDP [1]	6.1	7.7	8.6	10.0	12.4
Capital adequacy					
Capital to risk-weighted assets	20.6	21.0	21.2	22.0	16.3
Capital to assets	8.6	9.9	10.2	10.0	7.6
Asset composition and quality					
Total loans and advances to total assets	25.4	30.2	33.7	33.7	37.3
Sectoral distribution of loans					
Trade	22.1	23.8	23.6	23.7	18.9
Mining and manufacturing	24.4	27.3	23.4	22.5	22.6
Agricultural production	12.9	14.1	13.9	12.4	12.6
Building and construction	3.6	5.5	4.0	5.8	4.0
Transport	11.8	10.3	8.7	7.6	9.3
Foreign exchange loans	28.1	27.2	28.9	32.7	33.6
Gross nonperforming loans (NPLs) to gross loans [2]	8.3	4.5	3.5	4.9	7.3
Large exposures to total capital	58.2	59.3	64.1	53.3	27.3
Earnings and profitability					
Return on assets	1.8	2.1	2.9	3.3	3.9
Return on equity	20.6	20.7	28.4	33.1	37.0
Interest margin to gross income	48.0	51.5	54.8	60.9	74.9
Noninterest expenses to gross income	70.1	67.1	61.6	56.9	43.8
Personnel expenses to noninterest expenses	41.3	39.9	39.0	39.6	39.5
Trading and fee income to total income	45.2	42.3	39.1	33.6	28.9
Interest rate earned on loans and advances	15.7	13.8	14.8	15.0	16.4
Interest rate paid on deposits	3.4	3.9	4.4	5.3	7.2
Spread (lending vs. deposit rates) [3]	12.3	10.0	10.4	9.7	9.2
Liquidity					
Liquid assets to total assets	58.0	56.3	53.6	55.0	48.2
Liquid assets to total short term liabilities	68.9	62.8	62.0	62.4	55.2
Total loans to customer deposits	34.0	41.2	44.4	42.4	50.1
Foreign exchange liabilities to total liabilities	34.1	36.5	34.7	34.9	38.6

Sources: Bank of Tanzania and Fund staff estimates.

[1] Calendar year; end of period claims relative to annual GDP.
[2] The increase in nonperforming loans to gross loans between 2005 and 2006 was due largely to a change in reporting standards.
[3] Difference between lending rate and time deposit rate.

Table 7. Tanzania: Balance of Payments, 2005/06-2010/11

(Millions of U.S. dollars, unless otherwise indicated)

	2005/06	2006/07		2007/08		2008/09	2009/10	2010/11
	Act.	Prog.	Prel. Est	Prog.	Proj.	Proj.	Proj.	Proj.
Current account	-1,110	-1,410	-1,561	-1,680	-1,729	-1,908	-2,092	-2,282
Trade balance	-1,695	-2,012	-2,294	-2,541	-2,656	-2,960	-3,255	-3,636
Exports, f.o.b.	1,741	1,965	2,042	2,131	2,360	2,574	2,818	2,807
Of which: Traditional	364	400	281	360	407	425	445	465
Imports, f.o.b	-3,436	-3,977	-4,336	-4,672	-5,016	-5,534	-6,073	-6,724
Services (net)	135	88	241	278	274	335	393	526
Income (net)	-81	-98	-51	-36	-22	-42	-45	-48
Of which : interest payments due	-51	-34	-22	-43	-36	-42	-41	-40
Of which : interest on public debt	-49	-17	-21	-28	-25	-30	-31	-31
Of which : interest on central government debt [1]	-49	-17	-21	-28	-25	-30	0	0
Current transfers (net)	531	612	543	619	675	759	815	875
Of which : official transfers	502	555	509	593	641	724	778	838
Of which : program grants	435	553	496	593	641	724	778	838
HIPC relief	67	2	13	0	0	0	0	0
Capital account	662	4,998	4,889	492	602	675	744	820
Of which : project grants	281	323	219	442	552	623	692	766
Debt stock reduction under MDRI (including HIPC)	336	4,626	4,621	0	0	0	0	0
Of which: HIPC	37	1,157	1,157	0	0	0	1	2
Financial account	900	-3,561	-3,050	1,119	1,170	1,344	1,537	1,704
MDRI (including HIPC)	0	-4,626	-4,621	0	0	0	0	0
Of which: HIPC	0	-1,157	-1,157	0	0	0	0	0
Direct investment	541	520	653	650	700	775	860	955
Other investment	357	542	915	465	467	566	674	746
Of which: Program loans	293	379	254	349	357	403	426	445
Project loans	278	313	310	343	406	447	496	550
Government-scheduled amortization [1]	-87	-23	-21	-50	-48	-52	-57	-63
Errors and omissions	-69	0	10	0	0	0	0	0
Overall balance	383	26	288	-69	43	111	189	242
Financing	-383	-26	-288	69	-43	-111	-189	-242
Change in BoT reserve assets (increase, -)	-26	-30	-292	69	-43	-111	-189	-241
Use of Fund credit	-357	4	4	0	0	0	0	-1
Memorandum items:								
Gross official reserves (BoT)	1,995	2,025	2,285	1,975	2,349	2,460	2,650	2,890
Months of imports of goods and services (next year)	4.2	4.0	4.2	3.5	3.9	3.7	3.6	3.6
Current account deficit (percent of GDP)								
Excluding official current transfers	-11.3	-13.3	-14.0	-13.1	-13.7	-13.5	-13.2	-13.0
Including official current transfers	-7.8	-9.5	-10.6	-9.7	-10.0	-9.8	-9.6	-9.5
External debt service foregone due to MDRI (including HIPC)	33.3	171.8	173.0	117.1	118.2	172.5	166.9	165.6
IMF	33.3	72	72.6	12.4	12.7	63.5	48.4	35.1
IDA	0	95	95.1	99.2	100.0	103.3	111.4	121.8
AfDB	0	5	5.3	5.5	5.5	5.7	7.1	8.8
Foreign program and project assistance (percent of GDP)	9.5	10.6	8.7	10.0	11.3	11.2	11.0	10.8
Foreign direct investment (percent of GDP)	3.8	3.5	4.4	3.8	4.0	4.0	4.0	4.0
Nominal GDP	14,251	14,797	14,797	17,305	17,305	19,551	21,688	24,037

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

[1] Relief on some projected external debt obligations is being negotiated with a number of creditors.

[2] Arrears are on non-Paris Club official and commercial debt subject to rescheduling.

Table 8. Tanzania: Program Assistance, 2006/07-2007/08[1, 2]
(Millions of U.S. dollars)

	2006/07					2007/08				
	Q1 Act.	Q2 Act.	Q3 Act.	Q4 Act.	Year Prel. Act.	Q1 Prel. Act.	Q2 Proj.	Q3 Proj.	Q4 Proj.	Year Proj.
Grants	**259.7**	**178.2**	**38.4**	**6.3**	**482.6**	**429.8**	**54.8**	**34.9**	**121.1**	**640.5**
Multilateral	**0.0**	**39.2**	**0.0**	**0.0**	**39.2**	**0.0**	**37.8**	**0.0**	**13.0**	**50.7**
EU PRBS grants[3]	0.0	39.2	0.0	0.0	39.2	0.0	37.8	0.0	13.0	50.7
World Bank (PRBS)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Bilateral	**259.7**	**139.0**	**38.4**	**6.3**	**443.4**	**429.8**	**17.0**	**34.9**	**108.1**	**589.8**
PRBS 3	**230.7**	**102.5**	**0.0**	**0.0**	**333.2**	**409.1**	**0.0**	**5.0**	**37.0**	**451.1**
Canada	0.0	0.0	0.0	0.0	0.0	17.2	0.0	0.0	0.0	17.2
Denmark	0.0	15.2	0.0	0.0	15.2	12.8	0.0	0.0	0.0	12.8
Finland	11.1	0.0	0.0	0.0	11.1	0.0	0.0	0.0	14.4	14.4
Germany	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	10.9	10.9
Ireland	13.2	0.0	0.0	0.0	13.2	16.0	0.0	0.0	0.0	16.0
Japan	4.7	0.0	0.0	0.0	4.7	4.5	0.0	0.0	0.0	4.5
Netherlands	0.0	38.1	0.0	0.0	38.1	51.3	0.0	5.0	11.7	68.0
Norway	27.2	6.7	0.0	0.0	33.9	39.6	0.0	0.0	0.0	39.6
Sweden	0.0	42.5	0.0	0.0	42.5	51.2	0.0	0.0	0.0	51.2
Switzerland	4.6	0.0	0.0	0.0	4.6	4.8	0.0	0.0	0.0	4.8
United Kingdom	169.9	0.0	0.0	0.0	169.9	211.7	0.0	0.0	0.0	211.7
Sectoral baskets	**29.0**	**36.5**	**38.4**	**6.3**	**110.2**	**20.7**	**17.0**	**29.9**	**71.1**	**138.7**
Belgium	0.0	0.0	5.8	0.0	5.8	0.0	0.0	5.5	1.3	6.8
Canada	0.0	0.0	0.3	0.0	0.3	0.6	0.0	0.0	0.0	0.6
Denmark	11.2	1.7	1.8	0.3	15.0	1.8	1.6	1.7	15.9	20.9
EU	0.0	5.3	19.4	0.0	24.7	0.0	2.0	7.2	5.8	15.0
France	0.0	0.0	0.0	1.3	1.3	0.0	0.0	0.0	1.2	1.2
Finland	1.3	0.0	0.0	0.0	1.3	0.0	0.0	0.0	9.5	9.5
Germany	2.6	8.9	0.0	4.7	16.2	0.0	0.0	0.0	12.9	12.9
Ireland	7.4	4.1	0.0	0.0	11.5	12.5	3.0	0.0	1.9	17.4
Italy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Japan	0.0	2.1	0.0	0.0	2.1	0.5	0.0	0.0	0.0	0.5
Netherlands	2.5	0.8	5.8	0.0	9.1	0.0	1.9	13.4	18.9	34.1
Norway	0.0	1.6	0.0	0.0	1.6	0.0	1.0	0.0	3.2	4.2
Sweden	0.0	1.4	0.0	0.0	1.4	0.0	3.7	0.0	0.0	3.7
Switzerland	2.9	1.7	0.4	0.0	5.0	4.5	0.9	0.4	0.0	5.8
United Kingdom	0.5	8.9	4.9	0.0	14.3	0.0	3.0	1.7	0.2	4.9
Others	0.6	0.0	0.0	0.0	0.6	0.8	0.0	0.0	0.3	1.1
Loans	**215.0**	**0.0**	**8.1**	**31.2**	**254.3**	**338.5**	**0.0**	**17.3**	**0.9**	**356.7**
Multilateral	**215.0**	**0.0**	**8.1**	**31.2**	**254.3**	**330.8**	**0.0**	**8.1**	**0.9**	**339.8**
World Bank	215.0	0.0	8.1	31.2	254.3	255.1	0.0	8.1	0.9	264.1
PRBS loans	206.4	0.0	0.0	17.3	223.7	195.2	0.0	0.0	0.0	195.2
Basket Loans	8.6	0.0	8.1	13.9	30.6	59.9	0.0	8.1	0.9	68.9
African Development Bank	0.0	0.0	0.0	0.0	0.0	75.7	0.0	0.0	0.0	75.7
Bilateral	0.0	0.0	0.0	0.0	0.0	7.7	0.0	9.2	0.0	16.9
Total program assistance	**474.7**	**178.2**	**46.5**	**37.5**	**736.9**	**768.3**	**54.8**	**52.2**	**122.0**	**997.2**
Cumulative from beginning of fiscal year	474.7	652.9	699.4	736.9	736.9	768.3	823.1	875.2	997.2	997.2

Sources: Tanzanian authorities; and donors.

[1] Fiscal year: July-June.

[2] For 2006/07 based on projected disbursements, and for 2007/08 based on currently identified aid commitments.

[3] Poverty reduction budget support.

APPENDIX—LETTER OF INTENT

December 7, 2007

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. Strauss-Kahn:

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, progress during the last quarter of 2006/07 in the implementation of the economic and financial programme that we are implementing with support from the Fund through its Policy Support Instrument (PSI), and policies that the Government intends to pursue in the reminder of 2007/08. We also recently had an opportunity to consult with the staff of the IMF on the progress of the programme.

2. The programme remains broadly on track, with all end-June 2007 quantitative performance criteria observed, except for the ceiling on reserve money, which was exceeded by a narrow margin. However, the growth of both extended broad money (M3) and broad money (M2) were contained within targeted levels. The deviation in reserve money was on account of a strong supply of foreign exchange in the market by commercial banks, which frustrated efforts by the Bank of Tanzania to sell foreign exchange as programmed. Since late September 2007, the Bank of Tanzania has increased its foreign exchange sales and reduced its reliance on Government securities for liquidity management. On this basis, we are confident that reserve money growth will be returned to its original target path.

3. Implementation of core reforms continues to yield satisfactory results, especially the public service reforms and in the tax and customs policy and administration areas. The Government is accelerating implementation of the second generation of financial sector reforms, and will continue to undertake improvement of the business environment to promote investment as the prerequisites for accelerated and sustainable growth in a stable macroeconomic environment. In line with MKUKUTA objectives, we intend to maintain the policies towards broad based growth as the sustainable basis of poverty reduction through, among other things, investment in productive infrastructure, and protecting the gains made in the provision of social services.

4. In the context of the PSI framework, we will regularly update the IMF on developments in the economic and financial policies, and provide the data needed for the monitoring of the programme. The Government will also consult regularly with the Fund on any relevant developments at the initiative of the Government, or the Fund.

5. The Government of Tanzania intends to make this letter and the attached MEFP, together with Fund staff reports related to this review under the PSI, available to the public and hereby authorises the IMF to publish the same on its website once the review is completed by the Executive Board.

Yours sincerely,

/s/
Zakia Hamdani Meghji (MP)
MINISTER FOR FINANCE
UNITED REPUBLIC OF TANZANIA

Attachment: Memorandum of Economic and Financial Policies.

APPENDIX—ATTACHMENT I

Tanzania: Memorandum of Economic and Financial Policies

I. RECENT MACROECONOMIC DEVELOPMENTS AND PROGRESS UNDER THE PROGRAMME

Introduction

1. During the year to June 2007, Tanzania continued to record good overall macroeconomic performance, benefiting from sustained economic reforms over the last ten years. The second half of the year witnessed a recovery from a slow down in the expansion of economic activity that was recorded in 2006 in the wake of the drought in late 2005 and the high oil prices in the world markets. Particularly strong performance was recorded in the trade and tourism, manufacturing, mining, construction, and communication sectors.

2. In 2006/07, the economy experienced some inflationary pressures emanating mainly from rising prices of fuel and food. The pressure continued in early months of 2007/08, whereby headline inflation rose from 5.9 percent in June 2007 to 9.0 percent in July, 2007 before declining to 7.8 percent in August 2007. The sharp increase of inflation in July 2007 was mainly driven by food inflation which increased from 4.6 percent recorded in the year ended June 2007, to 10.3 percent in the year ended July 2007. Due to reasons such as increased cross border trade in food, a hike in transport costs and high inflation expectations following increases in fuel pump prices in the country, prices of food items this year did not decline as expected between June and July. The increase in food prices is therefore considered to be transitory. As such, inflation is expected to decline further in the coming months following improvements in food supply, and the impact of the recent fuel tax, increase dissipates.

Fiscal policy and public resource management

3. The Government's fiscal programme for 2006/07 (July–June) was implemented successfully, with outcomes in line with programme targets. Despite the energy crisis, domestic revenue exceeded programme estimates by 1.2 percent of GDP and expenditure was contained within programme estimates. [1] Despite a 1.5 percent of GDP shortfall in programme foreign loans and grants, the actual domestic financing of 1.3 percent of GDP was well within programme limits. Domestic revenue collections benefited from better than expected performance of import duties, VAT on local sales, and corporation tax. Excise duties on imports were the main item with a lower than projected performance. Our domestic resource mobilisation

[1] In what follows, ratios to GDP are expressed in terms of the revised GDP series issued by the NBS in September 2007. The revised series is about 10 percent higher in level terms.

effort continues to benefit from robust economic performance and recent policy and administration reforms, including integration of the Tanzania Revenue Authority (TRA) operations and increased use of technology. The overall balance after grants declined by ½ a percentage point of GDP compared with 2005/06.

4. The tax and customs administration reforms progressed well on the basis of TRA's Second Corporate Plan which focuses on improvements in both revenue collection and taxpayer service. Institution-wide reforms in TRA are geared towards certification by the International Standards Organization (ISO), following ISO certification of the Large Taxpayers' Department during 2006/07. The Customs Department programme to roll out ASYCUDA^{++} reached 12 stations by June, 2007 and is expected to be operational at 6 more stations by March, 2008, thus covering largely all import shipments. The integration of ASYCUDA^{++} with the destination inspection system is proceeding smoothly and the integrated processes will be operational in March 2008 as planned, facilitating electronic transfer of data from TISCAN's Classification and Valuation Report (CVR) database to Customs and *vice versa*. We target to have 40% of all non-motor vehicle shipments processed through the Green Channel, 40% through the Yellow (scanner) Channel, and 20% through the Red Channel (physical verification). Customs has developed a risk management strategy and, as part of the next steps, TRA will procure an appropriate software for implementing a National IMPORT Commodity Database (NICD).

5. Despite the drought, increasing international oil prices, and increasing domestic interest payments, Government expenditure was below the programme forecast, closing at 23.6 percent of the GDP for the year mostly due to under-execution of development spending. Foreign financing of the budget was 8.8 percent of the GDP, below the programme target of 12.1 percent. The Government protected essential expenditure for priority social services linked to the achievement of the MDGs, and implemented internal reallocations to respond to critical emerging needs because of the drought and high domestic interest payments. Domestic financing of the budget was 1.3 of GDP, within the adjusted programme target.

6. The Government's focus on promoting transparency and accountability in the management of public resources was sustained. The Government has prepared responses to the observations of the Controller and Auditor General in the 2005/06 audit report, including critical actions to address the issues raised in the NAO report. The Government has also established Audit Committees in all MDAs for effective and sustainable enforcement of financial regulations. It is expected that most of the NAO observations in the 2005/06 report will be adequately addressed at both the central and local Governments' levels following implementation of these measures. Preparation of three-month rolling cash flow plans has been delayed due to technical difficulties in line Ministries, which are being addressed.

7. The now fully staffed and operational Public Procurement Regulatory Authority (PPRA) and the Public Procurement Appeals Authority (PPAA) stepped up implementation of their

mandates during the year, including capacity building for all public institutions and the civil society. The PPRA has issued guidelines for preparation and evaluation of bids; standard bidding documents, and regularly publishes results from its procurement audits in line with its mandate under the Public Procurement Act, 2004. In the context of PFM reforms, strengthening of the procurement oversight institutions, along with the accounting and audit function, continues to receive high priority. Following procurement audits on 20 public procurement entities[2], the PPRA is refining its capacity building programme to address the observed capacity gaps.

Monetary policy

8. Monetary policy implementation during the quarter ending June 2007 was complicated by sizeable inflows of foreign capital in the context of shallow financial markets and high domestic interest rates. In contrast to the programme target of USD 60 million of net sales, the BoT purchased USD 120 million. This called for sales of liquidity papers to the tune of TShs. 320.4 billion compared to the program target of TShs. 29 billion, which contributed to upward pressures on domestic interest rates. Furthermore, there was an apparent shortage of shilling liquidity in commercial banks as reflected by their low participation in the Treasury bills and repo markets particularly in June 2007, and by the higher inter-bank cash market rates. Despite these challenges, the average reserve money closed at TShs. 1,685.2 billion in June 2007, missing the target by only a narrow margin of TShs. 5.2 billion.

9. Broader monetary aggregates moved in line with the monetary policy stance taken by the Bank. Extended broad money supply (M3) grew annually at 20.7 percent compared with 31.6 percent recorded in June 2006, while broad money supply (M2) grew by 20.1 percent compared with 24.5 percent. During the year, both M3 and M2 grew below their respective targets of 24.0 percent and 23.0 percent. Despite the tight monetary policy stance, the Bank facilitated the provision of adequate financial resources to the productive sectors. The annual rate of expansion of credit to the private sector remained strong and in line with the program, reaching 36.4 percent at end June 2007, up from 35.9 percent at end June 2006.

10. During the first quarter of 2007/08, the implementation of monetary policy was further challenged by strong liquidity pressures emanating mainly from donor inflows that came in July 2007 instead of June, and the huge expenditure float from the previous year – all of which were above the respective quarter projections. As a result, the indicative target for average reserve money was missed by a sizeable margin in September.

11. The Joint Cash Management Committee (CMC), with representatives from the Ministry of Finance and the BoT, that was established to develop and supervise implementation of a

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[2] The results of the audits were also published in the local press and on PPRA's website

strategy for improved liquidity management started its assignment in August 2007. The CMC's strategy includes (i) developing a three month rolling Government cash flow forecast; (ii) reducing the level of the expenditure float to the minimum; and (iii) eliminating the large Government deposits in the commercial banks. The Government is also re-assessing its roll over policy in relation to the stock of domestic debt, with a view to reducing the tender size and the frequency of auctions. It is envisaged that, together with the measures planned in the monetary programme, these actions will facilitate a reduction in domestic interest rates.

Financial sector reforms

12. The Government is implementing the second generation financial sector reforms in the context of its Financial Sector Reform Implementation Action Plan (FSIAP). During 2006/07, five consultancy assignments were initiated within the framework of the Second Generation Financial Sector Reforms (SGFSR). These relate to finance leasing, pension sector, mortgage finance, credit information data bank and legal and regulatory framework for credit information bureau. In the area of Lease Finance, a draft finance leasing law has been developed with the assistance of the International Finance Corporation (IFC) and was presented to Parliament in November, 2007. In the area of Pension Sector Reform, a draft legal and regulatory framework for the Pension Sector has been developed and was discussed by stakeholders at a workshop held in Dar es Salaam and the Inter-Institutional Committee on Financial Sector Reform (IIC) in July 2007. Investment Guidelines for pension funds have also been developed with technical assistance from the World Bank. However, the unified legal and regulatory framework and investment guidelines for pension funds were not submitted to Government by end-September 2007 as envisaged pending their harmonization with the amendment to the Social Security Act current under preparation (see para 32). With regard to Mortgage Finance, a draft bill for amending various laws has been developed along with a draft Unit Titles Act.

External sector developments

13. The external sector performance has been positive, although the export sector remains vulnerable to exogenous factors such as climatic conditions and terms of trade shocks. Exports of goods and services have been increasing at an average rate of 20 percent in the past five years. On the other hand, imports have been increasing at an average rate of 21 percent. In 2006/07, a surge in imports is attributed to high oil prices in the world market, and the increased demand of capital goods, as well as intermediate materials in keeping pace with growth momentum of the economy. As a result, during 2006/07, developments in the external sector were highly influenced by the increase in oil prices in the world market and a severe drought at home. A sharp increase in international oil prices, coupled with increased demand for oil for thermal power resulted in a higher import bill, which could not be supported by the modest increase in exports. Consequently, the current account deficit (net of program grants) widened to 14 percent of GDP from 11¼ percent of GDP in 2005/06. Nevertheless, the overall balance of payments

position remained positive on account of continued strong capital inflows in form of program and project assistance, direct foreign investments and debt relief received under the Multilateral Debt Relief Initiative (MDRI). As a result, official foreign exchange reserves increased to US$2.3 billion at the end of June 2007, enough to finance about 4 months of next year's imports. The shilling remained broadly stable in nominal effective terms during 2006/07, following a trend of depreciation in previous years.

14. In 2007/08, the current account deficit is projected to decline modestly, as the anticipated growth in exports will outpace the continued rapid growth of imports driven by demand for new investments particularly in the infrastructure and mining sectors. Export performance will result from expected improved performance in traditional exports assuming good weather continues and improved performance in the services sector especially tourism and transportation will be sustained. It is expected that the current account deficit that is projected at around 13¾ percent of GDP (net of program grants) in 2007/08 will be financed by strong foreign direct investments and increased disbursements in program and project assistance. As a result, the overall balance of payments is anticipated to remain positive, with gross international reserves remaining high at around 2.3 billion by the end of June 2008. The gross international reserves will be enough to cover about 4 months of the next year's import of goods and services.

Private sector development:

15. The Business Registration and Licensing Authority (BRELA) is being modernised, including digitisation of its records and those of related registries, to cope with growing business registration and licensing requirements. A database for land disputes and caseloads has also been established in the Ministry of Lands, Housing, and human Settlements Development, in preparation of a programme for backlog clearance. In line with recent labour law reforms, the Commission for Mediation and Arbitration (CMA) was launched in May, 2007 and eight tripartite sector Wage Boards established. Other activities include the operationalisation of the Commercial Court in Mwanza (northern Tanzania). The different efforts to strengthen the business environment are coordinated through the Business Environment Strengthening (BEST) programme.

Infrastructure

16. Consistent with the draft Medium Term Transportation Infrastructure Investment Plan (TSIP), the budget for implementation of key roads projects has been enhanced, from 2.6 percent of GDP in 2006/07 to 4.1 percent of GDP in 2007/08. Following the enactment of a new Roads Act in April 2007, the Government is exploring options for increasing the resource envelope for this area, including private sector participation. The funding of the Road Fund, established to provide for roads maintenance costs, has been enhanced thorough a 100 percent upward adjustment of the Fuel Levy to ensure sufficient financing of road maintenance. The

concessioning of the railway operations, which became effective in September 2007, is also expected to improve the performance of the transportation sector, thereby addressing one of the most binding constraints to private sector development.

Energy

17. Implementation of TANESCO's Financial Recovery Plan (FRP) continued reasonably well, assisted by the earlier than expected recovery of hydro generation capacity. The experts procured with World Bank support needed more time to finalise their input into TANESCO's tariff application to the regulator, EWURA, leading to a delay in the submission of the application. A decision by the regulator is expected by early 2008. TANESCO is using the private emergence power generators to meet intermittent supply deficits, pending finalisation of procurement of its own 145MW gas fired plants. TANESCO has also signed a TShs 235 billion (about USD 220 million) medium term loan with a syndicate of local financial institutions, as part of the FRP implementation. As the FRP envisages substantial investment in the power infrastructure, the Government is continuing consultations with development partners to secure their support to the investment budget.

18. Further to TANESCO related action, the Government is implementing a broader power sector reform agenda to increase the sector's contribution to the national effort towards growth and reduction of poverty. The main elements of the power sector reforms strategy include establishing an efficient energy production, procurement, transmission, distribution and end-use systems in an environmentally sound and sustainable manner; and ensure availability of reliable and affordable energy supplies. A new Electricity Act to facilitate competition in the generation, transmission and distribution segments, and clarifying the institutional and regulatory arrangements in the sector, was presented to Parliament in November, 2007.

Poverty reduction

19. Tanzania's effort towards reducing poverty and meeting the MDGs is guided by MKUKUTA, the national strategy for growth and reduction of poverty, formulated through very broad consultations, and linked to the National Development Vision 2025. The MKUKUTA Annual Implementation Report (MAIR) was released in November, 2007 showing progress in most areas, even as the measurement of poverty status is hampered by the infrequency of household budget surveys. MKUKUTA areas recording good performance include real GDP growth, domestic revenue collection and related revenue services, improved food self sufficiency, and public expenditure management. As in 2006, the report calls for further refinement of the growth strategy, focusing on areas that might yield quick results, particularly transportation infrastructure, energy, and education.

20. Improvements were also recorded in the education sector, where enrolment ratios for all levels of education system (pre-primary, primary, secondary, and tertiary) improved relative to 2006 levels, and the primary education pass rates reached 80 percent from 22 percent in 2000. The performance in the health indicators continue to depict a mixed picture, with substantial progress recorded in immunization coverage and a declining trend in HIV prevalence; while maternal mortality increased from 529 per thousand live births in 2000 to 578 in 2005 mainly on account of the HIV/AIDS pandemic. The mixed results in relation to the health indicators suggest the diversity of inputs required for improvement in the respective areas. In the year 2006/07 the Commission for Human Rights and Good Governance (CHRGG) received 4,523 new complaints (including 226 from remandees), out of which 3,149 were resolved. While the increase in reported and filed cases is a positive indication of awareness among the people in understanding their rights, the quick out turn of received and resolved cases suggests a significant improvement in the capacity of the Commission.

II. PROGRAMME FOR 2007/08

21. The economic recovery is expected to continue during the remainder of the year, on account of improved weather leading to good agricultural harvest and alleviates recent difficulties with the power supply. Real economic growth is projected at 7.1 percent in 2007 and 7.5 percent in 2008. In addition to the recovery in agricultural production, good performance is expected from the manufacturing and service industries. Food prices are expected to fall further following the harvest, leading to the moderation of inflation to around 6.0 percent by June 2008.

Fiscal programme

22. For 2007/08 the programme projects revenue would reach 16.0 percent of GDP. The substantial increase relative to 2006/07 reflects specific measures, expected to yield about 1 percent of GDP, and continued strengthening of tax administration. Policy measures include indexation of the specific excise duty rates, and adjustment of forestry and hunting fees, as well as the fuel levy and road user charges. Revenue administration measures include the following: the large taxpayers department is further strengthening audits in key areas, including developing specialized expertise in the mining sector, and is making progress on the introduction of electronic filing; the domestic revenue department is tightening procedures for medium taxpayers by establishing specialized units in district offices; and customs processes continue to be improved, in particular to enhance control of fuel products. Collections in the first quarter of the year are in line with this projection. The Government will continue to publish the list of tax exemption beneficiaries each quarter.

23. Total expenditure for 2007/08 is now projected at 27.8 percent of GDP. The wage bill is expected to remain at 5.2 percent of GDP. The Government is still reviewing the recommendations of the Presidential Commission on Public Service Pay as a basis for updating

the Medium Term Pay Policy (MTPP), and is discussing options with the trade unions. In addition to resource constraints for implementing a substantially improved pay package that would ensure improved efficiency of the public service, challenges in formulating a new MTPP include balancing the need for additional staff, especially in frontline services reflecting the MKUKUTA priorities with the need for overall sustainability of the fiscal and macroeconomic frameworks. Domestic interest costs are projected to rise slightly, from 1.0 percent of GDP in 2006/07 to 1.3 percent of GDP in 2007/08, on account of the costs of implementing monetary policy in 2006/07. Development spending is projected to increase to 10 percent of GDP from 6.2 in 2006/07, reflecting increased allocation for the roads sector, execution of MDRI-financed items, and larger project grants.

24. The backbone of the 2007/08 budget is increased domestic revenue and the Government's commitment to refrain from net domestic financing of the budget. To safeguard this objective, implementation of the budget will be based on a prioritised expenditure plan to ensure adequate spending on Government priorities in case of shortfalls in domestic revenue or unexpected spending needs. Shortfalls in programme external financing of up to USD 150 million (about 1 percent of GDP) may be financed domestically.

25. The Government is working to strengthen collection of non-tax revenues and management of natural resources. For this purpose, procurement of a consultant for a study on non-tax revenue, aimed at assessing the revenue potential and adequacy of the administrative framework is underway. In addition, a Government commission is studying the fiscal regime in the mining sector. The results of these studies will be inputs for the 2008/09 budget.

26. Public financial management (PFM) will continue to be focused on strategic resource allocation, and ensuring value for money in budget execution. To this end, the public financial management reform program, which guides our reforms in this area, will be updated by the end of 2007. For the 2008/09 budget, the Government will introduce scenario analysis in three pilot Ministries for the MTEF period covering 2008/09-2010/2011, to strengthen expenditure prioritisation. The Government will also continue consultations with development partners on ways to strengthen the MTEF through improved predictability of medium term external financing. The capacity to carry out value for money audits is being enhanced in the Expenditure Tracking and Monitoring Unit (MoF), the PPRA, and NAO. The Government is also working with East - AFRITAC to establish a framework for tracking budget execution along the MKUKUTA Clusters by achieving greater integration of the Strategic Budget Allocation System (SBAS) and the IFMS. In addition, the Government plans to replace the 1986 GFS economic classification of the budget with the 2001 classification. To this end, we are working with East – AFRITAC to develop the new structure before June, 2008. Regarding cash management, the CMU has introduced a framework and is working with all Ministries to prepare cash plans for the respective Votes, and will start producing the three-month rolling cash flows forecasts by

end-March, 2008. The CMC will finalise the plan to transfer Government deposits in commercial banks to the BOT (structural benchmark) by March, 2008 too.

27. Our medium term fiscal policy will continue to be based on no domestic financing of the budget, increasing revenue mobilisation, and improving effectiveness of public spending. We envisage increasing the share of spending on infrastructure to stimulate faster growth. We are also evaluating implementation modalities of the Constituency Development Fund with a view to ensuring that adequate controls, transparency, and coordination with central and local Government spending plans are in place. We will start work on updating the existing study on tax expenditures aiming at the preparation of a tax expenditure report to accompany budget documentation in the course of 2008/09.

Monetary policy

28. The implementation of monetary policy by the Bank of Tanzania continues to focus on achieving appropriate levels of liquidity in the economy that are consistent with the targeted reduction in the rate of inflation. As inflation is currently running above the target against the background of rising oil prices and high inflationary expectations, the BoT will strengthen its vigilance on liquidity expansion in the economy in order to bring it back on track. This will require curbing the annual growth rate of reserve money to 20 percent by end-June 2008. Correspondingly, the average stock of extended broad money (M3) is projected to grow by about 21 percent during the year.

29. In the context of using foreign exchange sales for liquidity management, exchange rate policy will remain flexible, with intervention limited to promoting orderly market conditions. In a bid to bring reserve money back on track for the remainder of the year, the BoT will step up its foreign exchange sales in the inter-bank market for sterilization purposes and conduct repurchase agreements more frequently to fine tune reserve money positions. This move will proportionally lessen liquidity management burden on Treasury bills and ease pressure on interest rates. Furthermore, to mitigate the impact of high and volatile interest rates on private sector credit, the BoT will reduce tender sizes in future auctions, broaden the direct participation of small and medium investors in the Treasury bills market, move to a biweekly schedule for the T-bill auction (by January, 2008), and develop benchmark maturities. These two measures combined will help achieve significantly lower interest rates.

30. The Bank of Tanzania will also inform market players and the general public – on a monthly basis of the objectives and rationale of its monetary policy stance for a given month. The objective of this move, which will start from December 2007, is to enhance the predictability of the Bank's monetary policy stance and promote orderly financial markets. In addition, the BoT intends to hold quarterly press conferences to inform the public on economic developments.

31. With the large aid inflows envisaged in the medium term, monetary policy will remain focused on reining inflation, particularly from a domestic demand perspective. The Bank will continue to use an appropriate mix of instruments at its disposal. Greater coordination between fiscal and monetary policies would be critical to facilitate effective absorption of donor funds without causing upward pressures on domestic interest rates; exchange rate of the shilling or on domestic consumer prices. To this end, the activities of the joint Cash Management Committee will be strengthened and sustained so as to facilitate effective management of liquidity in the economy.

32. The monetary policy stance of the Bank of Tanzania in the remainder of the year and in the medium term will continue to support a strong growth of credit to the private sector in line with envisaged broad based growth of the economy and poverty reduction initiatives. Increased competition among banks and measures being taken under the ongoing second generation financial sector reform aim to enhance the flow of credit to private businesses including small and medium enterprises (SMEs). Operational guidelines for the envisaged Development Finance Guarantee Facility have already been developed and approved by the Ministry of Finance although no funding has been provided in the budget during 2007/08. The facility is however expected to be operational once funding has been made available. With regard to monitoring of other guarantee schemes which are operational, namely Export Credit Guarantee and Small and Medium Enterprise schemes, the Bank of Tanzania in collaboration with Participating Financial Institutions continues to monitor all guaranteed projects both offsite and onsite with monthly reports being submitted to the Ministry of Finance. We will continue to adhere to our commitments on the size and governance of the medium-term credit and credit guarantee initiatives to ensure transparency and limit undue fiscal risks. Specifically, we will ensure that all credit facilitation and guarantee 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.

Financial sector reform and financial stability

33. In the context of implementation of the second generation of financial sector reforms, we will proceed expeditiously with the completion of the amendments to the Land Act and the new Condominium Law currently under preparation, which are critical steps in addressing key bottlenecks to the provision of medium-term credit. To strengthen the regulatory framework for non-bank financial institutions, especially the rapidly growing pension funds, we will proceed over the coming months to finalize the harmonization of the amendment of the Social Security Act with the unified legal and regulatory framework for pension funds with the objective to submit the legislation to Parliament by end-February 2008 (structural benchmark). This would allow the BoT to assume the role of the regulator and supervisor of financial aspects of pension funds until a new independent regulator is put in place under the unified legal and regulatory

framework. Furthermore, to gear prudential supervision toward overseeing a fast-growing and diversifying financial system, we intend to strengthen risk-based supervision by introducing by end-2007 a framework for quarterly stress-testing of banks.

Governance

34. The Government's programme for improving governance is guided by the PFM reforms and the second National Anti-Corruption Strategy Action Plan (NACSAP II). In conjunction with development partners, the Government is finalising a revised PFMRP Strategic Plan outlining the future of PFM reforms to support the Ministry of Finance, the National Audit Office (Union Government), and the National Audit Office in Zanzibar more oriented towards providing services to the MDAs and the general public without losing essential controls over use of public resources and ensuring value for money. Implementation of the NACSAP II launched in December 2006 and a new Anti-Corruption law enacted in April 2007 will be given further impetus with a strengthening of the Prevention and Combating of Corruption Bureau (PCCB). With the support of development partners, the Government is also scaling up its efforts to implement its comprehensive Legal Sector Reform Programme (LSRP).

35. The special audit of the EPA account at the BOT was completed in late November, 2007. When finalized, the findings of the audit will be made publicly available and we will prepare a decisive follow-up plan as required, in which case, the Government remains committed to the expeditious adoption and implementation of appropriate remedial measures.

Statistics

36. The Government will continue to strengthen its statistical base with the objective of subscribing to the Special Data Dissemination Standard (SDDS) as soon as possible. The recent introduction of new national accounts statistics will be followed by the development of quarterly GDP estimates. The National Bureau of Statistics (NBS) also plans to provide more information on methodology and supporting data for the new national accounts and for the consumer price index on its web site in the coming months. A new household budget survey is expected to be completed by mid-2008. Once the results are available, the NBS intends to rebase its consumer price statistics, for which it will request assistance from AFRITAC. The Bank of Tanzania is working to improve private debt and portfolio flows statistics in the financial account of the balance of payments.

Conclusion

37. Implementation of the economic and financial programme approved by the Executive Board of the Fund is progressing well, with substantial progress being noted in the fiscal and

some poverty reduction areas. A combined effect of high liquidity, low food production, and a poor appetite for foreign exchange among commercial banks led to higher than programmed growth in reserve money and inflation. The Government is implementing measures to address this, as part of the programme to be monitored by the Fund.

38. The programme to be implemented by the Government during the remainder of 2007/08 will be monitored by the quantitative assessment criteria and indicative targets set forth in ***Table 1*** annexed hereto**,** and the structural assessment criterion and benchmarks shown in ***Tables 2 and 3***. The programme seeks to promote high and sustainable growth as a basis for more rapid poverty reduction. This primary objective will be pursued on the basis of sustained macroeconomic stability, enhanced public resource mobilisation, efficiency in public spending, increasing the contribution of the financial sector to economic growth, and continuously improving the business climate to increase investment. The Government is confident that the development partners, including the Fund, will maintain and increase their support through financing and policy advice, especially in view of the large investment requirements in communication infrastructure, energy, water, and education.

MINISTRY OF FINANCE
DAR ES SALAAM, TANZANIA
DECEMBER, 2007

Table 1. Tanzania: Quantitative Assessment Criteria and Indicative Targets Under the Policy Support Instrument, 2007/08

	2007							2008			
	June			September		December		March		June	
	Assessment Criteria	Adjusted	Actual	Indicative Targets	Preliminary	Assessment Criteria	Revised	Indicative Targets	Revised	Assessment Criteria	Revised
	(Billions of Tanzania shillings; end of period, unless otherwise indicated)										
Net domestic financing of the government of Tanzania (cumulative, ceiling) [1, 2]	67	314	237	-230	-705	-300	-300	-90	-90	0	0
Accumulation of budgetary arrears (ceiling; indicative target only)	0	0	0	0	0	0	0	0	0	0	0
Average reserve money (upper bound) [3]	1,680	1,680	1,685	1,793	1,836	1,934	1,934	1,975	1,975	2,033	2,042
Average reserve money target [3]	1,664	1,664	---	1,775	---	1,915	1,915	1,956	1,956	2,013	2,022
Average reserve money (lower bound) [3]	1,647	1,647	---	1,757	---	1,896	1,896	1,936	1,936	1,993	2,002
	(Millions of U.S. dollars; end of period)										
Net international reserves of the Bank of Tanzania (floor) [4]	1,754	1,559	2,194	1,881	2,807	1,899	2,367	1,765	2,212	1,683	2,036
Accumulation of external payments arrears (ceiling) [5]	0	0	0	0	0	0	0	0	0	0	0
Contracting or guaranteeing of external debt on nonconcessional terms (ceiling) [5]	0	0	0	0	0	0	0	0	0	0	0
Memorandum item:											
Foreign program assistance (cumulative grants and loans) [1]	932	---	737	502	768	774	824	818	883	943	997

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 November 20, 2006.

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

[2] To be adjusted upward by up to US$150 million for the Tanzania shilling equivalent of a shortfall in foreign program assistance from the amounts shown in the memorandum item.

[3] Assessment criteria and indicative targets apply to upper bound only.

[4] Floors are set US$200 million below projected levels. Floor will be adjusted downward for any shortfall in foreign program assistance from the amounts shown in the memorandum item.

[5] Continuous assessment criterion under the PSI; excludes arrears on debt-service payments pending the conclusion of debt-rescheduling agreements.

Table 2. Tanzania: Structural Assessment Criterion and Benchmarks Under the Policy Support Instrument, July 2007 - December 2007

Measure	Target Date of Implementation	Status
Fiscal		
Cash Management Unit in the Accountant General's Department and Cash Management Committee, including both MoF and BoT staff, to produce updated Government's three month rolling cash flow forecast and liquidity management plan at the end of each quarter.	Continuous	CMU and CMC established, but 3-month cash flow is delayed
Customs and Excise Department to develop a risk management strategy/plan, with a detailed timetable, to strengthen risk management and selectivity principles.	End-September 2007	Completed
Financial Sector		
Inter-agency committee on financial sector reform will submit to Government a proposed unified legal and regulatory framework and investment guidelines for pension funds.	End-September 2007	Delayed pending harmonization with Social Security Act
Governance		
Complete the special audit of the NBC-EPA debt in accordance with the agreed terms of reference.	End-October 2007	Audit report submitted to the authorities in November
Energy		
Submit to the regulator a request for an aggregate electricity tariff increase based on full cost recovery (including all current operations, system maintenance, depreciation, and commercial financing costs), consistent with paras. 54-56 of the MEFP attached to the authorities LOI of November 20, 2006. 1/	End-July 2007	Submitted in mid-October

1/ Assessment criterion

Table 3. Tanzania: Structural Benchmarks Under the Policy Support Instrument, January 2008 - June 2008

Measure	Target Date of Implementation
Fiscal	
Cash Management Unit in the Accountant General's Department and Cash Management Committee, including both MoF and BoT staff, to produce updated Government's three month rolling cash flow forecast and liquidity management plan at the end of each quarter.	Continuous
Complete the integration of the Customs and Excise Department and TISCAN's import clearance processes.	End-March 2008
Adopt a plan to transfer government deposits in commercial banks to the BOT.	End-March 2008
Financial Sector	
Submit to Parliament amendments for harmonizing the regulatory framework for pension funds to allow the BoT to assume the role of the regulator and supervisor of financial aspects of pension funds.	End-February 2008
Establish the credit reference databank and its operating guidelines.	End-June 2008

APPENDIX I—ATTACHMENT II
Technical Memorandum of Understanding on Selected Concepts and Definitions Used in the Monitoring of the PSI-Supported Program

December 2007

Introduction

1. The purpose of this Technical Memorandum of Understanding (TMU) is to describe concepts and definitions that are being used in the monitoring of the quantitative assessment criteria and indicative targets under the Tanzania's PSI-supported program.

Net international reserves

2. Net international reserves (NIR) of the Bank of Tanzania (BoT) are defined as reserve assets minus reserve liabilities. The BoT's reserve assets include (i) monetary gold; (ii) holdings of SDRs; (iii) the reserve position at the IMF; (iv) holdings of foreign exchange, including the Tanzanian government's Poverty Reduction Budget Support (PRBS) and all of its foreign currency deposits at the BoT, and (v) other liquid and marketable assets readily available to the monetary authorities. Reserve assets exclude assets pledged or otherwise encumbered, including but not limited to assets used as collateral or guaranteed for a third-party external liability (assets not readily available). The BoT's reserve liabilities include (i) all short-term foreign exchange liabilities to nonresidents, and (ii) all liabilities to the IMF. Reserve liabilities exclude medium and long-term foreign liabilities.

Reserve money and reserve money band

3. Reserve money is defined as the sum of currency issued by the BoT, including the vault cash of commercial banks, and the deposits of the commercial banks with the BoT. The reserve money targets are the projected daily averages of December 2007, March 2008, and June 2008, within a symmetrical one percent band. The upper bound of the band serves as the assessment criterion or indicative target.

Net domestic financing of the Government of Tanzania

4. Net domestic financing of the Government of Tanzania (NDF) includes financing of the budget of the central (union) government of Tanzania ("government") by the banking system (BoT and commercial banks) and the nonbank public. NDF is calculated as the cumulative change since the beginning of the fiscal year in the sum of (i) loans and advances to the government by the BoT (including paper issued by the BoT for monetary policy purposes) minus all government deposits with the BoT (including funds from paper issued by the BoT for monetary policy purposes); (ii) loans and advances to the government by the commercial banks minus all government deposits held with the banks; and (iii) the outstanding stock of domestic debt to nonbanks excluding: government debt issued for the

recapitalization of the NMB and TIB; debt swaps with COMELCO (Russia) and the government of Bulgaria; mortgage on acquired sisal estates; compensation claims; and debt of parastatal companies assumed by the government.

Government deposits

5. Government deposits at the BoT include government deposits as reported in the BoT balance sheet, and foreign currency-denominated government deposits at the BoT, including the PRBS account and the foreign currency deposit account.

External payments arrears

6. External payments arrears consist of the total amount of external debt service obligations (interest and principal) of the government and the BoT that have not been paid at the time they are due, excluding arrears on external debt service obligations pending the conclusion of debt-rescheduling arrangements.

Contracting or guaranteeing of external debt on nonconcessional terms

7. The term "debt" will have the meaning set forth in Point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000 (Decision No. 12274-(00/85)). Government debt is outstanding debt owed or guaranteed by the Government of Tanzania or the Bank of Tanzania.

8. Government debt is considered nonconcessional if the grant element is lower than 35 percent, calculated using discount rates based on Organization for Economic Cooperation and Development (OECD) commercial interest reference rates (CIRR), adjusted as appropriate for different maturities. This assessment criterion applies not only to debt as defined in Point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000 (Decision No. 12274-(00/85)), but also to commitments contracted or guaranteed for which value has not been received.

Budgetary arrears

9. Budgetary arrears are defined as new arrears accumulated during the fiscal year on wages, domestic interest, and goods and services.

Foreign program assistance

10. Foreign program assistance is defined as grants and loans received by the Ministry of Finance through BoT accounts and commercial banks and is calculated as the cumulative sum, since the beginning of the fiscal year, of the receipts from (i) program loans and (ii) program grants.

Program exchange rate

11. The program exchange rate is set at the end-September 2007 exchange rate (T Sh 1230 per U.S. dollar).

Adjusters

Net international reserves

12. The quantitative targets for the BoT's net international reserves will be adjusted downward by the amount in U.S. dollars of any shortfall in foreign program assistance, up to a limit of US$150 million, relative to projections shown in the Quantitative Assessment Criteria and Indicative Targets Table attached to the applicable Letter of Intent and Memorandum of Economic and Financial Polices of the Government of Tanzania.

Net domestic financing

13. The quantitative limits on the net domestic financing of the Government of Tanzania will be adjusted upward for any shortfall in foreign program assistance in U.S. dollars, up to a limit of US$150 million, converted into Tanzania shillings at the program exchange rate.

Data reporting requirements

For purposes of monitoring the program, the government of Tanzania will provide the data listed below.

14. The following tables related reporting on the developments in relation to the program's assessment criteria and indicative targets to be provided quarterly:

Table of Quantitative Assessment Criteria and Indicative Targets.
Table of Structural Assessment Criteria and Benchmarks.

15. Other data to be provided monthly, quarterly, or other frequency of compilation:

The balance sheet of the BoT.
The consolidated balance sheet of the commercial banks.
The monetary survey.
Commercial banks domestic lending by borrowing sectors.
Commercial banks interest rate structure.
The flash report on revenues and expenditures.
The TRA revenue report.
The Monthly Domestic Debt Report.
Monthly report on Central Government Operations.
The external cash flow statement, including details on payments of interest and principal on government external debt.
Program grants and loans.
Exports and Imports.
Balance of payments.

The published consumer price index report of the National Bureau of Statistics (NBS).
The annual national accounts statistics in constant and current prices as prepared by the NBS.

INTERNATIONAL MONETARY FUND

UNITED REPUBLIC OF TANZANIA

Second Review Under the Policy Support Instrument—Informational Annex

Prepared by the African Department

December 7, 2007

Contents | Page

I—Relations with the Fund
(As of October 31, 2007)

I. Membership Status: Joined 06/10/62; Accepted the obligations of Article VIII, Sections 2, 3 and 4: 07/15/96.

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	0.44	1.40

IV. Outstanding Purchases and Loans:	SDR million	Percent Quota
Poverty Reduction and Growth Facility Arrangements	11.20	5.63

V. Latest Financial Arrangements:

Type	Approval date	Expiration date	Amount approved (SDR million)	Amount drawn (SDR million)
PRGF	08/16/2003	8/15/2007	19.60	19.60
PRGF	04/04/2000	08/15/2003	135.00	135.00
PRGF	11/08/1996	02/07/2000	181.59	181.59

VI. Projected Payments to Fund
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2007	**2008**	**2009**	**2010**	**2011**
Principal	--	--	--	0.28	1.40
Charges/interest	0.34	1.26	1.25	1.25	1.25
Total	0.34	1.26	1.25	1.53	2.65

VII. Implementation of HIPC Initiative:

	Enhanced framework
Commitment of HIPC assistance	
Decision point date	Apr 2000
Total assistance (US$ million)	2,026.00
Of which: Fund assistance (US$ million)	119.80
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[1]	7.45
Total disbursements	96.40

VIII. Implementation of MDRI Assistance:

1.	Total debt relief (SDR million)[2]	234.03
	Of which: MDRI	207.00
	HIPC	27.03

2. Debt relief by facility (SDR million)

	Eligible Debt		
Delivery date	**GRA**	**PRGF**	**Total**
January 2006	N/A	234.03	234.03

[1] Under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative, an additional disbursement is made at the completion point that corresponds to interest income earned on amounts committed but not disbursed during the interim, 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.

[2] The Multilateral Debt Relief Initiative (MDRI) provides 100 percent debt relief to eligible member countries that are qualified for the assistance. The debt relief covers the full stock of debt owed to the Fund as of end-2004 which remains outstanding at the time the member qualifies for such debt relief. The MDRI is financed by bilateral contributions and the Fund's own resources, as well as the resources already disbursed to the member under the HIPC Initiative (see Section VII above).

IX. Safeguards Assessments:

Under the Fund's safeguards assessment policy, Bank of Tanzania (BoT) was subjected to an assessment with respect to the PRGF arrangement approved on August 16, 2003. A safeguards assessment of the BoT was completed on December 05, 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.

X. Exchange Arrangements:

The currency of Tanzania is the Tanzania shilling. The Annual Report on Exchange Arrangements and Exchange Restrictions (AREAER, 2007) characterizes Tanzania's exchange rate regime as a managed float with no pre-determined path. The official exchange rate is determined in relation to 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 1,270 per U.S. dollar as of end-July, 2007. The exchange system is free of restrictions on the making of payments and transfers for current international transactions.

XI. Article IV Consultation:

The most recent Article IV consultation was concluded on June 27, 2007 (Country Report No. 07/246). The next Article IV consultation is expected to be completed in 2009.

XII. Technical Assistance

A. AFRITAC East[1]

	Area	*Focus*
2003/04	Public financial management	Intergovernmental financial relations; program budgeting
	Revenue administration	Work plan for the Tanzania Revenue Authority (TRA); Stamp Duty Act
	Financial sector regulation and supervision	Prudential supervision; AML/CFT legislation
	Monetary operations	Liquidity forecasting; monetary policy instruments; operational guidelines and procedures

[1] Unless otherwise indicate, refers to technical assistance provided to the mainland of Tanzania.

	Area	*Focus*
	Economic statistics	PPI; IIP; quarterly national accounts; agricultural census; industrial census; CPI; GFS
2004/05	Public financial management	Intergovernmental financial relations; program budgeting; Medium-term expenditure framework (MTEF); cash flow planning; IFMIS Zanzibar—design reform program; commitment control
	Revenue administration	Modernization of TRA; customs administration; tax policy
	Financial sector regulation and supervision	Financial sector legal framework
	Monetary operations	NPS legal and regulatory framework; liquidity management and seasonality; domestic debt market
	Economic statistics	Regional GDP; CPI; extending GDP series backwards Zanzibar—CPI
2005/06	Public financial management	Financial accountability; support to comprehensive PFM reform program; cash flow planning and management Zanzibar—commitment control
	Revenue administration	Tax administration; risk assessment and audit; IT support
	Financial sector regulation and supervision	Risk-based supervision; bank resolution; prudential regulations
	Monetary operations	NPS legal and regulatory framework; liquidity management and seasonality; domestic debt market; reserve management
	Economic statistics	Diagnostic analysis and strengthening of data weaknesses; industrial indicators; quarterly national accounts; GFS; CPI;BOP manual
2006/07	Public financial management	Cash-flow planning Zanzibar—cash management
	Revenue administration	Tax modernization program; customs reform and modernization; rationalization and integration of Customs and Tiscan

Area	*Focus*
	Zanzibar—Modernization plan for Zanzibar Revenue Board (ZRB); large taxpayer office; tourism taxation
Financial sector regulation and supervision	Risk-based supervision and on-site inspection; prudential regulations for new Bank and Financial Institutions Act
Economic statistics	BOP and International Investment Position (IIP); revised CPI; PPI

B. Headquarters

Department	Date	Form	Purpose
Fiscal Affairs	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
	July 2005	Mission	Improve the effectiveness of the Ministry of Finance
	Aug.- Sep. 2005	Mission	Tax administration
	Oct.–Nov. 2005	Mission	Strengthen macro fiscal analysis at the Ministry of Finance
	December 2005	Mission	Tax policy
	April 2006	Peripatetic advisor	Strengthen macro fiscal analysis in Ministry of Finance
	April - May 2006	Expert	Customs Administration
	October 2006	Mission	Customs Administration
	April 2007	Mission	Customs Administration
Legal	March – April, 2003	Mission	Income tax law
	Sept. 2003	Mission	Income tax law
	June 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,

Department	Date	Form	Purpose
			Electronic Transactions bill
Monetary and Capital Markets	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
	September 2005	Mission	Credit reference database and IFRS-generated reports
	January 2006	Mission	Monetary and foreign exchange operations
	January 2006	Mission	Problem bank resolution
	February 2006	Mission	Prudential regulations
	December 2006	Mission	Monetary and foreign exchange operations follow-up
	August 2007	Mission	Assessment of MCM TA implementation
Statistics	2002–03	Long-term consultant	Multisector statistics
	August 2003	Mission	Government finance statistics
	Jan.-Feb. 2005	Mission	Monetary statistics
	October 2005	Mission	Balance of payments statistics
	December 2005	Mission	Technical assistance evaluation
	February 2006	Mission	CPI software application
	November 2006	Mission	Monetary and financial statistics

XIII. Resident Representative: Mr. David O. Robinson has been the Senior Resident Representative since March 2007.

II—RELATIONS WITH THE WORLD BANK GROUP

Partnership in Tanzania's Development Strategy

Tanzania's development strategy is set forth in the MKUKUTA (2005-2010). It is a successor to the Poverty Reduction Strategy Paper (PRSP) that covered 2000-2004. The MKUKUTA addresses three clusters of outcomes: (i) growth and the reduction of income poverty, (ii) improving the quality of life and social well-being, and (iii) strengthening governance and accountability.

Bank Group Strategy

The Bank's Board discussed a new Country Assistance Strategy (CAS) for Tanzania on April 24, 2007. The Joint Assistance Strategy for Tanzania (JAST) comprises four parts, which collectively will serve as the World Bank Group CAS for FY07 to FY10. Part I is the national medium-term framework established by Government for managing development co-operation with its Development Partners (DPs) so as to improve the collaboration in achieving national development and poverty reduction goals. In discussion of the draft JAST, Government and DPs agreed on the need for further joint work on parts II-IV below, engaging the entire DP community and focusing on the Government's own planning process, the MTEF in particular. The appropriate balance of roles between Government and DPs in the JAST and wider planning process has been a fruitful area of dialogue, under continuing review through the Government-led JAST Working Group. Part II and Part III are the Joint Program Document (JPD) developed in consultation with Government by the Development Partners Group (DPG) as a response to Tanzania poverty reduction strategies (MKUKUTA for mainland Tanzania; MKUZA for Zanzibar) and the JAST. Part II is a joint country analysis describing Tanzania's development achievements and challenges. Part III is the joint program part, reflecting DPG planned support and aid effectiveness commitments to Tanzania over the 4 remaining years of MKUKUTA, FY07-10. The World Bank Group (WBG) Part IV describes the WBG's strategic approach and proposed program over support over the FY07-10 period (advice, analytic work and financing, both ongoing and planned). Based on the Results Matrix for all DPs in Part III, Part IV also includes a WBG specific results matrix with milestones that facilitate monitoring of progress during the FY07-10 period.

The Bank is supporting implementation of the MKUKUTA through its full range of instruments, including general and sectoral budget support, project support, analytic and advisory activities, guarantees, and equity investments by IFC.

General budget support is provided in the form of Poverty Reduction Support Credits (PRSCs), jointly with a group of 13 other donors. There is joint performance assessment and a common review process. Tanzania's first PRSP was supported through a series of three PRSCs (2003-2005). After the finalization of Tanzania's second PRSP, the Bank together with the other budget support donors developed a new Performance Assessment Framework based on Tanzania's new PRSP. Its implementation is expected to be supported by the Bank through a series of five PRSCs, the first and second of which (PRSC-4 and PRSC-5) were approved by the Bank's Board of Executive Directors on May 9, 2006 and April 24, 2007. It covers six focus areas. These are the three clusters of the MKUKUTA (i.e., growth and the reduction of income poverty, improvements of quality of life and social well being, and governance and accountability), macroeconomic stability, resource allocation and budget consistency, and public financial management. The most recent annual review of general budget support to Tanzania was held in November 2007.

In the social sectors, the Bank provides support through a sectoral development policy credit and grant for secondary education (US$150 million each), the third and last tranche (US$50million) of which is expected to be disbursed in FY07. The objectives are to improve education, expand school access, and increase retention at both primary and secondary levels. Bank support has already facilitated a significant increase in school enrollments. In April 2007, the Board approved a credit for US$42 million to support the education improvement project for Zanzibar. The objectives of the program are to improve completion on lower secondary education including achieving better examination results. This will be facilitated through construction of secondary schools, laboratories and facilities for teacher training, by providing in-service mathematics and science training to teachers, and making text books in core subjects available to all primary secondary schools in Zanzibar. After the focus on primary and secondary education, in FY08 the Bank will also support reforms of higher education and science and technology in Tanzania through a proposed credit in the amount of US$150 million. The Bank contributes to the health sector multidonor "basket fund," which supports sector reforms and funds 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 supports access to improved and sustained water and sanitation services in rural communities. A new Water Sector Support Program project (US$200 million) was approved by the Board in February 2007. It supports GoT's strategy for improving governance of water resources management and sustainable delivery of water supply and sanitation services. The objective of the IDA-funded Tanzania Social Action Fund (TASAF) is to 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, to continue the successful outcomes from TASAF-1.

In the agriculture sector, the Bank's Board approved in FY06 a project to support Tanzania's Agriculture Sector Development Program. In addition, the Participatory Agricultural Development and Empowerment Project Credit supports investments in technologies to reduce soil fertility decline.

A Forest Conservation and Management Project helps the government implement policy, particularly by building a framework for long-term sustainable management and conservation of Tanzania's forests. The Marine and Coastal Environment Management Project, aims to strengthen the management of the marine and coastal environment. In FY08, the Bank is expected to approve the multi-country (Tanzania, Uganda, Kenya, Rwanda and Burundi) Lake Victoria Environmental Project II which aims to support regional efforts to improve management of the Lake Victoria ecosystem.

Efforts to improve Tanzania's infrastructure are supported by road and railway projects. In April 2004, the Bank's Board approved a credit 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). In FY08, Bank support to this project is expected to be increased by a supplementary credit of US$100 million. The policy dialogue is now helping prepare a new Road Act, which will be the basis for strengthening the policy and institutional framework for road building and maintenance.

The Bank has also helped the government implement the Power Sector Restructuring Program. It has encouraged the government to build the domestic gas market and generate lower-cost power through the Songo Songo Gas Development and Power Generation Project, and is currently assisting the government in implementation of the Financial Recovery Plan for TANESCO and the development of a medium to long term strategy for the energy sector, which will provide the basis for further investment support. A credit to support rural electrification and access to ICT in the amount of US$105 million is under preparation for presentation to the Board in FY08.

The Local Government Support Project (US$150 million) is designed to strengthen fiscal decentralization, improving accountability in the use of local government resources, and improving management of intergovernmental transfers. Other project 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.

In December 2005, the Board approved a private sector competitiveness project to support Tanzania's efforts to create an enabling environment for its private sector and enhance its competitiveness; the focus is on micro-, small, and medium enterprises. The project will support Tanzania's Business Environment Strengthening (BEST) program, help set up computerized land and business registries, support judicial reform, and develop the financial sector.

An accountability, transparency, and integrity project was approved by the Board in May 2006. The project contributes to improved access to judicial and legal services and the accountable and transparent use of public financial resources. This will be achieved by improving the skills and systems to deliver judicial/legal services and public financial management, and strengthening the capacity of oversight institutions to perform their role.

The International Finance Corporation's (IFC) strategic focus in Tanzania is on the financial, agribusiness, tourism, infrastructure and SME sectors. Recent activities include a US$10 million investment in Bonite Bottlers, a carbonated soft drinks manufacturer, a US$5 million Exim Bank trade facility, and a US$5 million Tier II facility to Stanbic Tanzania. At present, the Multilateral Investment Guarantee Agency (MIGA) has no exposure in Tanzania and no projects planned.

Tanzania joined the World Bank Group in 1962. Beginning with an IDA credit for education in 1963, it has received a total of US$6.2 billion (US$6 billion from IDA) in credits, loans and grants from the World Bank. Total disbursements amounted to US$5.2 billion as of April 30, 2007 (US$4.7 billion from IDA, US$356 million from the IBRD, and US$214 million in IDA grants). Currently, the portfolio comprises 23 active projects, with commitments of US$1.9 billion, in all major sectors; the undisbursed balance is US$1.1 billion.

Statement of Loans, Credits, and Grants (As of April 30, 2007; U.S. dollars)

	IBRD	IDA Credits	IDA Grants	Total
Original Principal	361,030,400	6,004,469,393	274,400,000	6,639,899,793
Cancellations	5,477,944	235,719,662	0	241,197,606
Disbursed	355,552,456	4,662,178,055	214,406,832	5,232,137,342
Undisbursed	0	1,320,691,187	70,337,151	1,391,028,338
Repaid	355,462,456	470,731,336	0	826,193,792
Due	0	1,160,921,834	0	1,160,921,834
Exchange Adjustment	0	0	0	0
Borrower Obligation	0	1,160,921,834	0	1,160,921,834

Source: World Bank Group

Bank-Fund collaboration in specific areas

The IMF and World Bank staffs collaborate closely in supporting Tanzania’s structural reforms. As part of its assistance—through lending, country analytic work, and technical assistance—the Bank, in collaboration with the Fund, supports policy reforms in the following areas:

- **Public expenditure management.** Improvements in public expenditure management have been a top priority of the Tanzanian government since 1995. The Bank, the Fund, and other donors have worked closely to give the government needed support for institutional and policy reforms. The Fund is leading the dialogue on fiscal policy; the Bank concerns itself with strategic resource allocation and operational efficiency of public expenditures. 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 has helped to strengthen and open up the budget process and the allocation of resources to pro-poor priority areas. The Bank is also involved in the fiscal decentralization process through analytical work and the Local Government Support Project. The Bank and the Fund work together to support institutional budget and expenditure management reforms. The annual Bank-led Public Expenditure and Financial Assessment Report (PEFAR)—the most recent one finalized in October 2007—is the main instrument for the donor community to assess progress in these areas. It also integrates the assessment of Tanzania’s financial management and procurement systems, which previously had been assessed through separate Country Financial Accountability Assessment and Country Procurement Assessment Reports.

- **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 enhance domestic revenue collection. The Fund has taken the lead in reforms of tax policy; the Bank has taken the lead in reforms to strengthen tax administration.

- **Financial sector reforms.** Tanzania has instituted far-reaching reforms in the financial sector with strong support from both the Bank and the Fund. Besides contributing to the policy dialogue, the Bank has provided significant technical assistance for financial sector reforms, primarily through two financial institution development projects that support government withdrawal from banking and nonbanking financial institutions while strengthening financial sector supervision. Among successful outcomes of these reforms are the privatization of Tanzania's largest bank and the entry of a fairly large number of international banks into the Tanzanian market. The Bank has also been involved in 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 Program (FSAP) was completed in June 2003. The recommendations of the FSAP have been incorporated into a reform strategy document for the financial sector. The Bank and the Fund have been allocated specific donor responsibilities in implementing the strategy document and have been active in coordination of the implementation process, including donor coordination.

- **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. Among them are (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 improving governance; (vi) the establishment of a Good Governance Coordination Unit in the president's office; and (vii) the launch of the Legal Sector Reform Program. The PSRP has been central to these reforms because 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 to transform 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 directly affects fiscal stability and public sector financial management.

- **Energy sector.** The Bank and the Fund are working closely to find ways to address the crisis in the energy sector. The Bank takes the lead in assisting the authorities with developing emergency power generation plans to alleviate power supply shortages.

- **Trade reforms.** The Bank and the Fund are working closely to help Tanzania establish a pro-growth trade program. Within the context of the Integrated Framework, the Bank led the preparation of a Diagnostic Trade Integration Study that was issued in July 2005. The Bank will carry out follow-up trade and competitiveness analytical work in the coming years, possibly through the soon–to–be-established Multi-Donor Trust Fund for Mainstreaming Trade. The Bank is working toward trade expansion though its regional trade facilitation project. It is also active at the regional level in the dialogue on trade reforms within the East African Community.

World Bank Lead Economist: Paolo Zacchia

III—Statistical Issues

Economic and financial statistics are adequate for surveillance and program monitoring purposes, but remain weak despite progress in some areas and considerable technical assistance. There are 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 through the General Data Dissemination System (GDDS). GDDS metadata were posted on the IMF's Dissemination Standards Bulletin Board (DSBB) in July 2001 and were updated in September 2007. Tanzania is participating in the SDDS and government finance statistics modules of the Fund's GDDS Project for Anglophone Africa (funded by the U.K. Department for International Development (DFID)). This project aims to assist participating countries to implement plans for improvement identified in the metadata. A mission to prepare the data module for the 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 for mainland Tanzania are prepared by the National Bureau of Statistics (NBS) on the basis of data collected by its regional offices and by other government entities. Separate accounts for Zanzibar are compiled by the Office of the Chief Government Statistician for Zanzibar. The data sources for compiling the estimates for Tanzania by expenditure category, the external sector data, and the indicators used to extrapolate benchmark production levels suffer from deficiencies that complicate estimation of savings-investment. The accounts are largely based on the *1968 System of National Accounts* (*1968 SNA*), but also include certain elements of the *1993 SNA*, such as the inclusion of elements of government expenditure (health and education) as household consumption, and the valuation of imports of goods at free-on-board (fob) prices. Annual national accounts are published at current and constant (1992) prices. Annual GDP estimates are also compiled at current prices for 21 regions of Tanzania. To improve the quality of the national accounts, the authorities, with help from donors, are changing the base year of the national accounts from 1992 to 2001. The revised series will be based on the Household Budget Survey (HBS) 2000/01, Integrated Labor Force Survey (ILFS) 2000/01 and Annual Survey of Industrial Production 1999/2000. An East AFRITAC mission in April 2006 provided training and assistance in the compilation of quarterly national accounts (QNA), which have been compiled at current prices since 2001 but have not been yet released. The series have some methodological shortcomings, and in particular suffer from poor source data in the retail and wholesale sector. Recommendations have been made for improvements and for the compilation of constant (2001) price quarterly national accounts, pending also the production of annual accounts using the new base year.

Prices

The NBS compiles a monthly consumer price index (CPI) for mainland Tanzania based on consumer expenditure in 20 urban centers, and a separate price index (urban) is compiled for Zanzibar. The CPI has, since September 2004, been compiled (retroactively to January 2003) using weights based on the 2000/01 HBS data. Key changes were a reduction in the weight given to food from 71 percent to 56 percent and an expansion of the number of products. The index excludes imputations for the price changes of owner-occupied housing. However, methodological problems that may have understated inflation led to the release of a revised CPI from September 2006, though this has not been backdated. The results of a new HBS are expected to be available in 2008, which should eventually lead to revision of the CPI weights.

Government finance statistics

The authorities provide Fund missions with monthly data on central government revenue, expenditure, and financing on a timely basis. Although the underlying concepts broadly follow the *Government Finance Statistics Manual 1986*, the reporting differs from international standards in coverage and the treatment of lending minus repayments, and transfer payments. Coverage of data on the operations of the central government refers to Tanzania mainland only – recently the Ministry of Finance of Zanzibar established a unit tasked with developing a fiscal reporting framework for Zanzibar. The data also exclude the operations of extra-budgetary units and funds. Data for general government are not available as no information is yet provided on the financial position of local governments, although the authorities have stated their intention to produce such reports.

Despite improvements in the recording of government transactions, discrepancies remain between revenue and expenditure data, on the one hand, and financing data. 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, differing source data, and timing differences.

The Ministry of Finance created a database of donor-funded projects in 2001/02 (July-June), with donor assistance. Since then, the number of foreign-financed projects reported by and channeled through the budget has increased significantly.

The government has completed the computerization of its accounting system for budgetary units. Although the authorities indicated that it would allow resumption of reporting in the *Government Finance Statistics Yearbook (GFSY)*, no data were reported for the 2007 *GFSY*. 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 fiscal data for inclusion in the *IFS*.

Monetary statistics

The monetary statistics are broadly adequate for policy and analytical purposes. Nevertheless, a November-December 2006 mission confirmed earlier findings of methodological problems, such as (a) exclusion of some deposit-taking financial institutions from the institutional coverage of depository corporations survey, (b) arbitrary application of the residency criterion by the other depository corporations (ODCs), (c) inadequate subdivision of the resident sector data, (d) misclassification of certain accounting data among statistical aggregates, (e) discrepancies between reported interbank positions, (f) nontransparent 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, recommendations were made to improve the following definitions: net international reserves, foreign assets, foreign liabilities, loans to other resident sectors, claims on the central government, government deposits, central bank liabilities to commercial banks, and deposits included in broad money. The mission also (a) introduced the standardized report form─1SR for reporting central bank data to the IMF; (b) recommended that some additional schedules for reporting of data by commercial banks be introduced to fully satisfy compilation needs, in particular with respect to the sectoral breakdown of financial instruments used by the other depository corporations (ODCs) in their activities; and (c) recommended the expansion of the ODCs to include other deposit-taking financial institutions, such as the savings and credit cooperatives, Pride Tanzania L.M.T., Presidential Trust Fund (PTF), Small Enterprises Development Agency, Tanzania Investment Bank, Tanzania Postal Bank, Twinga Bancorp Limited, Mufindi Community Bank, and Mwanga Community Bank. A follow-up mission in FY2008 will assist the authorities in developing the standardized report form 2SR for reporting data for the ODCs.

Balance of payments statistics

Foreign trade data are prepared by Fund staff missions on the basis of customs data provided by the Bank of Tanzania, 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 continued and significant under-recording of trade and a dearth of information on services. The authorities acknowledged these problems in their response to the data ROSC report published in March 2004 and indicated that the Bank of Tanzania plans to commission a joint study by the NBS and the TRA to determine the magnitude of underrecorded trade and design an appropriate method of estimation. Re-exports are now included in trade data. Balance of payments statistics are reported annually to STA for publication in the *IFS*, along with the annual International Investment Position (IIP).

Tourism revenues are now estimated using the model that was developed from the International Visitor's Exit Survey conducted in 2001. Using the model and subsequent annual surveys, estimates have been made for 2001 through 2005.

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

Data on private "financial" flows are presently minimal. While some information on private banking sector flows can be derived from the monetary survey, other private "financial" flows are not adequately captured through the International Transaction Reporting System (ITRS) and are largely reflected in "errors and omissions." However, the authorities have made commendable progress in collecting information on certain components. The results of the Private Capital Flows Survey for 2000 and 2004 have now been incorporated into the balance of payments and IIP accounts, which improved estimates of foreign direct investment inflows as well as dividend payments and distributed branch profits. The Private Capital Flows Survey is designed to capture information on foreign direct investment and also asks investors to report committed and projected (for the near future) direct investment flows.

Data on the gross and net official reserves of the Bank of Tanzania are provided monthly with a short lag, and are available to the Fund with higher frequency 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, less 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.

East AFRITAC has provided assistance in international investment position statistics, most recently in March 2007. The missions have worked on training, questionnaires, and revised guidelines for international transaction dealers.

TANZANIA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE (AS OF NOVEMBER 14, 2007)

	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]	Data Quality Accuracy and reliability[8]
Exchange Rates	October 2007	November 2007	M	M	M		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	February 2007	March 2007	D, M	D, M	M		
Reserve/Base Money	September 2007	November 2007	M	M	M	LO, LO, LO, LO	LO, O, O, O, LO
Broad Money	September 2007	November 2007	M	M	M		
Central Bank Balance Sheet	September 2007	November 2007	M	M	M		
Consolidated Balance Sheet of the Banking System	September 2007	November 2007	M	M	M		
Interest Rates[2]	September 2007	November 2007	M	M	M		
Consumer Price Index	September 2007	November 2007	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	March 2007	May 2007	M	M	Q		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	July 2007	October 2007	M	M	A		
External Current Account Balance	2006	July 2007	A	A	A	LO, LO, LO, LO	LO, LNO, O, LNO, LNO
Exports and Imports of Goods and Services	April 2007	May 2007	M	A	A		
GDP/GNP	2005	May 2006	A	A	A	LO, LO, LO, LO	LNO, LNO, O, LO, LO
Gross External Debt	June 2006	September 2006	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 October 2002 mission for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning 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 source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies

Statement by the IMF Staff Representative
December 21, 2007

1. This statement reports on developments since the staff report for the Second Review under the Policy Support Instrument (PSI) was issued. The thrust of the staff appraisal remains unchanged.

2. The 12-month inflation rate fell to 7.3 percent in November, reflecting a considerable decline in the food component to 7.5 percent (from 11.4 percent in September). The nonfood component of inflation increased by 2½ percentage points to 7.1 percent.

3. Government revenues continued to exceed expectations through October 2007 (by 2 percent), somewhat diminishing the risk of a revenue shortfall in the current fiscal year (July–June). Total spending was below budget during this period, with a marked shift in the composition of spending toward foreign-financed development expenditures. As a result, net domestic savings through October amounted to just over T Sh 600 billion (nearly 3 percent of projected annual GDP), well above the forthcoming December target of T Sh 300 billion.

4. Steps taken by the Bank of Tanzania (BoT) in recent months to strengthen monetary and foreign exchange operations have succeeded in reining in reserve money (M0) growth. In particular, the BoT has relied more heavily on regular daily sales of foreign exchange to control liquidity, while reducing the amounts of government securities sold at primary auction. As a result, the BoT's internal ceiling for average M0 was met comfortably in November, and through mid-December average M0 remained well below the PSI program ceiling for the month. At the same time, the weighted average yield on T-bills has fallen to 10.5 percent in mid-December (from about 17 percent in October), while the exchange rate has stabilized following an initial appreciation.

INTERNATIONAL MONETARY FUND
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IMF Executive Board Completes the Second Review Under the Policy Support Instrument for Tanzania

The Executive Board of the International Monetary Fund (IMF) today completed the second review under a three-year Policy Support Instrument (PSI) for Tanzania.

The PSI was approved on February 16, 2007 (see Press Release no. 07/26) and is aimed at consolidating Tanzania's strong economic performance through market-oriented policies within an appropriate macroeconomic framework. The PSI seeks high and sustainable growth and more rapid poverty reduction based on enhancing public resource mobilization and efficiency of spending, increasing the financial sector's contribution to growth and the effectiveness of the monetary policy, and improving the business climate.

The IMF's framework for PSIs is designed for low-income countries that may not need IMF financial assistance, but still seek close cooperation with the IMF in preparation and endorsement of their policy frameworks. PSI-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners. This is intended to ensure that PSI-supported programs are consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. Members' performance under a PSI is reviewed semi-annually, irrespective of the status of the program (see Public Information Notice No. 05/145).

Following the Board's discussion on Tanzania, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair, made the following statement:

"The Tanzanian economy continues to perform strongly. The authorities are to be commended for their sound economic policies, which have contributed to buoyant economic growth and moderate inflation. Their commitment to continued structural reforms and the maintenance of macroeconomic stability will further raise the country's growth potential so as to make decisive progress in poverty reduction.

“Recent steps by the Bank of Tanzania have succeeded in reining in monetary expansion and moderating interest rates, and the Bank’s strategy is appropriately geared at further reducing inflationary risks and strengthening monetary control. In particular, it will be important to address the challenges stemming from large capital inflows by strengthening liquidity forecasting and increasing the reliance on foreign exchange sales as the primary tool for mopping up liquidity.

“Strong fiscal performance, underpinned by buoyant revenues and further improvements in tax administration, will continue to anchor macroeconomic stability. Pressing social and infrastructural needs warrant increased public spending, although careful planning will be needed to ensure that spending can be adjusted if domestic revenue falls short of its ambitious target. It is important to remain vigilant with regard to government guarantees and other contingent liabilities so as to ensure value for money in the area of public infrastructure projects. Public financial management will be strengthened through better cash management and expenditure tracking.

“Private sector development and continued productivity growth will be key to further accelerating economic growth. Priorities include accelerating regulatory reform to strengthen the business environment; deepening financial sector reform to improve access to financial services; strengthening prudential supervision, especially in the fast-growing pension fund sector; and reinforcing governance and public accountability. In particular, it will be important to address expeditiously any shortcomings that would be identified in the recently-completed special audit of the external payments arrears account managed by the Bank of Tanzania,” Mr. Portugal said.

**Statement by Peter Gakunu, Executive Director for Tanzania
and Ahmed Amani Ndyeshobola, Senior Advisor to Executive Director
December 21, 2007**

Introduction

1. The Tanzanian authorities are committed to strong macroeconomic policies and deepening of structural reforms, which have resulted in continued robust economic performance. They are thankful to the Fund for the constructive engagement and support, and are appreciative to staff for the candid policy dialogue and advice under the program.

2. The authorities remain steadfast in implementing their economic reform program. All but one end-June 2007 quantitative assessment criteria were observed. The ceiling on reserve money was exceeded by a narrow margin, but the Bank of Tanzania (BoT) has addressed this setback through increased sales of foreign exchange since September 2007 thereby reducing its reliance on Government securities' sales for liquidity management. All structural assessment criteria and benchmarks were implemented, though with a slight lag than envisaged for some of them. Given the strong performance under the program and continued satisfactory results yielded from implementation of core reforms, the authorities request Directors' support for the completion of the review. They broadly agree with the thrust of the staff assessment in the well balanced report on the second review of the PSI, and will take appropriate steps to implement the policy actions recommended.

Recent Economic Developments

3. Tanzania has continued to record impressive economic performance over the past decade, taking advantage of sustained economic reforms; favorable external environment; and broad-based growth, including in trade, tourism, manufacturing, mining, construction, and communication sectors. Real GDP growth is expected to reach 7.1 percent in 2007, while inflation remained within the single digit range at 6.3 percent in 2006/07, slightly above the authorities' objectives. Inflationary pressures intensified in 2007 due mainly to high inflation expectations stemming from high oil retail prices, and a hike in transport costs. The authorities, however, consider this inflationary spike to be transitory and should decline in the coming months following improvements in food supply, as well as continued prudent fiscal and monetary policies. Despite a significant shortfall in programmed foreign financing of about 1.5 percent of GDP, the fiscal position improved substantially in 2006/07, owing to strong revenue performance of up to 1.2 percent of GDP higher than the program projections. Foreign exchange reserves level also remained satisfactory at 4.2 months of imports in 2006/07, thanks to increased foreign direct investment (FDI) and other capital inflows. In addition, the MKUKUTA (PRSP) Annual Implementation Report (MAIR) of November

2007 shows strong progress in the achievement of some MDGs performance indicators, in particular in education and health.

Outlook and Policies for 2007/08 and in the Medium-Term

4. The country's economic performance is expected to remain strong in 2007/08 and the medium term, with real GDP growth projected to be in the range of 7-9 percent. Consolidating fiscal stability, supported by continued robust revenue performance, while accommodating substantive increases in development expenditure for social needs and productivity enhancing investments; as well as strengthening the external position, are among the authorities' main priorities. These, coupled with tighter monetary policy of the BoT, and the accelerated growth performance, are expected to relieve pressure on food prices allowing inflation to subside to the 5 percent target level.

5. The strong economic performance and favorable outlook notwithstanding, the attainment of the MDGs by 2015 remains the daunting challenge for Tanzania. The authorities are conscious that they will have to consolidate macroeconomic stability to mitigate the immediate risks to their economic outlook, including inflation and revenue shortfalls; address infrastructure bottlenecks; and deepen implementation of structural reforms to sustain high economic growth necessary to increase per capita income and reduce poverty substantially. In this connection, the authorities are determined to step up implementation of the MKUKUTA which offers an appropriate framework for further diversification of the sources of production and exports, improvements in public finance management, and integration in the regional and global economy.

Fiscal Policy

6. The authorities' objective in fiscal policy is to sustain fiscal stability in the medium and long terms. In this connection, the 2007/08 budget aims at increasing revenue performance by 1.5 percent of GDP to 16 percent, and the revenue collections in the first quarter of the fiscal year are on track. Appropriate revenue reforms and measures are scheduled with a view to further strengthening tax administration and broadening the tax base. These include reforming the mining sector's fiscal and regulatory regimes; indexing specific excise duty rates; and adjusting forestry and hunting fees, as well as the fuel levy and road user charges. The authorities are determined to further strengthen monitoring and transparency on tax exemptions by publishing the list of beneficiaries and the tax expenditure involved.

7. On expenditure side, while the recurrent expenditures remain stable compared to those of the previous year, the 2007/08 budget projects substantial capital spending increases (+4.1 percent of GDP) reflecting the MKUKUTA priorities, with a view to supporting the authorities' growth and poverty reduction objectives. The planned capital expenditure includes investments in infrastructure and social sectors, with increased allocation for roads,

execution of MDRI-financed items, and larger project grants. The authorities are sensitive to the potential impact of these spending increases on domestic demand and, to this end, are targeting a zero net domestic financing (NDF) of the budget. They, however, know that safeguarding such NDF objective is challenging, as it is subject to risks of revenue shortfalls. The authorities, therefore, intend to execute the budget on the basis of a prioritized expenditure plan, enabling protection of priority spending linked to the achievement of the MDGs, coupled with the implementation of required internal reallocations. The authorities will take advantage of the strong progress achieved in public finance management (PFM) reform program to continue ensuring effective use of public resources. Further steps will include more focus on strategic allocation of resources, and strengthening of expenditure tracking with the support of development partners.

Monetary and Financial Sector Policies

8. The BoT is committed to continue anchoring its monetary policy on maintaining low inflation levels. It has reaffirmed its determination to adopting appropriate measures to keep the reserve money levels in line with price stability objectives. Notably, it is expected that the strong liquidity pressures, stemming from foreign inflows observed over the recent months, will continue to be challenging to monetary policy operations in 2007/08 and medium-term. In this connection, the BoT will step up foreign exchange sales in the inter-bank market for sterilization purposes and carry out repo agreements more frequently to fine tune reserve money positions, thereby reduce reliance on Treasury bills and ease pressure on interest rates. In order to reduce interest rates levels and volatility on private sector credit, the BoT envisages to increase competition in treasury bill market and develop benchmark maturities. The measures planned to encourage competition include a reduction in tender sizes, an increase of frequency of auctions to bi-weekly schedules, and a broadening of direct participation of small and medium size investors. The BoT will also enhance transparency of its policy stance and promote orderly financial markets. Coordination between fiscal and monetary policies will be further strengthened to increase absorption of public funds, while adequately preventing pressures on interest rates and exchange rate, as well as on domestic prices. In this regard, the Joint Cash Management Committee (CMC) is strengthening its activities.

9. Tanzania has a diversified banking system, and a small but growing capital market, as a result of far-reaching reforms of the financial sector over the past decade. The authorities are mindful of the remaining challenges, in particular the need to reform the legal framework for land ownership; the weak capacity of the judicial system; and the need for strong oversight of a fast-growing and diversifying financial system, including introduction of risk-based supervision. In this regard, the authorities are vigorously implementing the second generation financial sector reforms in the context of the Financial Sector Reform Implementation Action Plan (FSIAP) focusing on lease financing with the help of IFC, and investment guidelines for pension funds with the support of the World Bank. Other areas of focus include mortgage

finance, credit information data bank and legal and regulatory framework for credit information bureau. The authorities are also in the process of completing amendments to the Land Act, and the new Condominium Law currently under preparation, which are critical steps in addressing key bottlenecks to the provision of medium-term credit to a wider spectrum of economic actors.

Structural reforms

10. The authorities recognize the need to entrench reforms and safeguard gains especially on macroeconomic stability and PFM, and to strengthen the overall investment climate that will further facilitate private sector development, attract and retain FDI, and sustain high economic growth. In addition to vigorously pursuing prudent macroeconomic and financial policies, the authorities are resolved to deepen implementation of the Business Environment Strengthening (BEST) reform program, the Medium-Term Transportation Infrastructure Investment Plan (TSIP) and the power sector reform agenda, including TANESCO's financial recovery plan.

11. Good governance and strengthened legal framework are also crucial to promoting a friendly business environment. In this connection, the authorities remain committed to providing further impetus to the implementation of the second National Anti-Corruption Strategy Action Plan (NACSAP II), as evidenced by the enactment of the new anti-corruption law and strengthening of the Prevention and Combating of Corruption Bureau. The authorities are also scaling up efforts to implement a comprehensive Legal Sector Reform Program. The field work in relation to the special audit of the EPA account at the BOT was completed in November, 2007 as envisaged under its terms of reference. The authorities are committed to making the findings of the audit publicly available, and implementing expeditiously appropriate remedial measures. To this end, they are grateful for the Fund's ongoing technical assistance on money and foreign exchange markets.

12. The authorities recognize that regional economic and trade integration will continue to play an important role towards sustaining sound macroeconomic policies and enhancing growth. They will continue to participate actively in regional integration frameworks to strengthen the existing regional trading arrangements, especially within the East African Community (EAC) and the Southern Africa Development Community (SADC). The authorities will work closely with the recently enlarged EAC partners to formulate a coordinated approach to economic and trade liberalization in the region, and participate positively in the multilateral trade negotiations effort for a rapid and successful conclusion of the Doha Round.

Conclusion

13. The authorities' continued commitment to strong policies over the past decade has started

to yield strong economic results. They are, however, aware of the further resolute reform effort required to consolidate the progress made. In line with MKUKUTA objectives and Tanzania Vision 2025, the authorities are determined to sustain macroeconomic stability and deepen structural reforms for a broad-based growth as a sustainable basis for poverty reduction and attainment of the MDGs. They count on the continuous engagement with the Fund and the support of the development partners going forward in meeting their development challenges.