UNIVERSITY OF DARES-SALAAM
ECONOMIC RESEARCH BUREAU

The Role and Impact of Foreign Resources On the Economy

First Final Report

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Table of Contents

List of Tables

List of Figures

List of Abbreviations

BEST	Business Environment Strengthening for Tanzania
BFI	Banking and Financial Institution
BOT	The Bank of Tanzania.
BRELA	Business Registration and Licensing Agency
BWM-SEZ	The Benjamin William Mkapa Special Economic Zone
COMESA	Common Market for Eastern and Southern Africa
DSE	Dar –es- Salaam Stock of Exchange
EC	European Cooperation
ECA	East African Cooperation
ERP	Economic and Recovery Plan
ESRF	Economic and Social Research Foundation
FSAP	Financial Sector Assessment Programme
GNP	Gross National Product
HIPC	Highly Indebted Poor Countries
ICSD	International Centre for Settlement of Disputes
ICT	Information and Communication Technology
IDA	International Development Association
IMF	International Monetary Fund
JAST	The Joint Assistance Strategy for Tanzania.
LART	Loans and Advances Realization Trust
LSTF	Legal Sector Task Force
MDGs	Millennium Development Goals
MIGA	Multilateral Investment Guarantee Agency
MNRP	Management of National Resources Project
MPAMITA	Mkakati wa Pamoja wa Misaada Tanzania
MRD	Migration Remittances for Development
MTS	Multilateral Trading System
NBFIs	Non- Bank Financial Institutions
NPEs	The National Poverty Eradication Strategy
OECD	Organization of Economic Cooperation and Development
PRSP	Poverty Reduction Strategy Paper
REI	Resource Endowment Initiative
RIA	Regulatory Impact Assessment
TCRA	Tanzania Communications Regulation Authority
TNCs	Transnational Companies
TP&TC	Tanzania Posts and Telecommunications Corporation
TRA	Tanzania Revenue Authority
TTCL	Tanzania Telecommunication Company
UNCEF	United Nations Children's Fund
UNDP	United Nations Development Programme
WFP	The World Food Programme
ZSGRP/MKUZA	Zanzibar Strategy for Growth and Reduction of Poverty

Executive Summary

1.1. Background of the Study

Since 1986, Tanzania has been perusing for reaching economic reforms aimed at promoting growth through market liberalization. The policy reforms undertaken from 1980s have to a great extent contributed in attracting a considerable amount of foreign resources in terms of Foreign Direct Investment (FDI), Official Development Aid (ODA) and remittances. These foreign resources have been used to augment the limited domestic saving and bring with them finance, managerial skills, technology, marketing expertise and market link all of which are most needed for the economic development. These benefits have thus influence the country to increasingly put in place the environment necessary for attracting their inflows.

1.2. Objective of the Study

The broad objective of this study was to analyze the role of foreign resources in the economy by examining the consensus in the literature that foreign resources lead to better economic performance. External assistance, in the form of ODA has been one of important sources of government revenues which accounting for about 40 percent of the national budget. Effective management of external assistance and use value of the resources for leading industries is important for growth and job creation. Specifically, the study required to, determine the level of domestic resources in Tanzania, identify the contribution of the policy reforms undertaken from 1980s to the effective use of foreign resources, identify how much external resources are needed to supplement domestic resource in the process of developing leading industry/primary industries which will stimulate rapid economic growth and spill-over effects, identify any success story on outwards looking policies that attracted more foreign resources to the economy.

1.3. Study Methodology

In view of the objectives of the study, four independent but complementary research methodologies and activities have been used. These methodologies and activities were major desk study, field research survey, internal and national consultative workshop.

1.4. Major Research Findings

The following are main research findings.

1.4.1. The level of domestic resources in Tanzania

High and sufficient levels of domestic natural resources

Tanzania is a rich country in term of mineral natural resources. It is noted that minerals have a big potentials to increase Tanzania's domestic resource mobilization capacity if utilized efficiently. The study also found that out of the arable land Tanzania has, it only uses about a third of it for cultivation with the other two thirds being idle. Tanzania thus is richly endowed with land which however is underutilized. The great underutilization of arable land is due to several complex problems and constraints. These include lack of capital to invest in agriculture, distorted market, poor productivity, and poor physical infrastructure in areas where the majority of the land is located. According to this study, optimal utilization of domestic resource is sufficient to break Tanzania dependency on foreign resource and poverty trap.

1.4.2. The contribution of the policy reforms to the effective use of foreign resources

In assessing the contribution of policy reform in attracting and utilizing foreign resource; it is found that adequate national development policies are in place and policy reforms are underway. There are also increasing policy consistencies and linkages between long and medium term policy strategies making policy reforms to have definitive positive contributions to effective resource utilization. Some sector specific policies which have had a positive impact include mining policy, investment policy, tourism policy and trade policy. These policies broadly aimed at stimulate investment, production and flows into export oriented areas in which Tanzania has comparative advantages as a strategy for inducing the introduction of technology and innovation into production systems as the basis for economic competitiveness.

1.4.3. External resources needed to supplement domestic resource

1.4.3.1 Official development Assistant (ODAs)

The study found that there is increasing but ineffective foreign aid. Despite the significant volume of foreign aid received by the country the economic growth has been slow at best and this poses an obvious question of aid effectiveness. Alongside many disappointment however, aid has financed many development projects and programmes which achieved high internal rates of return, including schools, health posts, bridges, and road. It also noted complex constraints of foreign aid which seems to determine development success and failure of foreign aid in Tanzania. The study also noted the failure of aid to address the main problem of poverty though is far too lofty expectation for aid but the assumption is that aid flows have potential to offset factors which cause poverty. There also complex challenges of foreign aid associated utilizing aid and capital inflows in ways which complement rather than replace domestic resources, efforts, and initiatives; improving macroeconomic indicators and reducing dependence while increasing reliance on domestic resources.

1.4.3.2 Foreign Direct Investment (FDI)

The study found that adequate FDIs (as one of the major external resources) flows is needed to supplement domestic resources in the process of developing leading industry and primary industries which will stimulate rapid economic growth and spill-over effects. The study found that there is a high level of FDI flow to the economy as compared to other foreign resources. This is largely explained by outward looking economic reforms (sector specific) accompanied with generous attractive fiscal incentives. The study found limited linkages of FDIs to the rest of the economy on one hand and relative impressive performance in various aspects of Tanzanian economy such as mineral export.

1.4.3.3 Remittances

There is a very low level of remittances flow to the economy as compared to other foreign resources. This is mainly explained by a small number of Tanzanians working abroad, limited dissemination of data and information about the international job opportunities, and high number of unskilled labors in the Tanzanian economy. However, other possible challenges include the country's stable peace and security, Tanzanians' culture of having strong ties to relatives and families altogether discourage them to move and work out of their home country, and Tanzania's remittances data capturing system is generally ineffective and therefore very obvious to leave out significant amount of informal remittances unrecorded. However, the study has also found that despite receiving very low remittances, the public appreciated some benefits that are accruing to the economy via remittances.

1.4.4 Success story on "outwards looking policies" that attracted more foreign resources

The study noted that Tanzania is now the leading non-oil destination for FDI in Africa after South Africa. FDI flows of $10 million or less per annum in the 1990s have grown FIFTY-FOLD to over $500 million per annum now. The immediate impact of these increased inflows of FDI has been an increased gold mining activities and production. It is projected that production in the identified mines will expand from 1.05 million oz (33,000 kg) in 2007 to 1.55 million oz (52,000 kg) by 2012. The study notes that mining foreign direct investments have dominated the total flow of FDI in Tanzania. These have only superseded other attractions for international capital. Mineral exports have been rapidly rising to be a major share of total exports in the country even when starting from a low base. Mineral taxation has become another significant source of total tax revenues with limited tax raising capacity. Most of gold mining use modern-day mining technologies and thus is a capital-intensive industry – so it is accounting for only a small employment. That is, currently employment is also low –typically only 1-2% of formal total employment in Tanzania

1.5. General and Specific Policy Recommendations

Given their mandate, this baseline study recommends that POPC to conduct detailed studies to determine the state of these foreign resources for development and provide generic policy recommendations to the government on the efficient utilization of those resources;

1.5.1. Enhancing sustainable domestic resources

As experiences in many rich mineral resources countries have shown, the most important action for poverty alleviation at the initial stage of their mining development is the creation of jobs and support to PRSP priority sectors. There are views that these have often been done through increased linkage between the mining sector and the building of labour-intensive and export-oriented industries, the development of agriculture and the processing of agricultural products, the development of consumer goods and services, and the raising of investment for education and health care. For poverty reduction efforts, the main challenge facing Tanzania is to uplift, transform and build strong, diversified and resilient modern sectors, which can produce efficiently for the domestic market and supply competitively to regional and world markets.

Encourage local driven large scale mining development

Tanzania is blessed with almost all the minerals and natural resources needed for self-sustainability and development, yet we are behaving like wretched lepers incapable of harnessing resources and potentials for our own survival and development. For large-scale mining development, the country needs to mobilize, manage and utilize own natural and additional capital resources through increased national economic governance, local private sector participation, competitive and liberalized market systems and public-private partnerships. Indeed, there is a need for a joint governance approach to development finance, which seeks synergies between domestic capital, and natural resources, private capital inflows, and all forms of foreign aid. In Tanzania, the notion of public-private partnership needs to be emphasized over a much longer time horizon, especially *where the indigenous population needs to take the driver's seat*.

The government should create an environment where more local and foreign investors invest in the large-scale gold, gemstone and industrial mining sub-sectors, which have proved to be of high growth mining potential. This can be achieved by extending the generous investment packages given to local investors in mining to the would-be investors in the large-scale operations. There is a need for prioritization of domestic entrepreneurs by positive discrimination, with the aim of fostering domestic investment to establish locally- based economic growth and mining development.

We should also look into the *issues of empowerment, ownership and employment* in order to ensure that the local people benefit from the large-scale investments that have been started in the country. Where the local people do not meet the standard required by foreign companies, the government should oversee their training, facilitation and acquisition rather than leaving this in the hands of the foreign private sector. Experience shows that if different forms of ownership and management of mining sector firms are employed, then results are positive. STAMICO was not necessarily bad, what should have been done was to let the economic entity to run as an independent corporate entity which was well capitalized.

1.5.2. To intensify implementation of social, economic and political reforms

The government has to ensure that these policy reforms have definitive positive contributions to effective resource utilization *for the interests of Tanzanians*. Tanzania has put a number of sector specific national development policies which have had positive impact on the foreign resources. These include the National Investment Policy, National Mining Policy, National Tourism and National Trade Policy. These policies lack effective strategies for local empowerment in the ownership, management and operation of sustainable mineral development.

These policies should also aim at raising efficiency and widening linkages in domestic production and building a diversified competitive export sector. One of the policy objectives is to *stimulate investment flows into export oriented areas in which Tanzania has comparative advantages as a strategy for inducing the introduction of technology and innovation into production systems as the basis for economic competitiveness.* Others include the need to attain [1] maximum mobilization and utilization of domestic capacity including cooperation with other developing countries [2], the encouragement of inflows of external resources to complement national efforts.

The POPC is also responsible for policy coordination of policy implementation of above investment, trade, production, foreign aid policies and strategies, monitoring, evaluating and analyzing socio- economic development trends and providing advice on macro and sectoral policies as well as broad based socio economic development issues. Equally, the Commission will have to focus on these foreign resource strategic policy issues and problems during this time of financial and economic global crisis with the view of proposing appropriate policy solutions.

1.5.3. There is a need for optimal utilization of foreign resources

Our policy framework of thinking suggested that under certain conditions imports of capital have effects on intermediate policy variables, government expenditure and, the economy. For foreign aid to have a positive fiscal or monetary effect, the marginal propensity to import must be less than the marginal propensity to consume. Interestingly, aid reduces the tax burden but widens the deficit government budget. One way of using foreign aid is to relieve the shortage of foreign exchange. In this way foreign aid can be considered as a source of foreign exchange channeled for example through the monetary system. Tanzania is receiving direct government budgetary support in the form of foreign currency. However, experience suggests that there have been no explicit monetary policy objectives on optimal public utilization of domestic natural resources given the availability of foreign aid. Usually these policies have been coordinated with private sector development policies. Because of the reluctance to increase tax and/or control the government's budgetary deficit, increases in foreign aid lead to expansive monetary policies.

In this study we considered foreign aid in rather general terms. During the global economic crisis foreign aid allocations geared to bilateral aid have been in terms of grants and/or soft loans. The country receives additional resources in foreign currency or its equivalent in goods, over the capacity to import generated by exports or financed from accumulated reserves without the need to make immediate repayment and at a cost lower than the prevailing rates of capital markets.

These foreign resources are used to affect the economic activities thus improving the quality of inputs and output performance above the level otherwise attainable. In turn, this had positive effects upon national goals and thus the economic development of recipient countries. The study did not discuss issues related to aid modalities i.e., the composition of aid, conditionalities and procedures that guide the delivery of foreign aid. However, we recommend that the purpose of foreign aid is at this point in time is to reduce poverty effectively and to induce and/or restore self-sufficient economic growth.

Frequently, all measures to improve efficiency and foreign resource allocation in JAST and MKUKUTA, as well as national and sector development policies to expand the productive capacity of the economy increase the effectiveness of aid on the national economy. Also, Tanzania has to continue undertaking serious and sustained second generation policy reforms as a way to attract new inflows of aid. All foreign aid can be useful if the government of the United Republic of Tanzania, as the major receiver, increases its aggregate demand for commodities and services with simultaneously instituting proper domestic investment policies. Within a good policy environment, the positive impact of foreign aid on growth is rewarded by increasingly higher aid flows.

1.5.4. Enhance implementation of foreign direct investment policy strategies

With reference from the study findings of, deliberate actions need to be done on FDI in terms of policy formulation, implementation, monitoring and evaluation. Precisely, for FDI to bring about significant positive effects in Tanzania, there should be a policy whose major objective is to attract in FDIs FDI that provide linkages with other sector (forward and backward), as well as those finding their ways towards sectors with high potential in raising incomes and reducing poverty through the strong linkages they have to the rest of the economy. Specifically the stakeholders prioritized agriculture sector, tourism sector, and value adding industries such as agro processing and lapidary (mining) industries.

This can be achieved through identification of all potentials in specific areas of the sector for new investments then constructions new and make improvements of existing infrastructure such as roads, railways and utilities (electricity, water, telecommunication, etc) would be a positive step towards attracting investments in the sector. Additionally, excessive incentives to FDI leading sectors, mining in particular can be cut down and raise or increase the same to sectors of interest to the economy.

Also, to gain more from both existing and potential FDIs, there must be sound domestic policies designated objectively to create capacity for absorption and diffusion of skills, knowledge and technology to domestic firms. This can be achieved through human capital development (through strategic education) and technological competency of local labour force (through short and long term but focused training) and through research and development (R & D) centers.

1.5.5. Design and implement remittances policy strategies

There is a need to have an explicit policy supporting migration and search for jobs in the international labour market. The POPC has to enhance national coordinated remittance policy efforts to ensure that the ministries of labour, home and foreign affairs collaborate on issues related to migration and the need to optimize Tanzanians and their resources in Diaspora for the development of the country.

Since we appreciate that remittance contribute to the stock of foreign resources and specifically to GDP, in addition to the public safety net and social security that they may provide for many poor families who treat migration as a strategy to address unemployment and loss of earnings at home. And the saved remittances of migrants represent a pool of funds, which can be mobilized for the development of the country. There is therefore a need to put in place the policy that will lead to increase in remittances. The specific generic policy recommendations may include

The government and concerned institutions should know who migrates, where and for which reasons. This will help to mobilize the working population (Diaspora) outside our country in order to increase the incoming remittances.

1.5.6. Need for balanced inward, outward looking and consistent policy options and strategies

The study done by Alan Roe of Oxford Policy Management in 2009 (*on the "Mining in Tanzania – What Future can we Expect*), suggests that in nine short years Tanzania has already built a high level of macroeconomic reliance on mining in several areas in terms of FDI, Exports and even government revenues and employment. The study notes that mining foreign direct investments have dominated the total flow of FDI in Tanzania. These have only superseded other attractions for international capital. Mineral exports have been rapidly rising to be a major share of total exports in the country even when starting from a low base. Mineral taxation has become another significant source of total tax revenues with limited tax raising capacity. Most of gold mining use modern-day mining technologies and thus is a capital-intensive industry – so it is accounting for only a small employment. That is, currently employment is also low –typically only 1-2% of formal total employment in Tanzania. The story suggests that outward looking policies are not necessary best policy options for optimal utilization of domestic resources and sustainable economic development. *There is a need for balanced inward, outward looking and consistent policy options and strategies for economic growth and reduction of poverty*.

Chapter One: Introduction

1.0 Background of the Study

Since 1986, Tanzania has been perusing for reaching social economic reforms aimed at promoting growth through market liberalization. Not withstanding this positive effort, the country continued to face many developmental problems. Beginning 1995 the government took initiative of preparing National Developmental Vision 2025 which was completed and launched in 1999. The Vision spells out national long term development goals priorities and direction. It is envisaged that the impact would have been much greater if it had not been poor management and inadequacy institutional capacity. The policy reforms undertaken from 1980s have to a great extent contributed in attracting a considerable amount of foreign resources in terms of Foreign Direct Investment (FDI), Official Development Aid (ODA) and remittances. These foreign resources have been used to augment the limited domestic saving and bring with them finance, managerial skills, technology, marketing expertise and market link all of which are most needed for the economic development. These benefits have thus influence the country to increasingly put in place the environment necessary for attracting their inflows.

Given this background the President's Office, Planning Commission, (POPC), finds necessary to review policies and strategies aimed at strengthening socio-economic development particularly policy reform and national development strategies. The review aims at providing data and information to answer the following questions:

- What has been the contribution of the policy reforms undertaken from 1990s to the effective use of foreign resources?
- How much external resources are needed to supplement domestic resource in the process of developing leading industry/primary industries which will stimulate rapid economic growth and spell-over effect?
- Is there any success story on outwards looking policies that attracted more foreign resources to the economy?

1.2 Justification of the Study

Since the government is committed to economic reforms that encourage the inflows of foreign resources into the economy, however there are some concerns in the effectiveness of such resources in countries economy. The shortcoming of Foreign Direct Investment (FDI) and Overseas Development Assistance (ODA) include lack of a foreign aid policy; lack of a comprehensive mechanism for determining foreign aid requirements; lack of clear strategy upon which the foreign resources can be coordinated for its effectiveness on the ground are anchored; inadequate capacity and mechanism for effective utilization of foreign resources such as ODA; and inadequate and unpredictable financing for economic development programs which is often compounded by lack of strategic prioritization.

It is therefore important to examine the role of foreign resources in the economic development of Tanzania, provided that government has adapted the outwards looking policies that have attracted more foreign resources to the economy. The analysis will provide an opportunity to establish whether external assistances have any significant role on economic development of Tanzania and thus pave the way for the formulation of a credible Foreign Aid Policy and strategies.

1.3 Objective of the Study

The broad objective of this study is to analyze the role of foreign resources in the economy by examining the consensus in the literature that foreign resources lead to better economic performance. External assistance is one of important sources of government revenues which accounts for about 40 percent of the national budget. Effective management of external assistance and use value of the resources for leading industries is important for growth and job creation. Specifically the study requires to: [1] Determine the level of domestic resources in Tanzania, [2], Identify the contribution of the policy reforms undertaken from 1990s to the effective use of foreign resources, [3] Identify how much external resources are needed to supplement domestic resource in the process of developing leading industry/primary industries which will stimulate rapid economic growth and spill-over effects; and [4] Identify any success story on outwards looking policies that attracted more foreign resources to the economy

1.4 Study Methodology

In view of the objectives of the study that followed from the terms of reference, three independent but complementary methodologies and activities have been used. These methodologies and activities are as follows; (i) Major desk study, (ii) Field survey and (iii) National consultative workshop.

1.4.1 Major Desk Study - Literature Review

Researchers undertook desk review of the current issues on the role of foreign resources in both developed and developing economies. All available relevant documents were reviewed, and this included reports of the central government ministries including President's Office, Planning Commission (POPC) and Ministry of Finance and Planning. Researchers also collected secondary data and information during literature review.

1.4.2 The Field Surveys

The research team has also carried field surveys at three levels. *The first level* focused on secondary data and information about current level, composition, institutional framework, and effectiveness of foreign resources in Tanzania. *The second level* has been field surveys which involved interviews with senior and top executive government officials from ministries, institutions and agencies that are beneficiaries of foreign resources. *The third level* has been field surveys focusing mainly on FDI. This involved consultative meetings and interviews with senior and top executives from multinational companies. The field research survey covered two regions of Tanzania mainland and Zanzibar. In Tanzania mainland field survey was carried in Dar es Salaam and Arusha. In both Zanzibar and Tanzania mainland a total sample of 120 people were targeted and randomly drawn. These people included senior and top government officials, business operators and experts in the area of foreign resource. Discussion with these key stakeholders provided useful data and information on the subject matter.

1.4.3 Caveats of the Study

Given the resource constraints in terms of time and financial resources, this study did not cover all regions of the Tanzania mainland and Zanzibar. Only few representative regions were selected in Tanzania Mainland and Zanzibar.

Chapter Two: Level of Domestic Resources in Tanzania

2.1. Introduction

The objective of Chapter Two is to analyze the level of domestic resources in Tanzania. This entails determining the amount of existing domestic resources and determining the extent of effectiveness and efficiency of use of domestic resources. The chapter will furthermore suggest ways of improving domestic resource mobilization and use in order to reduce dependency on foreign resources as a way of increasing control of formulation and implementation of policies geared towards economic and social development. It is worth noting that this chapter briefly identifies and examines the levels of domestic resources given the scope of this study.

2.2 Types and Levels of Domestic Resources

There are different types of domestic resources in Tanzania. These are natural, human and financial resources. Tanzania is one of the most natural resource endowed and rich country. Natural resources can be classified as minerals, land, livestock, and infrastructure such as hydroelectric power, gas pipelines, telecommunications and ports. The main financial domestic resources in Tanzania are savings and government tax revenue. Studies indicate that Tanzania has low domestic savings and government tax revenue ratios, (URT, Economic Surveys, (*various issues*)). All financial resources are in monetary terms but this does not mean that are the only domestic resources relevant in the country's social economic development. There are views that domestic resources are best utilized for achieving developmental goals when they have market exchange and use values and are conducive for optimal utilization. Non-financial domestic resources have to be analyzed in terms of economic values in monetary terms to get an idea of how they can be utilized to increase the domestic resource envelope.

2.2.1 Human Resources

Human resource constitute the total pool of human physical and mental labour available in the society engendering social, economic and political positive change; and for the production of private and public goods and services on which the survival and welfare of the people in that society depends. Human resource development is concerned with building skills and providing productive employment. It involves developing humans' physical and mental faculties so that a person is able to perceive, digest and articulate thoughts and ideas in a rational manner and is able to control and skillfully manage the different aspects of life and environment. Human resource is capable of transforming all the other resources for the betterment of its welfare. Thus, people are both the ends and the means of development. Table 2.1 and Table 2.2 show Tanzania's labour and employment situation and employment by sector respectively.

The 2002 Tanzania Census revealed a population of 34,569,232 with an average annual growth over the last few years of 2- 3 percent. The population of Tanzania in 2008 was estimated at 41,048,532. Tanzania population has increased slowly at 2.04 percent in recent decades. About 25 percent live in urban areas and rate of urbanization has been about 4.2 percent during 2005-8.

Table 2.1 shows that the labour force in Tanzania has 20.6 million active people with 2.3 million o those being unemployed to make up an unemployment rate of 11.1 percent. Table 2.2 shows that the agricultural sector is the dominant employer of the labour force accounting for over 76 percent of total employment in Tanzania. Employment in agriculture however has slightly declined from 84 percent to 76 percent from 2000/01 to 2007/08.

This may suggest that people have been migrating from rural areas to urban areas, in search for new ways of life or livelihood social economic activities. The rural urban migration has been without an increasing agriculture labour productivity.

Agriculture, the backbone of the economy, continues to be dependent mainly or rainfall and on backward technology. Thus increasing population level, slow and variation economic growth implies that agricultural productivity is low and erratic. Also productivity level in other productive sectors has equally remained low. The available domestic human resources have not been adequately mobilized and effectively utilized to promote development on a robust and sustainable basis.

Current estimates suggest that unemployment level has increased to about 15.5 in 2008, mainly because of the increasing domestic constraints and global social economic crisis. Unemployment in urban areas increased from 10.6 percent (Standard/ILO definition) in 1991 to 14.8 percent (Standard). According to the National definition, urban unemployment in 2008 was 32 percent compared to 8.4 percent in rural areas, while Dar es Salaam had an unemployment rate of 45 percent. Many people are either underemployed or and available human resource is mostly unskilled and not productive. This low level of human resource productivity also reflects a low degree of creativity and innovativeness including the low level of utilization of science and technology.

Table 2.1 Labour and Employment in Tanzania

Population	41,048,532
Labour force	20,600,000
Employed	18,300,000
Unemployed	2,300,000
Unemployment	11.1%

Source: Integrated Labour Force Survey, 2005/6

Table 2.2: Employment by Sector, According to National Definition (percentage)

	2000/2001			2005/2006		
Sector	Male	Female	Total	Male	Female	Total
Central/Local Government	3.0	1.5	2.2	3.3	1.6	2.4
Parastatals	0.8	0.2	0.5	0.5	0.2	0.4
Informal Sectors	6.7	4.6	5.7	10.4	8.2	9.3
Other sectors	6.7	2.1	4.4	11.5	4.2	8.0
Agriculture	80.7	87.6	84.2	72.9	79.9	76.5
Domestic	2.1	4.1	3.1	1.4	5.5	3.5
Total	100	100	100	100	100	100

Source: Integrated Labour Force Survey, 2005/6

The fact that Tanzania has a large active labour force which is mobile in terms of being able to move between sectors and that unemployment is over 11 percent implies that there is adequate labour to go hand in hand with increased domestic resources mobilization. The capacity of transformed agriculture sector to employ adequate country's labour force creates a unique opportunity for expanding utilization of arable land for agriculture by taking advantage of the ample land resources and large labour force in responding to the current global economic crisis and food crisis. This suggests the need to promote a broad human development investment strategy which involves a wide range of players as well as a broad resources base which embraces public sector, individuals, families, communities and private sector firms.

2.3 Core Natural Resources

A country's natural resource endowment is potentially a significant source of economic development if adequate initiatives are taken to transform such potential to financial resources that are useful in implementing a country's development agenda. Thus having an abundant natural resource endowment is just a necessary condition for having a high domestic resource mobilization potential but adequate strategies must be in existent to turn such potential into increased domestic resources that can be utilized to implement a country's development initiatives. Tanzania's major natural resources are minerals, land, livestock, and fisheries.

2.3.1 Minerals

Table 2.3 and 2.4 show the deposits of major minerals in Tanzania and mineral exports respectively.

Table 2.3 shows Tanzania's mineral deposits while Table 2.5 shows the estimated values of some of mineral deposits. However since the main interest is to determine the country's earning potential from its existing deposits of minerals, we use the value and quantity of mineral exports for 2007 and the quantity of deposits for gold, diamonds and copper to estimate the value of the deposits. Table 2.5 shows the estimated value of existing gold, diamonds and copper deposits

Table 2.3: Deposits of Major Minerals in Tanzania

Nr	Type of Mineral Resource	Levels of Mineral Resources
1	Gold	2,222 Tonnes
2	Nickel	209 Million Tonnes
3	Copper	13.65 Million Tonnes
4	Iron Ore	103.0 Million Tonnes
5	Diamond	50.9 Million Carats
6	Tanzanite	12.60 Million Tonnes
7	Limestone	313 Million Tonnes
8	Soda Ash	109 Million Tonnes
9	Gypsum	3.0 Million Tonnes
10	Phosphate	577..04 Million Tonnes
11	Coal	911.0 Million Tonnes

Data Source Geological Survey of Tanzania, 2007

Table 2.4: Tanzania's Mineral Exports

Quantity Exported							Value ('000 US$)				
Type of Mineral	**Unit**	**2003**	**2004**	**2005**	**2006**	**2007**	**2003**	**2004**	**2005**	**2006**	**2007**
Diamonds (Rough)	000 Carats	2,899	4,341	220	272	283	31,860	33,680	25,350	25,913	28,913
Gold	000 Grams	27,390	32,690	52,172	39,750	40,095	504,140	596,620	643,640	786,400	762,900
Gemstones	000 Grams	6,465	7,280	1,936,618	2,493,211	10,902,213	19,050	26,890	40,530	10,256	35,582
Phosphate	Ton		42	6,613	2,881	8,261		520	638	275	715
Silver	000 Grams			12,891	14,906	12,381			2,990	5,540	5,317
Copper	0001b			7,633	7,242	7,222			12,620	19,896	21,063
Bauxite	Ton			1,850	5,373	4,700			30	51	571

Source: Ministry of Energy and Minerals, 2008

Table 2.5: Estimated Value of Mineral Deposits in Tanzania

Mineral	Estimated Value (US$)
Diamonds (Rough)	1,001,227,561.84
Gold	28,540,965,207.63
Copper	583,301,024.65

Source: Ministry of Energy and Minerals, 2008

Table 2.3 – 2.5 suggest that Tanzania is rich in mineral resources. Tanzania has become one of the fastest-emerging gold producers in Africa, and is now the continent's third-largest gold-producing country after South Africa and Ghana. Annual production of gold has increased from around 43.2 t in 2002 to about 48.0 t in 2003. Based on ongoing projects and developing mines, Tanzania's estimated gold reserves have been calculated at a conservative total of Tanzania now has proven gold reserves in excess of 36 Moz (1000 t) or valued at about US$ 28,540,965,207.63.

Consultations with stakeholders suggest that mining sector does not well linked to other domestic social economic activities and that majority Tanzanians are not benefiting from current mineral exploitations. The failure of the mining sector to create strong linkages with the domestic economy has led to the perception among Tanzanians that it has failed to have an impact on the development of the country because of being in the hands of very few people.

A good example cited by many respondents is the case of tanzanite in which Tanzania is the only supplier in the world and thus has a monopoly. The dominating opinion among respondents is that tanzanite has a very high domestic resource mobilization potential because of the fact that Tanzania has a monopoly position in the market. Tanzania is thus perceived to have squandered the potential of tanzanite to mobilize domestic resources by allowing large scale mining which has led to oversupply in the world market resulting in lower prices than would have been the case with small-scale mining. Furthermore, small-scale mining which is dominated with indigenous Tanzanians has richer linkages with the rest of the economy than foreign owned large-scale mining sector. This suggests that ownership and management of natural mineral resources are major factors for weak mining sector linkages.

The best way to enhance the mobilization of domestic resources through minerals is to ensure that as much value addition as possible in Tanzania before the minerals are exported as well as boosting linkages with the rest of the economy by ensuring that more goods and services used by the companies involved in mining activities are obtained from domestic firms. However initiatives to increase the use of goods and services from local firms should go hand in hand with measures to support local firms in order to make them more competitive in terms of being able to offer quality goods and services so that they can meet the demand of the firms consuming imported goods and services. Increasing the role of the domestic sector in supplying goods and services to foreign firms involved in the extraction of minerals in the country will reduce the trend of foreign investment inflow coming into the mining sector ending up abroad through payments for imported goods and services.

2.3.2 Land

Land is an important element in national development and in enhancing the capacity of the country to enhance mobilization of domestic resources because a majority of Tanzanians live in rural areas and depend on land for their livelihoods. Since agriculture is the largest contributor to the Gross Domestic Product in Tanzania, land is thus the key to reducing poverty in Tanzania since the majority of Tanzanians are involved in agriculture in one way or another.

Land is an important factor of agriculture production in Tanzania and thereby its increased use can result in increased incomes for the farmers and other people using it. Increased income from agriculture resulting from increased land use will most likely translate to increased domestic resources in the country through linkages with the rest of the domestic economy, financial sector and government revenue. Table 2.6 shows land resources in Tanzania and its distribution by use

Table 2.6: Land Resources and Distribution in Tanzania

Total Surface Area	94,300,000 ha
Reserves	22,000,000 ha
National parks	4,200,000 ha
Game Reserves	7,700,000 ha
Forest Reserves	10,100,000 ha
Total Arable Land	15,100,000 ha
Gross area cultivated/planted annually	5,100,000 ha
Uncultivated Arable land	10,000,000 ha
Cultivatable Land in Reserves	4,000,000 ha

Source: Tanzania National Website, 2009

Table 2.6 shows that out of the arable land Tanzania has, it only uses about a third of it for cultivation with the other two thirds being idle. Tanzania thus is richly endowed with land which however is underutilized. However the fact that Tanzania is only using a third of its arable land for cultivation implies there is still sufficient room for Tanzania to expand use of its land to improve agriculture production which can play a big role in enhancing domestic resource mobilization due to the massive number of people standing to benefit economically in agriculture.

The underutilization of arable land in Tanzania is due mostly to several reasons which are lack of capital to invest in agriculture, distorted market, poor productivity, and poor physical infrastructure in areas where the majority of the land is located. Consultations revealed that these land issues need to be addressed in order to motivate human resource to increase utilization of land resources. Measures to increase utilization of land resources in Tanzania should thus be geared towards easing credit constraints, developing and improving physical infrastructure, allowing operation of free market, improved extension services.

Easing of credit constraint and improvement of physical infrastructure will lower the cost of undertaking agriculture production activities while improved extension services in terms of coverage will increase productivity. Allowing the smooth operation of the free market especially when it comes to refraining from imposing export restrictions will result in increase in farmers' incomes. Export restrictions on export of agricultural crops though having good intentions tend to lower the incomes of farmers while favoring the purchasers of the crops who pay the farmers lower prices than they would have paid was the market open for export. Enhanced domestic resource mobilization can best be achieved by letting the market operate freely rather than by protecting local buyers who pay farmers low prices just because they are protected by export restrictions.

2.3.3 Livestock

Livestock is one of important animal resources. Others are wild life animals. Livestock is among the major agricultural sub-sectors in Tanzania. Out of the 4.9 million agricultural households, about 36% are keeping livestock (Njombe and Msanga, 2006). The industry accounted for 4 percent to total GDP in 2007 (Economic Survey, 2007). The livestock sub-sector has strong linkages in the Tanzanian economy as it contributes to national food supply and food security by producing meat, milk, eggs, and hides and skins and thus acts as a source of cash income and employment. Furthermore livestock is an inflation free store of value and provides manure and draught animal power and thus contributes to sustainable agriculture. Table 2.7 shows the levels of livestock in Tanzania in 2008

Table 2.7: Quantity of Livestock

Type	**Quantity**
Cattle	19,100,000
Goats	13,600,000
Sheep	3,600,000
Pigs	1,200,000
Chicken	30,000,000

Source: Ministry of Livestock Development, 2008

Table 2.7 reveals that Tanzania has quite a large livestock population which if used well can enhance the mobilization of domestic resources in the country. The fact that the livestock sub-sector is rich in linkages with the rest of the economy through various dimensions such as production of food, hides and skins, manure, draught animal power and acts as a store of value implies that it affects the lives of many people both directly and indirectly. Harnessing of the domestic resource mobilization potential of the livestock sub-sector should focus on creating an environment that is conducive for the utilization of the existing population of livestock in the country and increasing the population and quality of livestock in order to benefit more from the livestock sub-sector.

The best way to harness the domestic resource mobilization of livestock in the country is to improve the quality of the livestock through improvement in breeds, research, emphasis on livestock management, and improved veterinary services which the government has begun to undertake. However although these quality improvement measures are being considered, they are being impeded by lack of resources in executing them implying that their implementation may take too long to have a significant impact on improving the quality of livestock in the country. There is thus the need to increase flow of resources into the livestock sub-sector on the grounds that it has strong linkages to the rest of the economy and will improve the livelihoods of many Tanzanians.

Hide and skins are the major foreign exchange earner from the livestock sub-sector in Tanzania but their production is impeded by poor quality of hides and skin caused by defects in each stage of processing. This problem can be addressed by emphasizing damage control as early as possible in the value chain in order to detect poor quality hides and skins and preventing them from entering the market by more efficient use of the proceeds of the export levy.

Processing, marketing and consumption of quality meat, and meat products has the potential to improve domestic resource mobilization. However, it is impeded by such factors as inconsistent supply of quality animals, inadequate market information, inadequate research and training in meat technology, low awareness of consumers on meat quality and lack of capital for investment in meat processing plants. Such problems have led some commercial companies to import meat and meat products into the country to supply to niche markets in tourist hotels, supermarkets and mining centres and thereby diminishing the capacity of the livestock sub-sector to contribute to improved domestic resource mobilization. In light of these problems, the strategy for enhancing processing, marketing and consumption is emphasizing quality improvement through collaboration with other stakeholders in promoting processing, marketing and consumption of quality meat and meat products in order to meet nutritional requirements and increase exports.

2.4 Other natural resources

Tanzania is endowed with other significant and rich natural resources, which include forests, woodlands, wild animals, rivers, lakes and wetlands. This section briefly presents some of these natural resources.

2.4.1 Water

Tanzania is a coastal state on the West Indian Ocean and shares three of most important inland lakes in Africa. Lake Victoria (Tanzania, Kenya and Uganda) the second largest fresh water lake in the world, with a total area of 68,800 km2 with Tanzania occupying 51% which is 35,088 km2. Lake Tanganyika (Tanzania, Burundi, DRC and Zambia) the second deepest lake in the world, has a total area of 32,900 km2 in which Tanzania has 13,489 km2. Lake Nyasa (Tanzania, Malawi and Mozambique) has a total surface area of 30,800 km2, in which Tanzanian share is 5,760 km2. There are also some small lakes and dams like Lake Rukwa, Lake Manyara, Lake Eyasi and Lake Natron, Mtera and Nyumba ya Mungu dams which cover more than 7% of the land surface. The Exclusive Economic Zone (EEZ) is estimated to be 223,000 km2 and the total coastline is 1,450 kilometers long.

Safe water is essential for resolving poverty and health problems. The poor, who mostly live in rural areas, have limited access to clean water for domestic use, crops and sanitation. Water-related diseases account for over half of the diseases affecting the population, and more than 80% of Tanzania's population. The government aims for a sustainable rural water supply, but consider these problems: one-third of Tanzania receives less than 800mm of rainfall, and is arid or semi-arid. Only one-third of the country has rainfall above 1000mm. There is a long dry season, running from June to October.

By 2008, only 47.5% of the rural population, and 70% of the urban population had access to clean and safe water. The demands for domestic water supply cannot be met by the government alone, so private investment is strongly encouraged for water development. This is one of Tanzania's greatest growth potentials. Ground water is a major source of water for many in Tanzania, and is the most viable alternative in the central and northern areas of the country. Consultations revealed that Tanzania is very rich in terms of water resources, but these resources have not been effectively utilized to change our style of life and living standards. The public is aware of the importance of water as an important factor of agriculture production, but there are effective water management and utilization for sustainable agriculture development.

Fishery resources

Tanzania is a coastal nation endowed with fishery resources, of both marine and inland. The marine water covers 64,000 square kilometres which includes the Indian Ocean and the Exclusive Economic Zone which covers 223,000 square kilometres. The fresh water includes the riparian shared waters of East African great lakes namely Lake Victoria, Tanganyika and Nyasa. The country has also other small natural lakes, man made lakes, river systems and many wetlands with fish potential. All these waters cover 58,000 square kilometres. The country has coastline of about 800 km declared as its Exclusion Economic Zone but has not yet been exploited. The present annual fish catch is about 350,000 metric tons.

The fishery potential of Tanzania is estimated to 730,000 metric tons (Table 1) based on a stock assessment survey carried out in the early eighties. The estimate covers only the territorial waters and there has never been stock assessment carried out in the Exclusive Economic Zone. Therefore, the estimated stock may not represent the actual status of the present resource

The fishery in Tanzania is multi-species, which include mackerels, king fish, scavengers, parrot fish, sardines, rabbit fish, rays, sharks, and crustaceans from marine waters. Lates niloticus, Tilapia species and Restrionebola argentae are the most common species from fresh waters. The main commercial species are Lates niloticus for freshwaters and Prawns, Octopus, Lobster, Crabs and Tuna like species from marine waters.

The number of fishermen who are permanently employed is 80,000 and few others obtain their livelihood from the sector by being employed in the fishing and fishery related activities. The artisan fishermen produce about 90% of the total fish catch in the country; only 10% is derived from industrial fishing. Most of the fish caught is consumed locally while Nile perch, sardines and prawns are for exports. Fishing contributes about one third of the animal protein or 30% of the total intake to the Tanzanian population. It is a source of employment, livelihood to the people, recreation, and tourism in order to generate foreign exchange. The contribution of the sector to GDP for the past five years has been staggering between 1.6 and 3.1%.

In 1997, the Government adopted the National Fisheries Sector Policy and Strategy Statement. Its main objective is to promote conservation, development and sustainable management of fisheries resources for present and future generations. The strategies of the National Fisheries Policy are based on the overall objectives of the government, which aim at poverty reduction, creation of employment opportunities, increased food security, increased economic growth and sound environmental management.

2.4.2 Forestry Resources

Forestry resources are, in essence, forestry assets. Economists define an asset as that which is owned and has a monetary value. Extending this definition to forestry, assets include land occupied by, or proclaimed to be forest, the produce found in such land, and the incommensurable human resources capable of fostering the development of such resources.

Wetlands cover a range of inland, coastal and marine habitats which share a number of common features. The range of wetland habitats which come under the mandate of the Ramsar Convention on Wetlands of International Importance especially as Wildfowl Habitat is impressive. Crude grouping of habitat types according to their basic biological and physical characteristics gives 30 categories of natural and 9 of man-made wetlands. In this report, only landscape units which are wetlands, or where wetlands form an important component, are considered; these are estuaries, open coasts, coastal forest wetlands, floodplains, lakes, freshwater marshes, peat-lands, swamp forests, and groundwater forests.

Wetlands have standing water for at least part of the year. This leads to the view that they are wastelands and that they should be filled in or drained so that they could be put to better use. Recently, informed public opinion and land and water management agencies of governments, notably in the United States, have taken the view that the world's remaining wetlands are more useful in preventing floods, recharging groundwater, controlling pollution and providing habitats and breeding grounds for fish and wildlife (Botts, 1982).

A significant amount of Tanzania's rice is obtained from the floodplains located in Mwanza, Shinyanga, Tabora, Mbeya, Morogoro and Coast Regions. The Wembere, Bahi and Malagarasi Swamps are important sources of fish. Estuaries, such as those of the Rufiji, Wami and Ruvuma Rivers and other coastal wetlands, are among the most productive environments in the world, acting as nurseries for valuable fisheries. Mangrove roots and branches diminish the effects of ocean waves and reduce beach erosion. The Kilombero and Kagera Swamps produce a significant proportion of Tanzania's sugar. In Iringa Region,Mbuga Swamps mitigate floods by retaining water and allowing groundwater recharge. The trapping of sediment by wetlands influences the output of hydroelectricity and the maintenance of riparian ecosystems downstream.

The swamps bordering the Malagarasi River playa significant role in the maintenance of biodiversity within Lake Tanganyika which contains one of the largest faunas (in terms of species) of any lake in the world. Over 1,300 species of invertebrates have been described from Lake Tanganyika, of which well over 500 are endemic. Distinct and diverse communities exist in the pelagic, benthic, and littoral biotopes (Cohen, 1991; Coulter, 1991). Lake Tanganyika is a rare natural laboratory where ecological, biological, behavioural and evolutionary mechanisms can be studied (Lowe-McConnell, 1991). The trapping of sediment resulting from deforestation of the lake's catchments, is a significant contribution of wetlands to the maintenance of the lake's biodiversity. The shores of the Rift Valley lakes provide excellent habitats for birds; flamingos are found in Lake Manyara, which is a major attraction to bird watchers in Tanzania. Mangrove vegetation, found in estuaries, provides feeding, roosting and breeding sites for birds.

It is difficult to assign a monetary value to the wetland attributes outlined above. As a part of on ecosystem, a wetland provides many functions that act together to increase its value. Tanzanian wetlands have value for agriculture, fisheries, wildlife, maintenance of biodiversity, and flood control. Considered as a biological system, rather than in terms of separate benefits, the ecosystem approach must be pursued in an effort to secure understanding of the complex interrelationships found in wetlands.

The Future of Tanzania's Wetlands

The following functions are attributed to Tanzania's wetlands:

1. The wetlands on water catchments are involved in flood prevention, recharging ground water, controlling sedimentation and pollution and maintaining biodiversity.
2. Wetlands are important food sources (rice, sugar), breeding grounds for fish, wildlife and commercially important invertebrates.
3. A majority of landscape units serve as sources of forest products many of which lead to small scale industries such as soap making, carpentry, mat making, and wine tapping.

4. They may be sources of plants useful for agro forestry and phytoreclamation, such as Mimosa pudica, 'Mtanga', and Tamarix sp.
5. Certain wetland vegetation types, such as the mangroves, are effective in the prevention of shore and beach erosion.
6. Wetlands are genetic warehouses; wild relatives of domesticated plants may be used in conferring resistance against disease.

The list is by no means exhaustive. Resource conservation in some of the wetlands needs improvement. Given the multi-utility perspective of wetlands and their diversity in structure, it is not possible to adopt a single conservation strategy. The only safeguard seems to be to prepare a list of uses and functions of wetlands and then let each use form the basis of a conservation programme. What has been recommended is the ecosystem approach to conservation incorporating the preservation of genetic and ecological diversity with scientific research, environmental monitoring, education and training. Most of the facets of Tanzania's flora and fauna have unique characteristics but these are not widely known by the Tanzanian community. Increasing public awareness of such characteristics needs to be strengthened so that this may guarantee their long term protection.

2.5 Financial Resources

The financial sector is important in any economy because it performs the function financial intermediation whereby it mobilizes savings from economic agents with surplus resources and allocating such savings to economic agents with deficit resources. An efficient and effective financial sector which does the job of financial intermediation well thus plays a pivotal role in domestic resource mobilization in a country and thus should be supported in terms facilitating its smooth functioning (Senbet and Otchere, 2005). Since the core function of a country's financial sector is intermediation of resources by linking surplus spending economic agents and deficit spending economic agents so that an economy's resources are put to optimal use instead being left idle while an economy turns to foreign resources to fill the domestic resource gap.

2.5.1 Private Financing

An efficient financial sector is evaluated based on two major benchmarks, namely its ability to mobilize resources from surplus spending economic agents through the use of existing instruments and introduction of new instruments and its ability to allocate resources efficiently to deficit spending economic agents once it has mobilized the resources. Efficient allocation of mobilized resources by the financial sector to deficit spending economic agents imply that the allocation of such mobilized resources should be directed towards deficit spending economic agents with investment needs with good potential in terms of profits and activities with abundant linkages in the domestic economy (Mishkin, 2008).

Table 2.8: Commercial Bank Deposits (Tshs. Million)

	2004	2005	2006	2007	2008	Growth
Demand deposits	595,622	793,920	942,660	1,106,663	1305862	118%
Time Deposits	269,133	328,711	455,180	517,776	569553.6	110%
Saving Deposits	401,130	508,964	691,508	864,118	1391230	161%
Foreign deposits	746,609	899,976	1,353,523	1,651,819	2560319	155%
Total	2,012,494	2,531,571	3,442,871	4,140,376	5755123	139%

Source: Economic Survey, 2007 and ERB estimates

Directing financial resources towards economic agents with great potential of making profits and engaging in activities with abundant linkages in the economy has the advantage of making the financial sector sustainable because such pattern of resource allocation leads to further mobilization of resources in the economy and enhanced domestic resource mobilization in general.

It is known that the financial sector of a country is potentially an important source of domestic resource mobilization in Tanzania; however the issue of determining the extent to which such potential is being harnessed by the country warrants a closer look at the country's financial sector deposits and lending. Table 2.8 shows commercial bank deposits in Tanzania.

Table 2.8 shows that that commercial bank deposits registered big increases between 2003 and 2007 with a 139 % increase in total deposits and savings deposits registering the largest increase of 161 %. The fact that total deposits in Tanzania have doubled in just five years implies that the financial sector in Tanzania is doing a good job in mobilizing resources from surplus spending economic agents. Furthermore such a promising trend of resource mobilization shows that Tanzania has plenty of domestic resources which can still be mobilized.

Table 2.9 Commercial Bank Lending in Tanzania (Tshs Million)

Allocation	2003	2004	2005	2006	2007	Growth
Private Sector	658524.6	965985.8	1219305.6	1,658,843.7	2,261,597.2	243%
Treasury Bills	190446.1	205111.9	183632.9	440,011.6	1,182,403.9	521%
Government Stocks and Treasury Notes	156719.9	170388.1	222357.5	297,056.6	346,136.8	121%
Total Government Securities	347166.0	375500.0	405990.4	737,068.2	1,528,540.7	340%
Total	1,005,690.6	1341485.8	1625296.0	2,395,911.9	3,790,137.9	277%

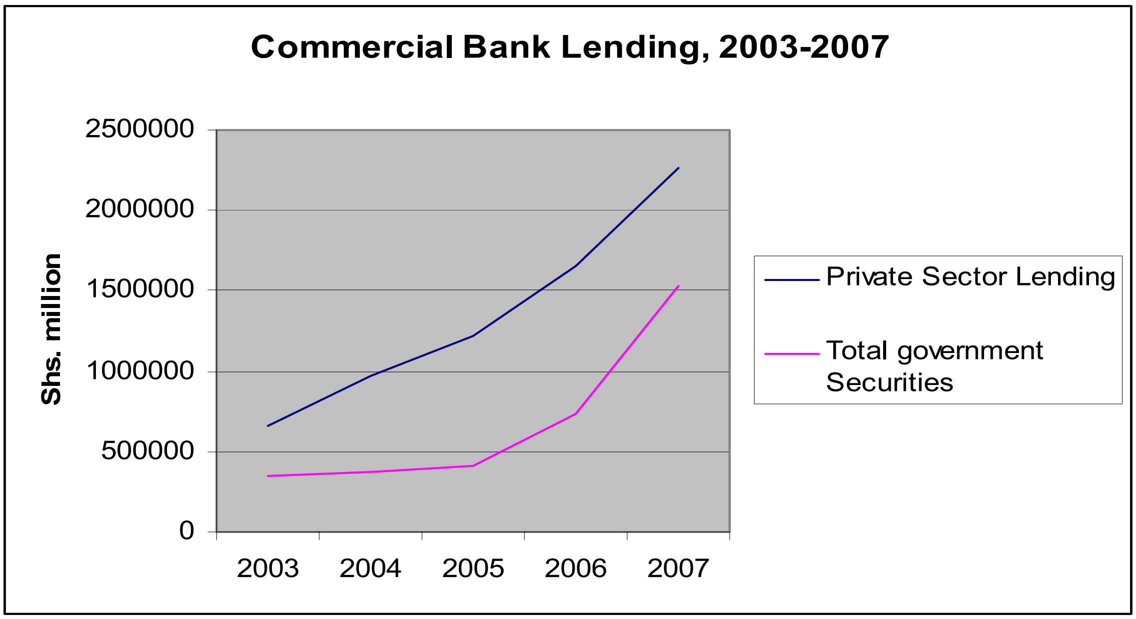
Source: Economic Survey, 2005, 2007 and calculations

The satisfactory increase in mobilization of savings from surplus spending economic agents points to the fact that the financial sector in Tanzania is performing efficiently in the first dimension of financial intermediation. However, in order to determine whether the financial sector is performing efficiently overall, there is a need analyze the other dimension of financial intermediation which is the allocation of mobilized resources. Table 2.9 shows the allocation of resources in terms of commercial bank lending in Tanzania. According to this table the total commercial bank lending grew by 277 percent between 2003 and 2007 with private sector lending growing by 243 percent while total government lending in terms of government securities grew by 340.3 percent. Sale of treasury bills grew by a staggering 521 percent in the same period of time. Fig. 2.1 shows the trend of commercial bank lending to the private sector relative to the government between 2003 and 2007.

Fig. 2.1 shows that although private sector lending is higher than government lending, the latter has been rising at a greater rate than the latter implying that public sector borrowing is rising in Tanzania at the expense of the private sector thereby leading to crowding out of the private sector in the credit market. Such a situation is not consistent with the notion of earmarking the private sector as the engine of development in the economy. Furthermore, increased government borrowing implies that it is not mobilizing enough domestic revenue in terms of taxes to finance its expenditures while impeding the private sector from enhancing domestic resource mobilization at the same time by crowding it out of the credit market.

The trend of financial sector lending in Tanzania is tilted towards the public sector at the expense of the private sector. This is the result of financial institutions perceiving most private sector players as being risky and thus not being worth taking the risk on. Most financial institutions thus end up taking the easy path by purchasing government securities which are risk free and offer good interest rates. The financial sector in Tanzania seems to be intent on restricting credit to the private sector as it tends to charge unreasonably high interest rates on loans which usually range between 17 percent and 20 percent which are quite prohibitive for the private sector. It is thus safe to conclude that the financial sector in Tanzania has been inefficient in allocating resources to areas where such resources can be used optimally but rather prefers to allocate resources to the government which is no longer the engine of growth of the economy.

Fig 2.1: Commercial Bank Lending



Source: Study using Data from TRA

The fact that financial sector lending is tilted towards public sector lending is a result of the fact that the Tanzanian government has high demand for credit because of its high expenditure requirements meaning that it provides a lending alternative to a financial sector that has an aversion of lending to the private sector. In other words the actions of the Tanzanian government encourage the country's financial sector to continue to refrain from allocating credit to the private sector. This being the case, the best way for the government to encourage the financial sector to increase domestic resource mobilization through increased private sector credit allocation is to reduce its expenditure in order to deprive the financial sector of an alternative to lending to the private sector. This would compel the financial sector to view the private sector as a destination for directing its excess deposits rather than continue holding the deposits in an irrational manner. Another way of improving lending systems to support direct investment is by supporting initiatives to minimize risks in borrowing increase access to micro financing.

2.5.2 Public Sector Financing

The amount and efficiency of government spending is an essential part of making domestic resources and engine for the development of an economy. The public sector mobilizes resources through taxation and other forms of revenue generation.

Table 2.10: Trend of Government Finance in Tanzania

	2003/04 Actual	**2004/205 Actual**	**2005/06 Actual**	**2006/07 Actual**
A. DOMESTIC REVENUE	1459303	1773710	2124844	2739022
1. Tax Revenue	1342798	1615248	1946433	2529439
Import Duty and Excise Duty	352320	350532	452406	765644
Sales Tax(local & imports)	0	0	0	0
Value Added Tax(VAT)	548572	731597	845790	861050
Imports	315958	439796	502437.3	431614
Domestic	232614	291801	343353	429436
Income Tax	366651	465455	581244	790877
Other Taxes	123500	132040	136954	218581
Refunds accounts	-48245	-64376	-69961	-106713
2. Non Tax Revenue	116505	158462	178411	209583
B.TOTAL EXPENDITURE	2516943	3248352	3972608	4474680
1. Recurrent Expenditure	1780115	2017490	2661863	3137469
2.Development Expenditure	736828	1230862	1310745	1337211
Local Funds	133041	239651	296100	503291
Foreign Funds	603787	991211	1014645	833920
C. DEFICIT/SURPLUS(A-B)	-1057640	-1474642	-1847764	-1735658
D. FINANCING	1045883	1474642	1847764	1735660
1.External Sources	1053531	1416618	1604641	1689337
Grants	494889	992975	1043422	971547
Basket Support	94331	156745	82302	47331
Import support/OGL Loans	0	65396	257677	266946
Project Loans	509456	308592	328956	433203
Amortization(foreign)	-45145	-107090	-107716	-29690
2.Internal sources	-7648	58024	243123	46323
Non-Bank Borrowing	21357	144954	219241	212475
Bank Borrowing	0	0	129645	25533
Proceeds from privatization	9767	0	33309	0
Payment of arrears	0	0	0	0
NBC bonds	0	0	0	0
Recapitalization	0	0	0	0
Adjustment to cash	50776	53211	37104	-60370
Amortization(local)	0	0	-19001	0
Expenditure float	-89548	-140141	-157174	-131315

Source: Economic Survey, 2008

Tax revenue is a major domestic financial resource in all economies. Indeed taxes account for most of government revenue in the majority of African countries, but they do not generate enough, particularly when compared to other regions (Aryeetey, 2008). The efficiency of public sector resources is analyzed in the context of domestic resource mobilization through the amount of revenue collected and the expenditure pattern. Table 2.10 shows the trend of Government finance in Tanzania.

Table 2.10 reveals that although Government revenue rose consistently between 2003/04 and 2006/7, expenditure also rose steadily in the same period. This table reveals that the increase in Government revenue in Tanzania has been accompanied by similar rise in expenditure thereby leading to an increase in the Government deficit. Furthermore, less than a third of Government is for development purposes with the rest being for recurrent purposes. The local contribution to the development budget is low at 37 % which implies that Government resources are directed mostly towards recurrent expenditure which has less impact on enhancing domestic resource mobilization than is the case for development. Increased budget deficits also lead to increased government borrowing which crowd out the private sector in the credit market and lowers the capacity to mobilize domestic resources.

2.6 Domestic Resource Gap

Once major potential avenues of increasing mobilization of domestic resources have been identified as has been done in the previous sections the next step is naturally to estimate the cost in domestic resources required in order to achieve Tanzania's development goals which are consistent with the Millennium Development Goals (MDGs). This will enable the determination of domestic resources required to complement the current resources which are neither sufficient nor stable enough to allow the full attainment of the first Millennium Development Goals by 2015 (UNCTAD, 2006; UNECA, 2006). The need for additional resources in Africa is generally believed to amount to between 10 and 20 percent of GDP (UNECA, 2005; UNECA, 2006). CFA (2005) projects that low-income country in Africa, after allowing for constraints on absorptive capacity, need additional resources of $37.5 billion per annum in public expenditures until 2010. One-third of this would come from domestic resources and $25 billion from aid.

2.6.1 Estimation of Tanzania's Domestic Resource Gap

Estimation of Tanzania's domestic resource gap is based on the assumption of African countries needing additional resources of between 10 and 20 percent of GDP (UNECA, 2005a; UNECA, 2006) and assumption that a third of additional resources should be domestic (CFA, 2005). The Tanzanian 2007 GDP figure of Shs. 13.8 trillion and additional resource requirement of 20 percent of GDP are used as a basis for the calculations. Table 2.11 shows the results of the calculations and the resource gaps.

Table 2.11: Tanzania's Resource Gaps (Tshs. Million)

GDP	Total Resource Gap	Domestic Resource Gap
13,801,921	2,760,384.2	910,926.8

Source: Study Calculations

Calculations from Table 2.11 show that Tanzania's total resource gap is 2.76 trillion shillings annually of which 910.9 billion shillings must come from domestic resource mobilization annually. However, the total resource gap is dynamic and not static in the sense that efficient utilization of resources in activities with widespread economic linkages makes domestic resource mobilization more sustainable and leads to decreased need for foreign resources. This being the case, increased efficiency in allocation of government resources and financial sector resources as well as improved exploitation of natural resources will lead to reduced reliance on foreign resources and will reduce the total resource gap even further.

2.8 Level of Misused Resources

Resources which are budgeted for by a government are intended to be used for specified purposes in order achieve efficient and effective use of such resources as regards outputs. This being the case, the misuse of resources which are allocated in the budget in terms of misallocation or in a non-procedural fashion will undoubtedly lead to sub-optimal outcomes that fail to achieve value for money in resource use.

The best national indicator of misuse of resources in the country can be obtained from the Annual General Report of the Controller and Auditor General which shows the extent of misstated transactions as a percentage of total central government expenditure. Misstated transactions include such issues as outstanding bank reconciliation items, unretired imprests, difference of arrears of revenues reported, questionable payments, deferred payments, unvouched expenditures, improperly vouched expenditures just to mention a few. Table 2.12 shows the level of misstated transactions for the fiscal year 2007/08.

Table 2.12: Misstated Transactions

Total Misstatement	370,545,506,566
Total Actual Expenditure	5,017,378,196,000
Percent of Misstated Transactions and Balances	7%

Source: National Audit Office, 2009

Table 2.12 shows that total misstatements for fiscal year 2007/08 was 7 percent which far exceeded the pre-set materiality level of the National Audit Office for the current year of 2 percent. Given the pre-set materiality level of 2 percent the accepted total misstatement should have been about 100 billion shillings. This implies that an excess 270 billion shillings over the accepted amount has been misused. This amount is significant and results in inefficiency in achieving objectives of resource allocation.

2.7 Perceptions and Feelings on Domestic Resources in Tanzania

2.7.1 Domestic resources

ERB Survey (2009) from selected region on the type of domestic natural resources, points land and water bodies, minerals, livestock and other resource such as national packs, heritage sites, game reserves etc as the main types of domestic resource in Tanzania. Table 2.12 below shows these types of resources. According to this table land and water bodies is mostly pronounced as key resource in Tanzania (43.89 percent), followed by minerals 22.21 percent, livestock (12.19 percent) and other resource 21.70 percent.

Table 2.12 Main Domestic (natural) Resources in Tanzania

Resource	Percentage
Land and water bodies	43.89
Minerals	22.21
Livestock	12.19
Other resources (reserves, national packs, forest etc)	21.70

Source: ERB –POPC survey 2009

Given data and information discussed above, it is obvious that Tanzania is blessed with natural attractions and the vast size of the country (land) provide tremendous opportunities for developing and promoting different tourist activities, ranging from game viewing and hunting safari to beach holiday activities, mountain climbing, gliding, sight seeing, and photographic safaris. Equally, the country has both marine and inland fisheries potential. The country has also other small natural lakes, man made lakes, river systems and many wetlands with fish potential to mention a few.

2.7.2 Domestic resource price levels

In assessing views of stakeholders on the price levels of various domestic resources, the study presents the findings in table 2.13. According to this table stakeholders have the opinion that the price levels are low for almost all domestic resources. About 70 percent of respondents finds land price to be low and only 7.6 percent assume the price to be high. It is true that land price in Tanzania has been rising, but relatively low to other EAC member states. This could partly explain massive amount of unutilized land in Tanzania. Another reason for relatively low prices of resources in Tanzania is the fact that a resource such as land is not adequately formalized and hence it cannot be used to access credit implying it has low value. Distorted markets and lack of entrepreneurial skills required to take advantage of existing resources impact peoples' perception of the value of such resources negatively.

Table 2.13 Price levels of domestic / natural resources

Type of resource/Price level	V. Low	Low	Moderate	High	V. High
Land and water bodies	53.8	15.4	23.1	3.8	3.8
Minerals	40.4	17	31.9	8.5	2.1
Livestock	44.1	11.8	5.9	26.5	11.8
Other resources	33.3	20.8	20.8	16.7	8.3

Source: ERB- POPC survey 2009

It is argued that large part of fertile land is not utilized in productive economic activities. This means with proper technology and other franking measures in agriculture sector, Tanzania would become a net food exporter. With on going global food crisis proper exploitation of the land should force land price up. This is not much forthcoming an indication of not realizing this window of opportunity.

2.7.3 Level of understanding on ownership and control of national resources

This study also wanted to know the level of understanding in terms of data and information of natural resource in the country. Ideally, the study explores the extent to which Tanzanian communities are aware of how much, where and who own the national resource. Table 2.14 below shows the response of the survey in this regard.

Table 2.14 Understanding of ownership and control of major natural resources

Type of resource/Price level	V. Low	Low	Moderate	High	V. High
Land and water bodies	57.6	27.3	6.1	3	6.1
Minerals	42.1	34.2	2.6	13.2	7.9
Other resources (Reserves, national packs, forest etc)	66.7	33.3	0	0	0

Source: ERB- POPC survey 2009

Table 2.14 shows that the majority of respondents have no data and information on the ownership and control of resource. About 57.6 percent and 42.1 percent suggest having very little information and data on land and minerals resources in the country. This means special campaign to promote and create awareness is essential for proper management of natural resource and sustainable use.

2.7.4 Domestic Resources Sufficiency versus Foreign resource Dependency

The study also examined the perception of people regarding whether domestic resource is sufficient to break dependency on foreign resource. Table 2.15 below indicates the response of the survey. According to this table 49.5 percent of respondents find that domestic resource is sufficient to break Tanzania dependency on foreign resource. In contrast 50.5 percent finds domestic resource is not sufficient to break Tanzania dependency on foreign resource. This means despite abundance in domestic resource, there still syndrome on donor/ foreign dependency. Majority of Tanzanian do not have confidence to exclusively depend on domestic resource.

2.7.5 Public perceptions on the use of domestic resource

Development has generally been characterized by increasing dependence on foreign aid with low level of mobilization of domestic natural, human and financial resources to produce wealth and to raise the standards of living of the people. The study examined what policy measures are to be taken to reduce Tanzania dependency on foreign resource and optimize use of domestic resources

The mobilization and effective utilization of domestic resources (natural, financial and human) is the foundation on which the realization of the Tanzania Development Vision 2025 rests. These resources should be utilized to build adaptive capacity for promoting economic activities that enjoy comparative and competitive advantages with a view to minimize the impact of external economic shifts and shocks. Table 2.15 summarizes the perceptions on what could be done for Tanzania to enhance optimal utilization of domestic resources.

Table 2.15 General recommendations on the optimal utilization of domestic resource

Recommendation	Percentage
Promote investment in Human Resource	15.16
Improve management of resource	59.50
Promote local participation	15.30
Proper mechanism to determine value of national resources.	10.04

Source: ERB- POPC survey 2009

Table 2.15 shows that 59.50 percent suggest improvement in management of national resource. This entails proper taxation system of the natural resources, proper ownership and management systems, the need to take into account the interests of stakeholders at levels, and efficient investment incentive package for domestic investment efforts. Moreover, 15.16 percent and 15.30 percent argue for promoting investment in human resource through proper training and promotion of local participation respectively. Finally, 10.04 percent suggest for proper mechanism to determine value, quality and quantity of national resources. It is widely accepted that optimal utilization of domestic resources is everybody's responsibility. The roles of the government institutions are to assist Tanzanians to become aware of their own situation and support them to become responsible for their own destiny. Important is policy formulation, setting regulatory and institutional framework and promotion of education programmes on ownership, management and use of domestic resources. Furthermore, the government will be responsible with timely provision, updating generation and dissemination of accurate information related with domestic natural and human resources.

2.8 Main Domestic Resource Issues

2.8.1 High Levels of Domestic Resources

Tanzania has high levels of domestic resources such as human resources, minerals, land, water, fisheries, and financial resources which offer a strong potential to increase domestic resource mobilization in the country. However, this potential has not been utilized so far and if it is to be utilized there could be a significant increase in domestic resource mobilization which can lead to reduced dependency on foreign resources and eventually lead to more flexibility in undertaking the country's development agenda in terms of increased policy space. Tanzania is only utilizing a third of its arable land for cultivation with the rest being idle due to several complex problems and constraints such as lack of capital to invest in agriculture, distorted market, poor productivity, and poor physical infrastructure in most of the geographical areas where the land is located.

2.8.2 Performance of Financial Sector in Resource Mobilization

Commercial bank deposits and lending in Tanzania have increased significantly over the past several years with the former increasing by 139 percent and the latter increasing by 277 percent between 2003 and 2007 implying that the financial sector has done a good job in mobilizing resources. Although the financial sector has done a good job in mobilizing in terms of increasing levels of deposits, it has not been very efficient in allocating resources in terms of lending. The financial sector has thus been inefficient in allocating the savings it mobilizes as private sector lending growing by 243 percent while total government lending in terms of government securities grew by 340.3 percent between 2003 and 2007 with the sale of Treasury bills growing by a huge 521 percent in the same period of time.

2.8.3 Crowding Out of Private Sector in Borrowing Market

Although private sector lending has increased in Tanzania over the past couple of years, total government lending has been growing faster with the latter growing faster by almost 100 percent more than the former between 2003 and 2007. Higher growth of government lending relative to private sector lending implies that the Government is borrowing at the expense of the private sector and is therefore crowding out the private sector in the credit markets. The fact that financial sector lending is tilted towards government lending implies that the financial sector perceives lending to the Government especially in terms of Treasury Bills to be a less risky undertaking than lending to the private sector hence resulting in banks willing to sit on excess deposits rather than lend to the private sector.

Financial institutions tendency to tilt their lending towards the Government at the expense of the private sector is perpetuated by increased rise in government expenditure which has outstripped increases in revenue collection and hence leading to growing budget deficits that can only be financed through borrowing from the financial sector.

2.8.4 Wide Resource Gap and Misused Resources

Working under the assumption that African countries need an additional resources between 10 percent to 20 percent of their GDPs and that a third of those additional resources should be domestic, the study assumes that Tanzania additional resource requirement are 20 percent of GDP, the study finds that the total resource gap is 2.76 trillion shillings annually of which 910.9 billion shillings must come from domestic resource mobilization.

Data from Annual General Report of the Controller and Auditor General for 2007/08 shows that the percentage of misstatements as a percentage of total government expenditure was 7 percent or 370 billion shillings which exceeded the pre-set materiality level of 2 percent for fiscal year 2007/08 by 5 percent or 270 billion shillings which is quite significant and results in inefficiency in achieving objectives of resource allocation.

2.9.5 Squandered and Missed Opportunities on Minerals

The failure of the mining sector to create strong linkages with the domestic economy has led to the perception among Tanzanians that it has failed to have an impact on the development of the country. A case in point being tanzanite of which Tanzania has a monopoly. The major perception is that although tanzanite has a high domestic resource mobilization potential because of the fact that Tanzania has a monopoly position in the market, it has squandered this opportunity by allowing large scale mining which has led to oversupply in the world market which has lowered prices more than would have been the case with small-scale mining.

Chapter Three: Contribution of the Policy Reforms

3.1. Introduction

This chapter identifies contributions of the policy reforms undertaken from mid-1980s to the effective use of foreign resources. This is done by analyzing main policy reforms, issues, implementation performances, problems, constraints and challenges. Invariably, the later chapters provide a more detailed review on selected sector specific policies in determining the role and impact of foreign resources to the economy. These policy reforms may refer to the policy processes, systems, guidelines and directives which govern foreign resource utilization. For example reformed investments, production and trade policies may help in the formation of effective systems and procedures with respect to the effective mobilizations and use of foreign resources in Tanzania.

There is a general thinking that contributions of policy reforms should have enhanced ownership, management, coordination, utilization, equality and efficiency and the promotion of transformational developments. Table 3.1 shows that about 53.0 percent of the population sample appreciated the significant contribution of reforms on mobilization of foreign resources more so in form of FDIs and ODAs in Tanzania. Also about 7.75 percent of respondents appreciated reforms' contributions in mobilizing foreign banks services and thus increasing the access to financial resources. However, few respondents about 2.9 percent argued that there are no significant contributions to the economy as the result of reforms. About 36.41 percent of the sample population was indifferent or not sure about the contributions of the policy reforms on the effective foreign resource use.

Table 3.1: Contribution of Policy Reforms on Mobilization of Foreign Resources

Responses	Frequency	Percent
More resources (FDI and ODAs)	55	52.97
Excessive exploitation of natural resources	3	2.87
Access to financial services- banks	8	7.75
Others, (Not Sure)	38	36.41
	104	100.00

Source: ERB-POPC Field Research Survey, 2009

Above data analysis suggests that Tanzanians are aware of the recent policy reforms and efforts. Many people have knowledge and information on the policy reform processes and their contributions. However, some are not well informed on the details, systems and mechanism. The government of Tanzania has made concerted efforts towards putting in place various short, medium and long term development policies. Section 3.2 reviews the general policy environment and contributions and Sections 3.3 to 3.5 provide first generation policy reforms, second generation reforms, sector specific national development policies and medium term poverty reduction strategies.

3.2. General policy environment

Tanzania has, in the past 15 years been undergoing social economic and political reforms, which have re-oriented the economy from a government-led to a private-sector-led one.

Tanzania has made significant progressive in the formulation, implementation and performances of social economic policies intending to empower Tanzanian in managing own social economic activities. The reforms and changes in policies have resulted in the shrinking of a formal public sector contribution, which used to be the main coordinator, generator, user and consumer of resources in the formal sector.

Having been guided by socialist policies since the late 1960s, re-orienting the economy has meant making deliberate effort to promote private sector development and liberal input and output competitive market systems. The first and second generation reforms that were pursued since early 1980s up to day will be examined and linked to optimal utilization of foreign resources in an open, liberal and private led Tanzanian economy. We propose to consider the first generation reforms occurring during 1985/6 – 1995/6 and the second generation policy reforms happening during 1996/7 – 2008/2009.

3.3. First Generation Policy Reforms

Since the mid 1980s, Tanzania has introduced a series of policy reforms intended to restore macroeconomic balance, stimulate economic growth and facilitate social and political development (URT, 1996 and Semboja, 2004). Experience with the first generation reforms in 1986 - 1996 suggests that private sector initiative and market-oriented economic systems propel higher growth rates than centrally planned economic systems. These broad based measures included the fiscal, liberalization of internal and external trade, the removal of restrictive tendencies, the liberalization of the foreign exchange market and the institution of a general policy environment, which is more favourable to private sector expansion, coordination and management of domestic resources.

Fiscal policy reforms had several dimensions. The government has established the Tanzania Revenue Authority (TRA), which has contributed to increased domestic financial mobilization through increased revenue collections. The government has increased control and cut expenditure using the cash budget system. Civil service and parastatal reform has curbed expenditure and raised revenue. Both measures have had a positive impact on increase financial resource allocation to the private sector.

Monetary policy has been strengthened by reorienting the objectives of the BoT to the achievement of low inflation, deregulating interest rates and by raising the reserve requirement ratio. Together the tightening of the fiscal and monetary stance has greatly improved macroeconomic stability, domestic as well as foreign financial resource mobilization.

Both fiscal and monetary measures have had immediate and short-term negative consequences for investment, production and trade. Fiscal restraints have reduced the government's ability to undertake high priority investments in the social sectors, such as education, health, water and in infrastructure. The cash budgeting system has reduced the ability of the government to effectively manage its long term development programs and especially its public investments. And tight monetary policy has resulted in high real interest rates and credit squeeze– reducing private sector investment opportunities.

Exchange rate adjustment and trade liberalization have increased the supply of foreign exchange and needed (imported) inputs into production. Exchange rate devaluation has increased the incentive to export and invest in exporting activities. The impact of these policies in the short- to medium-run has been mixed. The real exchange rate has appreciated since 1994 again raising the possibility that interest rates are too high.

More generally, while some firms have been able to exploit the opportunities arising from trade liberalization, others have suffered (sometimes fatally) from increased competition. Civil service and parastatal reform improved the efficiency of the public and private sectors in Tanzania. Yet it is clear that both policies have had adverse short-term effects on employment. The increased price (from near zero) of utilities and staple foods had negative effects on the poor.

Action on share ownership has taken the form of establishing the Capital Markets and Securities Authority in 1994 leading to the establishment of the Dar es Salaam Stock Exchange in 1998 and adopting the Privatization Trust Fund Act in 1997. The DSE is still narrow with 15 companies listed of which only 4 are cross listed and the Privatization Trust Fund is not yet operational.

The country has shifted from its previous reliance on control mechanisms to a predominantly competitive market-oriented environment and private enterprise development as a result of these outward looking policy reforms. Significant progress has been made with the development of a more market-oriented financial system with the liberalization of interest rates. A substantial number of both local and foreign banks and non-banking institutions have been established to provide short, medium and long-term loans to the private sector. This has allowed increased assess and utilization of domestic resources over time.

3.3.1. Positive macro-economic performances

There are many people who argue that the overall impact of these first generation reforms on the development has been significantly positive. Tanzania has recorded significant improvement in overall macroeconomic performance since the mid 1980s largely on account of sustained policy actions on stabilization and structural adjustment.

Monetary policy has continued to focus on maintaining low and stable inflation, to ensure macroeconomic stability in support of the broader macroeconomic objectives of Government, by maintaining an appropriate level of liquidity in the economy, through a combination of open market and foreign exchange market operations, (URT, 2005b). The annual inflation rate continued to decrease and low. During the 1985/6 and 1995/6 fiscal policy remained geared towards economic growth stimulation. On the revenue side, government tax reform efforts continued to produce positive results. The government revenue efforts increased. The strong government revenue performance has mainly been attributed to increase efficiency and effectiveness of the tax systems and administration.

3.3.2. Negative impacts

Despite those macroeconomic progresses, poverty levels and overdependence on foreign aid for development and recurrent expenditure remained as worrisome as ever and the medium-term strategy is to get out of much of it through development of a strong and expanded domestic revenue base. In the meantime, macroeconomic management is confounded by large foreign aid inflows, a tendency and fear for such effects as an appreciation of the real exchange rate and the crowding out of domestic savings, particularly so if aid is not used to strengthen the capacity of the economy to grow. The growth-effectiveness of foreign aid can be enhanced by easing absorptive capacity constraints in the economy and targeting reduction of aid that finances such recurrent expenditures as wages since these are not easy to scale back. To enhance growth and the revenue base aid can also be targeted to develop the private sector which is still small in

Tanzania. The continuing agenda on foreign aid delivery modalities remains crucial, but the most important thing is its effectiveness for growth, whichever modality.

3.4. Second Generation Reforms

Based on the experiences of implementation of first generation macro-reforms, the government has been conscious of the need for long term perspective development plans and has made a more comprehensive review of its micro-economic and sector policies to resolve fundamental problems, which are still inherent in the economy and to also ensure that the current interest by investors in the economy is enhanced and sustained. These second generation reforms have been underway and been implemented during this period 1996/7 and 2008/9. These second-generation reforms are still focusing on macro-micro linkages subject to intensification of first generation reforms in terms of continuation of fiscal, monetary, legal, regulatory and institutional reforms.

The second-generation reform policies aim at facilitating ownership, empowerment and optimal domestic resources. These policy strategies which reflects inward in ward looking promote the creation of enabling environment for good governance, effective co-ordination and peoples participation; capacity building for enhancing economic growth and equity through a conducive macroeconomic, sectoral (agriculture, industry and mining) and infrastructure (financial, transport, communication, energy (electricity) and marketing) policies and strategies; education, health, water supply and sanitation, employment opportunities, protection and preservation of the environment and housing and settlement.

Ideally, a nation's development should be people-centred, based on sustainable and shared growth and be free from abject poverty. For Tanzania, this development means that the creation of wealth and its distribution in society must be equitable and free from inequalities and all forms of social and political relations which inhibit empowerment and effective democratic and popular participation of all social groups (men and women, boys and girls, the young and old and the able-bodied and disabled persons) in society.

3.4.1. Broad based national development policies

The formulation and implementation of the series of sector specific, macro-economic and other broad based national development policies mark the second-generation reforms. The most important policies which have had direct bearing and relevancies to effective mobilization of foreign resources include the National Development Vision 2025, Tanzania Assistance Strategy, (TAS) and Joint Assistance Strategy for Tanzania, (JAST).

The Tanzania National Development Vision 2025

Tanzania envisioned is that the society by 2025 will be a substantially developed one with a high quality livelihood. Abject poverty will be a thing of the past. In other words, it is envisioned that Tanzanians will have graduated from a least developed country to a middle income country by the year 2025 with a high level of human development. The economy will have been transformed from a low productivity agricultural economy to a semi-industrialized one led by modernized and highly productive agricultural activities, which are effectively integrated and buttressed by supportive industrial and service activities in the rural and urban areas. A solid foundation for a competitive and dynamic economy with high productivity will have been laid. Consistent with this vision, Tanzania of 2025 should be a nation imbued with five main attributes:

- High quality livelihood.
- Peace, stability and unity.
- Good governance.
- A well educated and learning society; *and*
- A competitive economy capable of producing sustainable growth and shared benefits.

Tanzania should have created a strong, diversified, resilient and competitive economy which can effectively cope with the challenges of development and which can also easily and confidently adapt to the changing market and technological conditions in the regional and global economy. The TDV 2025 calls for efficient utilization of domestic resources. The mobilization and effective utilization of domestic resources (natural, financial and human) is the foundation on which the realization of the Vision rests. These resources should be utilized to build adaptive capacity for promoting economic activities that enjoy comparative and competitive advantages with a view to minimize the impact of external economic shifts and shocks.

The Tanzania Assistance Strategy (1999)

The GOT prepared the Tanzania Assistance Strategy, (TAS) in 1999, aimed at restoring local ownership, as well as promoting partnership in designing and executing development programmes and optimal utilization of foreign aid. TAS provides a comprehensive mechanism for determining Foreign Aid requirements and it is a clear strategy upon which the foreign resources coordination for its effectiveness on the ground are anchored. It was also about good governance, transparency, accountability and capacity building and effectiveness of foreign aid. TAS was not a program or a project; it was about a policy process for change. The TAS initiatives date back to the mid 1990's when Tanzania/donor relations were stained mainly due to serious slippage in revenue collection and rising corruption. The formulation of TAS took cognizance of appropriate ongoing and pipeline initiatives.

TAS was a first generation s five-year strategic national framework articulating: Policy Framework; National Development Agenda; Priority Actions; Basic elements for promoting local ownership and leadership; and building partnership. The framework was later reviewed after the first five years. The preparation of TAS took place with that of PRSP thereby sharing a number of common themes. However, whereas the TAS provided a broad strategic national framework within which PRSP operated the PRSP details out the characteristics of poverty and monitorable benchmarks and actions for poverty reduction in the medium and long term.

Joint Assistance Strategy for Tanzania

The Joint Assistance Strategy for Tanzania (JAST), in Kiswahili 'Mkakati wa Pamoja wa Misaada Tanzania' (MPAMITA), is the second national medium-term framework for managing development co-operation between the Government of the United Republic of Tanzania (Government) and Development Partners so as to achieve national development and poverty reduction goals. It however also outlines the role of non-state actors to the extent that they contribute to the successful implementation of the Strategy.

The JAST has been implemented at all levels of the Government within the existing national, sector and local processes for all aid relations with Development Partners. Development Partners will adopt the Strategy as a basis for guiding the management of their development co-operation with the Government. Bilateral agreements and country assistance strategies will be brought in line with the JAST and will specify concrete arrangements in implementing the JAST for individual Partners. All partners recognise that implementing JAST is a gradual process of moving towards higher levels of development co-operation.

The overall objective of the JAST is to contribute to sustainable development and poverty reduction in line with the National Vision 2025 and the Zanzibar Vision 2020 by consolidating and coordinating Government efforts and Development Partners' support under a single Government-led framework to achieve results on the National Strategy for Growth and Reduction of Poverty (NSGRP/MKUKUTA) and the Zanzibar Strategy for Growth and Reduction of Poverty (ZSGRP/MKUZA) as well as other national development and poverty reduction programmes.

JAST articulate forms, needed capacity and mechanism for effective utilization of foreign aid. JAST provide predictable public financial framework for economic development programs and allows joint efforts for strategic prioritization. That is, the intermediate objective of the JAST is to build an effective development partnership in line with national and international commitments to aid effectiveness by [1] strengthening national ownership and Government leadership of the development process, [2] aligning Development Partner support to Government priorities, systems, structures and procedures, [3], harmonising Government and Development Partner processes, [4] managing resources for achieving development results, [5] ensuring mutual accountability of the Government and Development Partners, and [6] strengthening accountability of the Government to the citizens of Tanzania.

3.5. Sector specific national development policies

Tanzania has put a number of sector specific national development policies which have had positive impact on the foreign resources. These include the National Investment Policy, National Mining Policy, National Tourism and National Trade Policy. Table 3.2 shows peoples perceptions on the major policies which have been impacting the performances of foreign resource utilization in Tanzania. About 65 percent mentioned the National Trade Policy and about 24 percent mentioned monetary policy. Other included ICT policy, Tourism and Land national development policies.

Table 3.2 Major Policies which have been impacting foreign resource utilization

Nr	Type of Policy	Percent
1	Trade Policy	64.78
2	Monetary Policy	23.88
3	ICT Policy	2.84
4	Tourism Policy	5.67
5	Land Policy	2.84
		100.00

Source: ERB-POPC Field Research Survey, 2009

Table 3.3 identifies outwards looking policies that attracted foreign resources to the economy. Over 57 percent of respondents suggested that national investment policies and reforms to have been a big success in Tanzania. This is followed by national trade and mining policies. The study also explored the types of resource flows and recipient sectors.

Table 3.3: Identified Success Policies

Policy	Percentage
Trade policy	26.37
Investment policy	57.69
ICT policy	5.49
Mining policy	10.44

Source: ERB-POPC Field Research Survey, 2009

3.5.1. The National Trade Policy

The goal of National Trade Policy (2003) is that of raising efficiency and widening linkages in domestic production and building a diversified competitive export sector as the means of stimulating higher rates of growth and development. Five specific policy objectives emanate from and reflect this goal.

The *first specific objective* is to stimulate a process of trade development as the means of triggering higher performance and capacity to withstand intensifying competition within the domestic market. *The second objective* involves economic transformation towards an integrated, diversified and competitive entity capable of participating effectively in the MTS. *The third objective* entails the stimulation and encouragement of value-adding activities on primary exports as a means of increasing national earnings and income flows even on the basis of existing output levels. *Fourth is the stimulation of investment flows into export oriented areas in which Tanzania has comparative advantages as a strategy for inducing the introduction of technology and innovation into production systems as the basis for economic competitiveness*. *The fifth objective* is the attainment and maintenance of long-term current account balance and balance of payments through effective utilization of complementarities in regional and international trading arrangements as a means of increasing exports combined with initiatives for higher efficiency in the utilization of imports.

Tanzania National Trade Policy instruments are measures taken by governments to influence the direction and pattern of trade development. The application of these instruments in Tanzania will be guided by the need to stimulate domestic production, promote exports, safeguard domestic industry against dumping practices and protect consumers. Tanzania will exercise trade policy options in line with its international obligations. These instruments include: tariff-based (ad valorem) instruments; NTBs; trade Defence mechanisms; trade development instruments; and international trade policy instruments as listed hereunder.

The NTP (2003) has a number of trade development instruments. This group comprises of instruments that are used in stimulating the development of export trade by focusing on measures at all levels of production, such as crop/animal husbandry practices and product transformation processes through the various aspects of marketing and actual delivery. They target addressing the supply side constraints that remain the major impediment to trade expansion in developing countries. Trade development instruments include EPZs, Investment Code and Rules, export development/ promotion and export facilitation.

The investment code as a trade policy instrument works through compensation for distortions which impede the flow of foreign investments largely due to market imperfections. In principle, the investment code is considered a necessary interim instrument for stimulating both foreign and domestic investments while initiating measures for strengthening the enabling business environment and working for the emergence of a vibrant market economy. In the long-run, the necessity of this instrument declines as imperfections in the market are reduced and an enabling environment emerges. Tanzania has undertaken significant efforts to encourage investments through the Tanzanian Investment Act of 1997 and the establishment of the Tanzania Investment Centre (TIC), the Mining Act of 1998 and the establishment of Dar es Salaam Stock exchange in 1996.

3.5.2. The National Investment Policy, 1997

Tanzania has a very friendly national investment policy environment. Given the resources and other intangible advantages that Tanzania enjoys, and taking into account the point that development is a dynamic process; in order to meet the challenges facing Tanzania to make its socio-economic aspirations a reality, the national investment policy objectives are to attain [1] maximum mobilization and utilization of domestic capacity including cooperation with other developing countries; [2] maximum promotion of export orientation in domestic production of goods and services to enhance the development of a dynamic and competitive export sector, [3], the encouragement of inflows of external resources to complement national efforts; [4] encouragement and facilitation of the adoption of new technologies in activities that especially have direct bearing on productivity, quality and increased competitiveness.

The specific national investment policy objectives that the Tanzania wishes to further through, for example, the promotion of local and foreign investments include the; [1] optimization of foreign resource inflows through export-oriented activities to complement domestic resources; [2], encouragement of the most productive domestic activities to be export-oriented as a way to improve competitiveness in the domestic production of goods and services.; [3] encouragement of the development of local capacities in the field of science and technology, and the transfer of appropriate and new technology and promoting the adoption of new and emerging information technologies in the communications sector.

The government recognizes the importance of adequate and effective incentives in facilitating the mobilization of increasing magnitudes of appropriate local and foreign investments. Accordingly, the investment incentives provided will facilitate the achievement of the investment policy objectives, some of which are specified in the investment code. The incentives provided will be competitive, and directed towards investments in areas that are most crucial to Tanzania's economic development and suit the country's changing needs.

The incentives are broadly standardized to avoid the high administrative costs associated with a large number of incentives differentiated by activities and sectors. The incentives are also performance-based, and thus will be availed to investors subject to the satisfaction of performance criteria. This performance will largely be reflected in the investment plans submitted by the investor and agreed upon with IPC/IPA.

The investment incentives are categorized into fiscal and non-fiscal incentives. The fiscal or tax incentives include: investment allowances on capital expenditure; reinvestment allowances on capital expenditure; infrastructure allowances on infrastructure expenditure; preferential tax rates for withholding tax on dividends, royalties and interest; preferential tax rates on personal income tax; preferential rates on indirect taxes; and double deductions of approved/specified costs and expenses. In addition, the incentives must be stable, affordable and competitive.

3.5.3. The National Foreign Policy

The Tanzania National Foreign (2002) policy manifests itself in active international engagement, which is basically leveraged upon the pursuit of economic objectives, while at the same time preserving the gains of the past and consolidating the fundamental principles of Tanzania's traditional foreign policy. Among the principles of the foreign policy, the country intends to promote deeper economic cooperation with our development partners; support for the practice of the policy of non-alignment and South-South Co-operation and support for the United Nations in its search for international economic development, peace and security.

The foreign policy focuses on economic diplomacy. The specific economic diplomacy objectives include the need [1] *to project, promote and protect political, economic, social and cultural interests through active and sustainable economic diplomacy*; [2] to ensure that Tanzania relations with other nations and international entities are also driven in line with economic interests; and [3] to create the necessary conditions which, shall enable URT to participate effectively in the regional and global economies and international negotiations. The term "economic diplomacy" has been evolving from trade diplomacy to including production and investment. A distinctive feature of economic diplomacy in Tanzania is that private sectors are involved in the foreign policy decision-making processes and missions to influence negotiating positions to remain in the global or regional competitive market. This is because firstly competitive market developments are rigorously monitored by private sectors. *Secondly,* they are in the field and they know where and how to invest, sell, goods and services in the interests of a country.

The URT's New Foreign Policy has a number of specific strategies. These include Buildings Facilitative Internal Environment, Forging International Partnership, Redefining Bilateral Diplomacy, Strengthening Multilateral Diplomacy, Promoting Good Neighborliness, Enhancing Regional Peace and Security, Strengthening Regional Economic Integration (EAC, SADC,IOR-ARC), Upholding African Union (AU), Reaffirming Non-Alignment, Promoting South-South Cooperation, Enhancing the Commonwealth Organization, Promoting the United Nations Organization, Readdressing Financial Issues and external Debt, Cooperating with Multinational Corporations and Supporting Effective NGOs.

Economic diplomacy may operate in three levels: (a) bilateral (b) regional and (c) multilateral. Bilateral economic diplomacy forms a major part in economic relations, whether this consists of informal dealings between two countries on a range of issues or formal bilateral agreements on trade or investment or avoidance of double taxation. Regional dimension in economic diplomacy is of growing importance. Regional economic agreements offer a more rapid way of opening markets. Liberalisation of economy may be easier to accept for national interests when it occurs within a regional grouping of countries.

One of the areas of economic diplomacy noted in this report is related to bilateral free trade agreements (FTA). Different countries may use different levels of trade agreements. The multi-level nature of economic diplomacy means that governments take advantage of such levels. It implies that governments have many options to take. Bilateral trade agreements have been the order of the day. Bilateral Free Trade Agreements (FTA) are being concluded by many countries. The number of FTAs constituting trade blocs has increased substantially in recent years. The main strategies of the foreign policy included the need, [1] to create an interface of both internal and external determinants of growth and development and [2] to formulate an organizational arrangement receptive to change, and administrative procedures that are well adjusted and realigned to the needs of economic diplomacy.

3.5.4. The Minerals Policy of Tanzania, (1997)

Tanzania has a considerably high potential in terms of her mineral resources. This potential can be harnessed to make a significant contribution to the national economy and make the benefits reach a wider spectrum of the people in Tanzania. The mineral resources' potential can be utilized to increase its contribution to the national output and value-added, generate employment and make greater contributions to foreign exchange earnings as well as government revenue. The mineral sector policy underlines specific policy strategies to enhance the utilization of the mineral resources potential for the realization of the above goals and at the same time ensures that acceptable standards of human health and safety are maintained and that strategic environmental impact assessment of all mining activities is observed

The overall policy objective for the mineral sector development is to attract and enable the private sector to take the load in exploration, mining investment by administering regulating and promoting the growth of the sector. Accordingly the policy objectives of the Government for the mineral sector are [1] to stimulate exploration and mining development; [2] to regularize and improve artisanal mining; [3], to ensure that mining wealth supports sustainable economic and social development, [4] , to minimize or eliminate the advise social and environmental impacts of mining development; .[5*], to promote and facilitate mineral and mineral based products marketing arrangements*; [6] to promote and develop Tanzania as the gemstone centre of African and [7] to alleviate poverty especially for artisanal and small scale miners.

A sound macro-economic private sector environment and effective fiscal policies are important prerequisites for mineral development; as they strongly influence the performance of the mining sector. Thus, there is need to develop a favourable macro-economic and trade policy, a market-based foreign exchange regime, and taxation arrangements that are competitive and fair to both the government and investors. A sound private sector investment environment shall include the provision of two fiscal regimes; one being the right to export; and the other being an assurance of the ability to import the necessary plant, equipment and other mining supplies with little or no import duty being imposed. The sustainable development of the mining sector requires a stable, transparent and predictable macro-economic environment aimed at both internal and external balances.

3.5.5. National Tourism Policy

The national tourism policy seeks to assist in effort to promote the economy and livelihood of the people essentially poverty alleviation through encouraging the development of sustainable and quality tourism that is culturally and socially acceptable, ecologically friendly environmentally sustainable an economically viable it is also sought to market Tanzania as a favorable tourist destination for touring and adventure (a wildlife safety in a country renowned for sits cultural diversity and numerous beaches. It is recognized that the private sector will play a major tale in the industry's development with the government playing the stylistic roe of providing and improving the infrastructure a swell as providing a conducive climate for investments.

The policy strategies for investment include the need for [1], *promoting tourism as priority sector for development streamlining investment procedures and providing fiscal and non-fiscal incentives to investors in his sector*; [2], dissociating information on the tourism investment opportunities available in the industry to potential investors within and outside the country; [3], promoting tourist projects by way of joint venture arrangements with local partners; [4], discouraging vertical integration in tourism investments.

3.6. Medium Term Economic Strategies

3.6.1. The National Poverty Eradication Strategy, (1998)

NPES was crafted as a strategy that provides a framework to guide poverty eradication initiatives in order to reduce absolute poverty by 50 per cent by the year 2010 and eradicate it by year 2025. The strategy targets improved economic growth and people's incomes as a basis for poverty eradication. A growth rate of 8-10 per cent for the economy was targeted. NPES was the first attempt to translate Vision 2025 to medium term targets.

3.6.2. Poverty Reduction Strategy Paper (2000)

The Poverty Reduction Strategy Paper (PRSP) was formulated as a medium-term strategy of poverty reduction, in the context of the enhanced Highly Indebted Poor Countries (HIPC) initiative. It is through PRS that resources to the priority areas were to be directed and national policies implemented. The process of formulating PRSP involved limited consultations, mainly limited by the short time required to produce the document. The Strategy adopted a "priority sectors" approach. Priority in allocation of Government resources was to be in basic education, basic health, irrigation, infrastructure (feeder roads), water, good governance and cross-cutting issues (gender, environment and HIV/AIDS)

3.6.3. National Strategy for Growth and Reduction of Poverty

Following the second review of implementation of Tanzania's Poverty Reduction Strategy (PRS) in 2004, the government launched a five year National Strategy for Growth and Reduction of Poverty (NSGRP) in 2005. The NSGRP improved on PRSP through adopting an outcome-based approach focusing on three clusters: a) growth and reduction of poverty; b) improvement of quality of life and social well-being; and c) good governance and accountability in the public sector. Policy design and government initiatives were to be organized with respect to their contribution to the achievement of these and other related objectives.

The strategy focuses on both local and foreign resources. The strategy seeks to ensure access to domestic resources (finance, land, water); technological and managerial skills including marketing; market information and contacts. On the foreign resource, the strategy fosters conditions that attract more Foreign Direct Investments with a view to realizing the gains in form technology transfer and increased productivity and diversification of the structure of the economy. A stable investment and regulatory climate will be ensured. Issues related to the choice of technology, strategic links with local firms and higher learning and R&D institutions, technical capabilities and readiness of local firms and labour-force to adapt technology will be examined. The strategy links domestic and foreign resources by recommending facilitating linking-up of domestic producers with local and foreign R&D institutions.

3.6.4. The Tanzania Mini -Tiger Plan 2020 (2004)

The government of Tanzania drew up the "Tanzania Mini-Tiger Plan 2020" as a vehicle to achieve the objectives of the Tanzania Development Vision 2025. The mini-tiger plan is inspired by the growth experiences of South East Asian countries. It is expected to facilitate the creation of a favourable climate for both domestic and foreign investment through the establishment and promotion of Special Economic Zones (SEZ), a revised regulatory framework and a supportive legal framework.

The plan is based on the "ponds and birds" theory, along the Asian economic development model, which focuses on employment creation by attracting Foreign Direct Investment (FDI), the "migrating birds" and promoting exports by developing Special Economic Zone (SEZ), the "ponds". Three basic strategies have been adopted in order to accelerate to 8-10 per cent annual growth rate of the economy: building SEZs and aggressively promoting most promising Industries (Primary, Light Industry and Tourism); quickly improving the National Balance Sheet by expanding exports from $1.0 billion to $2-3 billion within 3-4 years and solving as many bottlenecks by additional borrowing and foreign currency earning plus FDI. Also, expanding investment activities further into more high value-added sectors and moving into larger investment projects not only in the export-oriented industries but also moving into import-substitution industries and processing industries as more domestic and foreign capital become available.

The Plan has set five targets for year 2020: GDP to be growing at an average of 8-10 per cent and reach $40 billion; exports to be expanded from $1.1 billion to $20 billion; per capita income (PCI) to be increased from $280 to at least $1,000; creating 2-3 million new jobs and developing at least 25-30 SEZs in the country and attracting FDI aggressively.

Various activities have been carried out as part of the implementation of the Tanzania Mini-Tiger Plan. The activities included continuation of the construction of a Special Economic Zone at Mabibo – Dar es Salaam known as "The Benjamin William Mkapa Special Economic Zone (BWM- SEZ)" by putting in place infrastructure systems such as water, electricity and roads. Special Economic Zones Act was passed by the Parliament of the United Republic of Tanzania in 2006, as a prerequisite for the establishment of SEZ Authority.

3.6.5. Financial Sector Reform Programmes

Tanzania's financial reforms, which aim at enhancing resource mobilization and intermediation, is based on the implementation of the recommendations of the Presidential Commission of Enquiry into the Monetary and Banking System in Tanzania (1990), and those of the 2003 IMF/World Bank Financial Sector Assessment Programme (FSAP) mission.

The reforms have resulted not only in a new landscape for the country but also in a new culture of doing business. The banking sector that had only three commercial banks before the reform is now comprised of many relatively competitive commercial banks and non-bank financial institutions (NBFIs). An Inter-bank Foreign Exchange Market thrives; operationalizing market determined exchange rates for the Tanzanian Shilling. The reforms in the insurance sector have seen the number of insurance companies increase from two to thirteen, of which eleven are privately owned. The enactment of the Capital Markets legislation led among other things to the establishment in 1998 of the Dar es Salaam Stock Exchange (DSE).

The outcomes of the reforms can also be gauged by looking at some simple indicators of financial intermediation notably the ratios of broad money (M2) and private sector credit to GDP; the proportions of savings and capital formation to GDP; as well as the share of population with access to finance (including microfinance and saving facilities). The ratio of money to national product, at the simplest level, reflects progress in monetizing economic activities but, to the extent that various bank deposits (savings) are included in the money definition, it also indicates progress in domestic saving mobilization. All these improved access to financial resources by private sector business operators which in turn attracted both foreign financial sector investors and other foreign investors into the country. Studies indicate that impact of financial sector reforms on economic growth and investment could be 'mixed' but at least agree that efficient financial sector is a necessary condition for both local and foreign investors operation.

Therefore, the various broad and sector specific reforms undertaken in Tanzania have been instrumental in stabilizing and improving the macro economic condition and other business environment condition necessary for attracting and optimizing use of foreign resource. The main challenge is to consolidate these first and second generation policy reforms and ensure coordination between sector specific policies that would promote effective use of foreign resource in complementing domestic resources.

3.6.6. Local Government Reforms

Tanzania local government system is based on political devolution and decentralization of functions and finances within a unitary state. Local governments are hostilic, i.e. multi-sectoral, government units with a legal status (body corporate) operating on the basis of specific and discretionary powers under the legal framework constituted by the national legislation. Local governments have a responsibility for social development and public service provision within their areas of jurisdiction; facilitation of maintenance of law and order and promotion of local development through participatory processes.

The implementation phase of the Local Government Reform Programme (LGRP) began on 1st January 2000 in the 38 Phase 1 Councils. The ongoing local government reform is one of the boldest and far-reaching reforms ever carried out in Tanzania since the country's independence. The reform is both a product and an outcome of a national conference of delegates representing the entire spectrum of Tanzanians to shape a shared vision for a local government system, which would be instrumental in providing both services, and in speeding up development at local levels. To this extent the reform can be categorized as demand-driven reform mooted by the people, for the interest and development of the people.

The core value for the far reaching changes in the Tanzanian local government system is improved delivery of service provided through and facilitated by local government authorities to all citizens. Other values identified in the shared vision include increased autonomy, transparency, efficiency and cost effectiveness in service delivery and increased accountability to the people. These are clear and specific values which meet the cry of the masses who have for long been victims of maladministration and poor services provided by or through a centralized governance system. The changes taking place in the local government system are intended to give the citizens a greater say in formulating and implementing their own service delivery and development plans and in how services are to be managed and delivered. To this end, the main strategy which has been opted for is devolution of powers, responsibilities and resources from central government to local government authorities and from council levels to communities.

In a situation where real power has always vested in and has been exercised by leaders on behalf of the people the devolution strategy is invariably wrought with a host of difficulties and challenges. It is now clear that the difficulty of getting the existing power holders to part with their much cherished powers and prestige and give it to the people as the Constitution already provides and the difficulty of getting the ordinary citizen to accept that he or she as a member of society is the source and fountain of all power and authority which has in most cases has been exercised by the government on his or her behalf, have to be reckoned with and will have to be addressed for a long period to come. In the above context the local government reform is a major and massive revolutionary change which demands a complete change of mindset both on the part of leaders at all levels on one hand and the general public on the other hand

Another fundamental lesson to learn is that meaningful decentralisation by devolution through local government authorities will not come about unless existing sectoral policies and laws are harmonised to conform to the national shared vision on local governance and hence clear the required ground to implement the desired political, administrative and financial decentralisation. Unless this is done upfront, there will be no incentive for people to participate in the reform process.

Finally, it is evident that the changes which are taking place in the local government system will take a long time and will certainly outlive the current donor-supported programme. With this fact in view and to ensure sustainability of the reform process there is need to enhance the mainstreaming reform measures in the normal operations of the main actors at central and local levels. The overall challenge is to keep leaders and the general public firmly focused on the core value and end result of local government reforms: good governance at all local government levels and improved service delivery which at the end would improve effective use of both domestic and foreign scarce resource for economic growth and poverty reduction.

3.6.7. Rural Development policy

Tanzania, like many developing countries has its share of problems associated with developing its rural sector where the majority of its population lives. Since independence, the government of Tanzania has proclaimed the development of the rural sector as the cornerstone of the country's development strategy. A number of approaches have been tried in Tanzania. Some of them abolished and then re-established in an effort to pave a smooth road towards rural development through improved agricultural performance and provision of essential social services. Thus, rural development policy is well encored in the overall development policy through improving and upgrading sector specific policies. The main challenge remains that besides the provision of social services such as clean water, schools and dispensaries to about half of the rural population, none of the approaches has led to the anticipated transformation of production structures and productivity of the rural sector. The rudimentary production tools and techniques has sustained leading to low productivity and hence uncompetitive products in terms of quality and price. The on going initiative under "Kilimo Kwanza" should serve a best strategic opportunity to address the constrained agriculture sector that have abundant arable land remaining idle as an effective step towards optimal utilization of domestic resource.

Chapter Four Foreign Aid Resources

4.1. Introduction

Chapter four aims at analyzing the role and impact of foreign aid in Tanzania. Specifically, it examines the level and magnitude of Official Development Assistance, (ODA) that is, needed to supplement domestic resource in the process of developing leading industry/primary industries which will stimulate rapid economic growth and spell-over effect in Tanzania. The chapter consists of four major sections. Apart from section 4.1, the introduction, section 4.2 describes the composition and trends in foreign aid flows in Tanzania. The section also examines the macroeconomic policy environment in which foreign aid can perform effectively to raise economic growth and reduce poverty. It also states the main objectives, role and importance of foreign aid to the recipient economy. Section 4.3 discusses the issues of external debt development and external dependence associated with foreign aid flows into the economy. The issues of optimal mobilization and utilization of foreign aid and the need for foreign aid to supplement rather than substitute domestic resources are examined in section 4.4. The last section 4.5 presents the main ODA findings.

4.2. Foreign Aid: Conceptual Framework

Foreign aid can be defined as additional resources in foreign currency or its equivalents, over the capacity to import generated by exports or financed from accumulated reserves, without the need to make immediate repayments and at costs lower than the prevailing rates of commercial loans, (Semboja, 2005). This includes the provision of skilled manpower and the transfer of technical skills through foreign assistance. These additional resources aim at enhancing the economic performance of the recipient country above the level that would be otherwise attainable. That is, either the country achieves a higher rate of growth without reducing the anticipated consumption or it implements the anticipated rate of growth and managing to increase the consumption level. A common means of defining and measuring foreign aid is official development assistance (ODA). ODA consists of grants or loans that one government or multilateral organization gives to a developing country to promote economic development and welfare. That assistance must be granted on concessional terms, which in the case of a loan means that at least 25 percent of it must be in the form of a grant.

4.3. Perceptions on Foreign Resources

According to the 2009's ERB-POPC Survey, 48.60 percent of foreign resource is thought to flow into the country through foreign direct investment, 31.63 percent through official development assistance, 15.23 percent through remittances and 4.54 percent through other forms such as technical assistance (Table 4.1). These perceptions are consistent with secondary data and information available from the government data sources such as Bank of Tanzania and the Ministry of Finance and Economic Affairs which indicate that larger percent of FDI flow into the country than other forms of foreign resources. About 50 percent of FDI flows into the country implying limited domestic investment and great potential business environment. However, over 31 percent indicates that the country heavily depends on foreign aid for economic growth and reduction of poverty. It is argued that a strong nation have to be independent both economically and politically. This demands the need to promote FDI flow into the country and encourage private public partnership particularly in strategic sectors of the economy such as mining. This should be done systematically with building capacity for local investors and creating balanced, possibly favourable investment climate for domestic investors.

Table 4.1 Types of Foreign Resource Flows in Tanzania

Foreign resource	Percentage
FDI	48.60
ODAs	31.63
Remittances	15.23
Others	4.54

Source: ERB- POPC Survey 2009

4.4. Foreign Aid Performance

4.4.1. Composition and Trends in Foreign Aid Flows into Tanzania

ODA is composed of both grants and loans. Table 4.2 shows the ODA is one of the main sources of external transfer for Tanzania. Figure 4.2 presents composition of ODAs in Tanzania and their trends in the 1986/87-2006/07 period.

Table 4.2 ODAs in Tanzania (in Tshs Million and Annual Growth Rate)

	ODAs		Grants		Loans	
	Tshs (Mil.)	% Δ	Tshs (Mil.)	% Δ	Tshs (Mil.)	% Δ
1986-87	6235.0	-	-	-	6235.0	-
1987-88	6880.9	(10.4)	-	-	6880.9	(10.4)
1988-89	10619.3	(54.3)	-	-	10619.3	(54.3)
1989-90	5567.3	(-47.6)	-	-	5567.3	(-47.6)
1990-91	6186.4	(11.1)	-	-	6186.4	(11.1)
1991-92	12003.0	(94.0)	-	-	12003.0	(94.0)
1992-93	122023.5	(916.6)	59751.5	-	62272.0	(418.8)
1993-94	207400.0	(70.0)	106790.0	(78.7)	100610.0	961.6)
1994-95	100870	(-51.4)	58505.0	(-45.2)	42365.0	(-57.9)
1995-96	39112.0	(-61.2)	31096.0	(-46.8)	8016.0	(-81.1)
1996-97	111361.8	(184.7)	81415.6	(161.8)	29946.2	(273.6)
1997-98	284769.9	(155.7)	130852.9	(60.7)	153917.0	(414.0)
1998-99	223788.4	(-21.4)	169945.6	(29.9)	53842.8	(-65.0)
1999-00	468093	(109.2)	280306.7	(64.9)	187786.3	(248.8)
2000-01	459186.4	(-1.9)	286306.0	(2.1)	172880.4	(-7.9)
2001-02	567203.5	(23.5)	379848.0	(32.7)	187355.5	(8.4)
2002-03	895643.9	(57.9)	622302.1	(63.8)	273341.8	(45.9)
2003-04	1112403.9	(24.2)	655378.8	(5.3)	457025.1	(67.2)
2004-05	1413616.2	(27.1)	724396.5	(10.5)	689219.7	(50.8)
2005-06	1388834.4	(-1.8)	972927.9	(34.3)	415906.5	(-39.7)
2006-07	2093100.7	(50.7)	1096040.0	(12.7)	997060.8	(139.7)

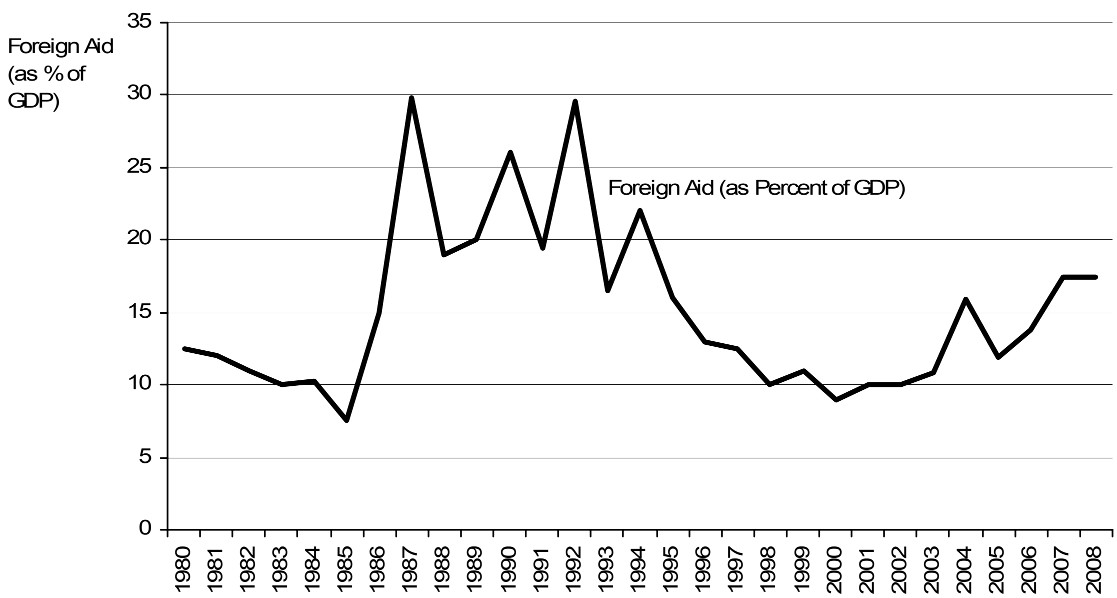
Source: Bank of Tanzania (Various issues): Notes: figures in the parentheses are annual growth rates

The table indicates ODA as one of the main sources of external transfer for Tanzania grew by 55 percent between 1993 and 1999, during that time the average annual growth rates of grants and loans were 43 percent and 104 percent respectively. During the 2000 - 2006 period, total ODAs increased by 26 percent on average, in which grants grew by 23 percent, whereas loans rose by 38 percent on average. This trend implies that ODAs did not grow faster during the first half of the 2000s in comparison to the 1990s average annual rate of growth. However, loans which constitute less than 50 percent of foreign aid in Tanzania grew faster that grants during both 1990s and early 2000s.

Figure 4.1 shows that Tanzania received large and sustained aid flows for much of the late1980s and early 1990s. Even when aid flows decreased in the early 1980s and late 1990s, Tanzania received higher aid inflows than most sub Saharan African countries (SSA) (Figure 4.2 and Table 4.3). Between 1985 and 1990, the ratio of aid disbursement/GDP ratio increased steadily. During this period Tanzania embarked upon a wide-ranging structural adjustment supported by both the World Bank and IMF after a decade of protracted economic decline. In the mid-1990s inflows again declined, but remained higher than most other SSA countries at almost 10 percent of GDP, (Muganda, 2004). During the 1993/94 relations between government and major donors deteriorated over failure of the former to collect counterpart funds under the commodity import support, (CIS), scheme and to increase the tax collection efforts generally. There was a suspicious of corruption. Donor started to question the effectiveness of their aid. Government on its part felt that the donors' demands were often unrealistic and too intrusive in matters which were essentially domestic. Strained relations between the government and donors had a significant adverse effect on aid flows to Tanzania in the early and mid 1990s.

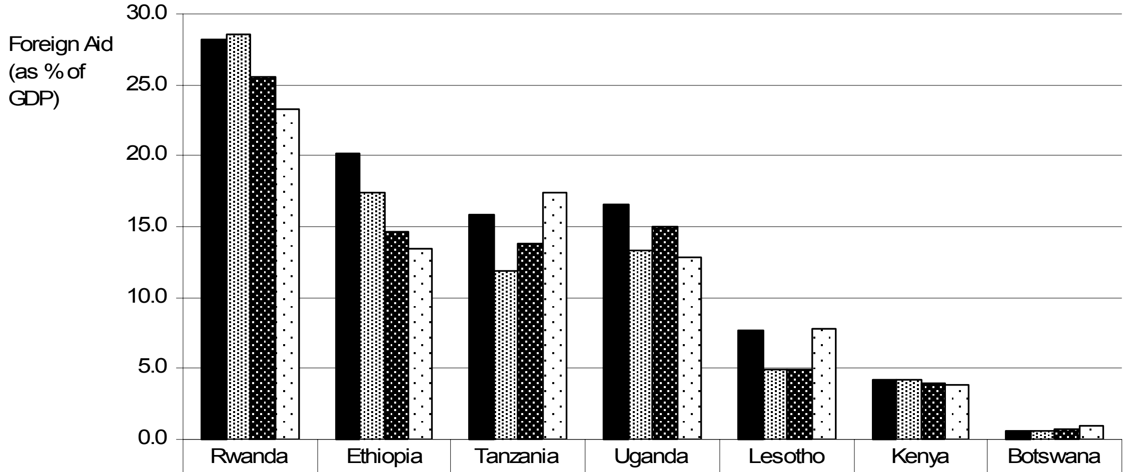
Since 2000, the commitment to macroeconomic and structural reform emphasizing the importance of restricting the role of the state in the economy has coincided with another surge in aid flows, with the aid/GDP ratio over 12 percent in recent years (IMF, 2005).

Figure 4.1: Tanzania: Aid Flow (as Percent of GDP), 1980-2008



Source: OECD-DAC

Figure 4.2 Selected Countries: ODA Flows (as Percent of GDP), 2004-2007



	Rwanda	Ethiopia	Tanzania	Uganda	Lesotho	Kenya	Botswana
2004	28.3	20.2	15.9	16.5	7.7	4.2	0.6
2005	28.5	17.4	11.9	13.4	4.9	4.2	0.6
2006	25.6	14.7	13.8	15.0	5.0	4.0	0.7
2007	23.3	13.4	17.4	12.9	7.8	3.9	1.0

Source: OECD-DAC, UNCTAD, and Authors' Calculations

Figure 4.2 shows that the ratio of ODA to GDP in Tanzania grew from about 12 percent in 2005 to 17 percent in 2007, which implies that Tanzania remains dependent on foreign financial support. In the next couple of years, about 40 percent of the national budget will be funded from foreign resources. According to the World Bank designed Debt Sustainability Framework, Tanzania is capable of taking on new loans. This framework has many flaws, including that it fails to take account the quality of loans or the financing needs for the Millennium Development Goals (MDGs). As long as Tanzania has insufficient finance for the implementation of the MDGs, this finance should come as grants rather than loans. Other foreign aid dependent countries such as Rwanda, Ethiopia, and Uganda have seen their external aid dependence relative to GDP declining over time (see Figure 4.2).

Table 4.3 indicates that in 2007 Tanzania received a record of US$ 2643 as a net disbursement of ODA, ahead of all African countries in nominal value (OECD-DAC, 2008). During that period, Tanzania's ODA-GDP ratio was 17 percent which, was ahead of Uganda's ODA-GDP ratio of 13 percent and Kenya's ODA-GDP ratio of 4 percent. Although, countries such as Rwanda and Ethiopia recorded higher ODA-GDP ratios in the 2000s than Tanzania, these had in fact received lower levels of ODAs than Tanzania in nominal terms. This augment is surprisingly contrary to responses from interviewees.

Table 4.3 Sub-Sahara Africa: Net Disbursement of ODA (USD Million)

	1991/92 Average	1996/97 Average	2004	2005	2006	2007
Burundi	365	103	380	375	415	425
Congo, Dem. Rep.	482	198	1 920	1 847	2 049	1 112
Ethiopia	1 463	846	1 914	1 973	1 948	2 227
Kenya	1 126	616	682	786	943	1 184
Lesotho	175	120	101	71	72	120
Malawi	732	505	534	599	684	676
Mauritius	73	40	34	34	19	67
Mozambique	1 659	1 154	1 319	1 332	1 605	1 619
Rwanda	459	434	516	595	586	655
Somalia	549	106	215	248	392	351
Sudan	917	220	1 061	1 892	2 052	1 951
Tanzania	*1 562*	*1 118*	*1 860*	*1 534*	*1 825*	*2 643*
Togo	269	159	68	86	79	110
Uganda	900	929	1 288	1 229	1 549	1 592
Zambia	1 218	756	1 194	1 191	1 426	967
South of Sahara, regional	909	1 007	1 513	1 153	1 590	1 577

Source: OECD-DAC: USD Million at 2006 prices and exchange rates

Table 4.4 shows that only 8 percent of the respondents said that Tanzania attracts and utilizes foreign resources more than other East African countries and developing countries in general, whereas about 28 percent of the interviewees argued that Tanzania attracts and utilizes foreign aid less than any other developing countries. Importantly, more than half of the respondents said that they did not know whether Tanzania was above or below other developing countries in attracting and utilizing external aid mainly due to lack of information. This observation therefore, has strong policy implication. In parallel with this argument, one can argue that there is no strong evidence that aid has better growth impact or it has played a big role in poverty reduction. However, this study observed that growth in Tanzania would be lower in the absence of aid. It necessary follows that slow economic growth record in Tanzania cannot be attributable to aid ineffectiveness, to this extent; aid has not failed in Tanzania.

Table 4.4: Tanzania Vs Other Developing Countries in Attracting and Utilizing Foreign Aid

Responses	Percent
Tanzania attracts and utilizes foreign resources more than other East African countries and developing countries	7.73
Tanzania attracts and utilizes foreign resources less than other East African countries and developing countries	28.18
It is not well known whether Tanzania attracts and utilizes more/less foreign resources than other developing countries	64.09

Source: ERB-POPC Survey, 2009

In 2003, Tanzania was the second largest non-European foreign aid recipient country after Afghanistan, (EC, 2006). Foreign aid of this magnitude is certainly of major macroeconomic importance. It can have both direct and general equilibrium effects on economic variables, and also influences the policy environment. In the traditional macroeconomic view the flow of aid contribute to long-run development by releasing bottlenecks associated with low incomes. In low income countries such as Tanzania, rapid growth may require an investment rate that is too high to be financed by subsistence saving. Foreign aid provides the additional financing. Moreover, given the narrow export and tax base in Tanzania, imports and government spending may be binding constraint. By supplementing domestic resources, foreign aid enables the achievement of short run growth target.

Table 4.5 shows that during the 1998–2005 period, the largest donor was the World Bank's IDA followed by UK and the EC; also Nordic countries and Japan played important role. There are three channels through which Tanzania receives foreign aid from Development Partners: Budget Support, Common Basket Funds, and Project Funds. The World Bank, Denmark, Finland, and others focus on the common basket while the United Kingdom, Sweden, the EU, and others take the form of budget support. Norway, Netherlands and Switzerland use both common basket and budget support according to their purposes. The United States, Germany, the UNDP, and Japan have limited participation in the common basket and budget support. Financial aid in Tanzania is comprehensively monitored, audited and evaluated by the various development partners.

TABLE 4.5a: **Amount of DAC countries' and International Organizations' ODA disbursements to Tanzania, 1998-2005**

DAC Countries, ODA Net												
												(Net disbursements, $ million)
Year	1		2		3		4		5		Japan	Total
1998	U.K.	158.6	Germany	109.9	Japan	83.4	Netherlands	80.3	Denmark	69.6	83.4	769.2
1999	U.K.	88.6	Denmark	80.9	Japan	74.8	Germany	66.6	Netherlands	55.2	74.8	613.4
2000	Japan	217.1	U.K.	152.7	Netherlands	97.3	Denmark	68.8	Sweden	63.5	217.2	778.7
2001	U.K.	290.1	Japan	260.4	Netherlands	75.1	Denmark	66.6	Germany	48.2	260.4	943.8
2002	Netherlands	138.3	Italy	132.3	U.K.	103.2	U.S.A.	85.4	Belgium	70.6	58.2	902.8
2003	U.K.	285.5	Germany	98.5	Netherlands	95.8	Denmark	85.5	U.S.A.	75.2	74.5	965.6
2004	U.K.	215.6	France	120.0	Netherlands	117.6	Denmark	93.9	U.S.A.	89.5	52.5	1,028.7
2005	U.K.	215.9	U.S.A.	108.9	Sweden	91.8	Netherlands	90.2	Denmark	84.7	36.1	871.0

Source: OECD/DAC

TABLE 4.5b: **Amount of DAC countries' and International Organizations' ODA Disbursements to Tanzania, 1998-2005**

International Organizations, ODA Net												
												(Net disbursements, $ million)
Year	1		2		3		4		5		Others	Total
1998	IDA	84.7	AfDB	56.4	CEC	43.2	UNDP	13.3	IMF	10.7	20.0	228.3
1999	IDA	174.9	CEC	71.0	IMF	51.3	AfDF	44.2	UNDP	9.9	24.7	375.9
2000	IDA	109.4	CEC	32.4	IMF	27.4	AfDF	26.4	UNHCR	22.4	28.0	246.0
2001	IDA	119.9	CEC	96.7	IMF	37.1	UNHCR	25.1	WFP	16.5	35.0	330.2
2002	IDA	146.3	CEC	70.2	IMF	29.3	UNHCR	27.0	AfDF	17.1	40.7	330.6
2003	IDA	424.9	CEC	185.1	AfDF	44.6	UNHCR	22.1	UNICEF	8.0	53.4	738.1
2004	IDA	474.2	CEC	161.9	AfDF	55.7	GFATM	16.6	UNICEF	10.0	11.4	729.8
2005	IDA	275.2	CEC	155.8	AfDF	114.7	GFATM	68.6	UNICEF	10.9	-3.2	621.8

Source: OECD/DAC

4.2.2. Financial Aid, Growth, and Macroeconomic Stability

Macroeconomic Policy Environment in Tanzania

The case for a stable macroeconomic policy environment as a necessary condition for rapid economic growth and for effective aid implementation has been emphasized in recent years. According to World Bank (1990), this involves low and predictable inflation, appropriate real interest rate, exchange rates which are competitive and predictable, stable and sustainable fiscal policy, and a balance of payment which is perceived viable. The effectiveness of foreign aid will be greater when there is macroeconomic stability and few distortions. Distortionary policies such as trade restrictions and financial repression reduce the effectiveness of foreign aid and the rate of economic growth for a given level of aid.

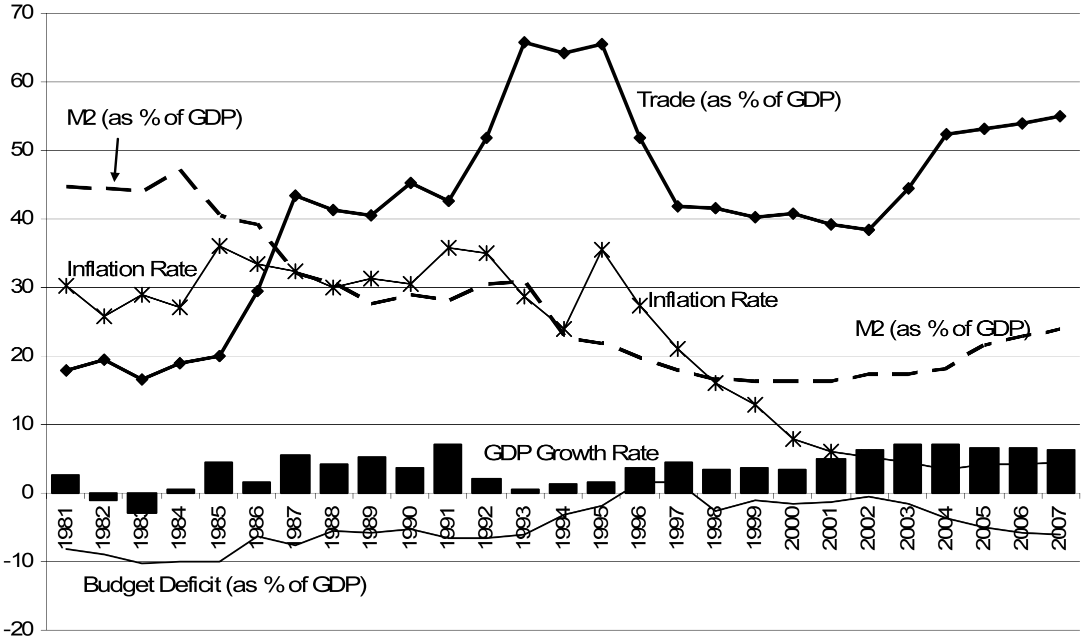
The World Bank (1990) emphasizes that reductions in fiscal deficits have been at the core of successful stabilization programmes and are prerequisites for successful structural adjustment and improved efficiency of investment. Thus, reducing a fiscal deficit could be expected to improve growth performance.

Figure 4.3 shows the trend of macroeconomic variables in Tanzania for the 1981-2007 periods. The sluggish performance of the economy in the 1980s and the first half of the 1990s, when real GDP growth rates never exceeded 4.5 percent were attributable to, among other factors, the impact of poor performance of the international trade, high and unpredictable inflation, and unsteady fiscal management. Fischer (1993) regards the inflation rate as the best indicator of macroeconomic policies, with the budget surplus as a second indicator. The inflation rate indicates the overall ability of the government to manage the economy: high inflation rates implying that the government has lost control, since high inflation rates on average tend to be correlated with high inflation variability, the latter might also indicate the prevailing macroeconomic climates with regard the fiscal variable.

During the early 1980s, and leading to the 1986 balance of payment crisis, macroeconomic conditions in Tanzania deteriorated sharply as a result of unsustainable economic programme and economic price shock, consequently real GDP growth declined sharply, while consumer price inflation took off averaging 30 percent annually. Larger imbalances in the country's fiscal and external accounts emerged. The major liberalization initiatives affected the inflation rate since the mid-1980s. Inflation rate fell from 36.1 in 1985 to 4.2 in 2005. The government identifies that this is one of the greatest achievements and maintains that this provides the basis for growth. GDP growth rate rose from 1.5 percent in 1986 to 7.2 percent in 2003.

Trade liberalization as one of the structural adjustment programs concern was adopted from the second half of the 1980s aiming at improving trade and enhances economic development following failure of the restrictive policies to achieve the desired objectives. By 1993/94, the system of exports licensing for both traditional and non-traditional commodities was abolished, the requirement of registration of exporting companies eliminated. The relaxation of trade restrictions was supported by strong macroeconomic stabilization measures, which brought about a substantial fall in inflation, as well as steps to correct the exchange rate misalignment, reflected in a depreciation of the real exchange rate. More concerted efforts at trade liberalization and other economic reforms were undertaken from the mid 1990s to create an environment that is conducive both to domestic and foreign investment. Between 1993 and 2000, all trade restrictions (except for goods restricted for health and security) were abolished, a foreign exchange market was introduced while the fixed exchanged rate was replaced by market-determined exchange rate. In 1996, Article VIII of the IMF was adopted, which liberalized all current account transactions. By end of the 2003, non-tariff barriers were almost eliminated and largely confined to restriction on petroleum imports.

Figure 4.3 Macroeconomic Variables and GDP Growth Rate, 1981-2007

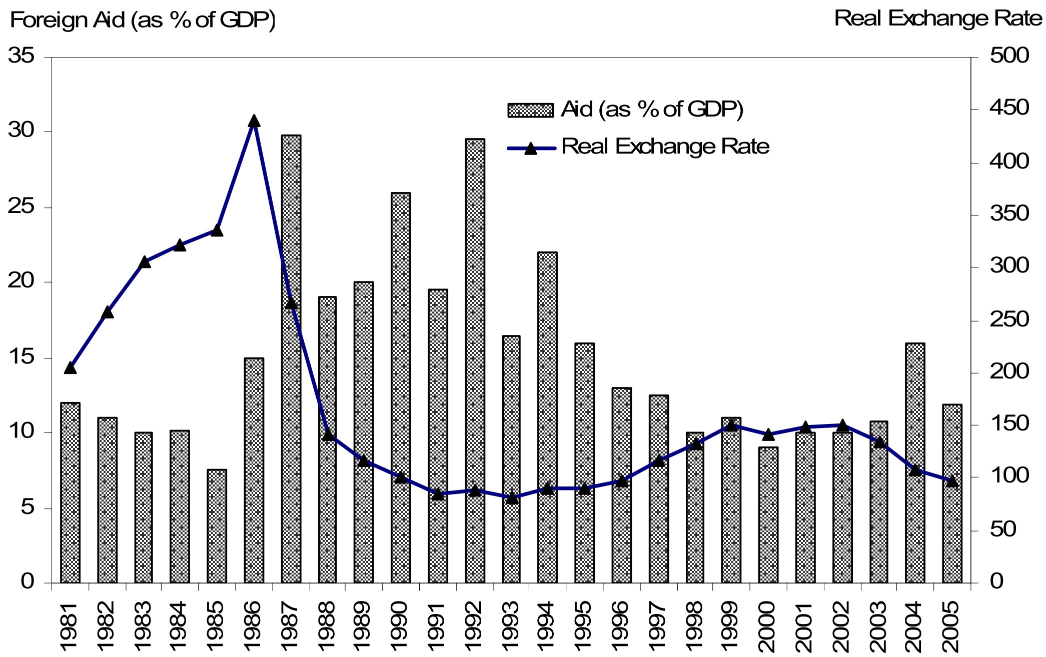


Source: BOT various issues and Authors' Estimates

A conventional way of measuring this is the degree of openness computed as the share of trade values (imports plus exports) in GDP. The coefficient of openness rose steadily from 2.7 percent in 1981 to 65.7 percent in 1993, however, the rate of GDP growth fell from 2.7 percent to 0.6 percent during the same period. Whether openness has led to economic growth in Tanzania is still, however, an empirical question, but there seems to be a general agreement that trade openness and increase in volume of import is one of a central elements of successful growth of the economy. During the first half of the 2000s the degree of openness averaged 45 percent, whereas the GDP growth rate improved steadily, averaging 6 percent during the same period, implying a negligible impact of trade to the economy.

Foreign aid that is spent in the local economy contributes to an increase in the demand for both tradables and non-tradables. When tradable goods prices are fixed by the international prices it is non-tradables prices that would tend to increase the pressure of the expanded liquidity on domestic demand and prices of non-tradable goods would lead to a real exchange rate appreciation. Figure 4.4 indicates that no such relationship appears to be present in Tanzania. In fact the series are highly negatively correlated, that is depreciation (appreciation) of real exchange rate is associated with increase (decline) in foreign aid flows. The equilibrium relationship described could be muted on nonexistent for number of reasons. There may be no changes in the real exchange rate if aid is spent entirely on imports, implying no impact on money supply or aggregate demand in the local economy. Alternatively, if the economy receiving the inflows is characterized by unemployed resources then the increase in demand generated by aid inflows may not lead to an increase in non-tradables prices. Import purchases and unemployed resources can explain why there may be a muted or no response in the real exchange rate to an aid surge but they do not explain the observed negative relationship in Tanzania. There are numerous theoretical explanations for this relationship, but proper multivariate framework that accounts for the nonstationarity of these series and controls for other factors is necessary before this relationship can be taken seriously.

Figure 4.4: Foreign Aid Flow and Real Exchange Rate



Source: OECD-DAC, Bank of Tanzania, and Authors' Calculations

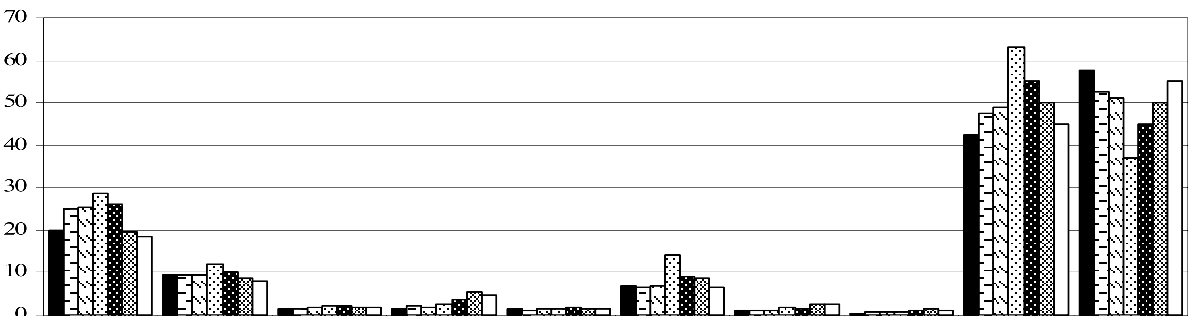
Furthermore, studies indicate that the stabilizing role of the government is proxied by references to its action in mobilizing resources as captured by the budget surplus. This is defined as the sum of current and development revenue including grants less the sum of current and development expenditure as a percentage of GDP. Fischer (1993) argues that a fiscal deficit also serves as an indicator of a government that is losing control. However, Tanzania has experienced an increasing level of public expenditure over time. This has tended to be associated with rising fiscal deficit suggesting its limited ability to raise sufficient revenue to finance higher levels of expenditure. The recurrent expenditure constitutes an increasingly and disproportionately large share of total spending, especially in the reforms and post reforms period compared to that on development expenditure, and servicing of foreign debt absorb an increasing share of recurrent revenue.

During the 1980/81-2004/05 period, total government expenditure/GDP ratio averaged 21 percent. During the same period tax revenue/GDP ratio was 13 percent whereas current revenue/GDP ratio was 14 percent. As a result the country recorded large deficits in the fiscal budget and the balance of payments account. The progress made in economic reforms so far is being undermined by fiscal and financial difficulties. There was a serious shortage of revenue, inadequate financing for critical development activities, and unstable fiscal situation during the period 2003 and 2007. However, the sharp decline of government budget deficit from Tshs 783,433 million in the 2006/07 to Tshs 1219.8 million in 2007/08 was mainly due to increase in grants. Grants rose from Tshs 952225.5 million in the 2006/07 to Tshs 1573195.4 million in the 2007/08 (BOT, 2008).

During the early phase of liberalization and reforms, the budgetary deficit narrowed. There was a decline in the fiscal deficit, due mainly to a sharp drop in expenditure in relation to GDP from 30.4 percent in 1982-84 to 22.6 in 1988-90. During this period tax effort fell from 20.1 to 18.3 percent. There was a setback in the period between 1985-87 and 1991-93. The revenue-GDP ratio went up slightly from 22.3 to 22.9 percent leading to falling in budget deficit from 6.7 to 4.2 percent of GDP (BOT, 1994). The government attempted to improve fiscal situation by lowering the tax rates and broadening the base, and reducing expenditure. But the measures were not enforced effectively enough to offset revenue lost by tax simplification. The weak tax administration found it difficult to widen the tax base while dropping rates. Enforcement was insufficient to compensate for the drop in rates.

From the period between 1994 and 1996 onwards the budgetary deficit has been increasing. In the 1995/96, the Government again intensified its efforts to bring the fiscal situation in line. A mid-year budget was adopted to raise revenues and enforce tighter spending controls. Restrictions on check issues by line ministries were proposed, and banks were given authority to reject checks in excess of funding limits. However, performance remained below expectation due to weak administration and overrun on current expenditures from various sources, including wage payments, clearing of arrears to the electricity corporation, retrenchment costs of the civil service reform and higher than expected interest payments on domestic debt. Moreover, in the mid 1995 the Government of Tanzania started to tighten fiscal policy under pressure from the international lenders to (i) raise revenue and tighten spending (ii) reduce spending in selected areas (iii) restructure so as to increase spending in critical areas such as education, health, agriculture, water, and infrastructure services (iv) enforce accountability and adherence to financial rules and budgetary ceilings (World Bank, 1996). However, priority sector expenditure has not consistently grown faster than expenditure on non-priority sector. Indeed, this seems to contradict the intension of the Poverty Reduction Strategy Paper (PRSP). Figure 4.5 illustrates that over the 1999-2005 period, there was a shift in budgetary shares first toward and then away from the priority sectors identified in Tanzania's PRSP.

Figure 4.5 Tanzania: Sector Shares for Priority and Non-Priority Sectors (as Percent of Total Expenditures Excluding Interest), 1999-2005



1999	20	9.5	1.5	1.5	1.5	7	1	0.5	42.5	57.5
2000	25	9.5	1.4	2	1.1	6.5	1.2	0.7	47.4	52.6
2001	25.5	9.5	1.7	1.9	1.4	7	1.2	0.8	49	51
2002	28.5	12	2	2.5	1.4	14	1.8	0.8	63	37
2003	26	10.3	2	3.5	1.8	9	1.4	1	55	45