STUDY 1

TANZANIA'S MACROECONOMIC AND FISCAL REFORMS - POSITIVE DEVELOPMENTS

(MID-TERM REVIEW OF THE 5 YEAR PLAN)

EXECUTIVE SUMMARY

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INTRODUCTION

The main goal of this report is to present findings of the interim review which sought to perform an in-depth analysis of the macroeconomic and fiscal reforms in Tanzania amid the implementation of the second FYDP II (2015/16-2020/21). The study explores the current situation in relation to the implementation of the right and adequate macroeconomic and fiscal policies/reforms. In doing so, this report highlights three key areas that inform macro-financial performance of the Tanzanian economy, focusing on achievements and vulnerabilities. The report also suggests ways to deal with these issues particularly through policy dialogues. These broad areas are: monetary banking sector performance; fiscal and budgetary framework; and the external sector performance. Accordingly, the review team examines the main assumptions and drivers behind the macroeconomic and fiscal reforms made at midterm in order to analyze the main achievements and gaps in the implementation framework.

This study builds on a review of relevant documents and research. Evidence assessed during the review process includes national surveys and reports, sector reports, annual reports from different stakeholders, studies and information issued from the World Bank, IMF databases and different FYDP reports. Apart from that, for triangulation purposes, the review team made field visits in the regions of Mwanza, Shinyanga, Moshi, Dodoma and Dar es salaam to check on reliability and consistency of the secondary data and reports.

KEY FINDINGS

Intermediate Outcomes: Macroeconomic Performance

The average GDP growth during the reform period was significantly positive despite a slow start in 2015 due to the cumulative impact of a decline in net foreign budgetary inflows, weak private sector cash flows associated to subdued global demand and a higher caution among banks arising from global uncertainties and higher regulatory standards. This also led to a massive deterioration of credit to the private sector from 24.8% in 2015 to 1.7% in 2017. This improved to 11% in 2018 but deteriorated further to 3% in 2020 (Bank of Tanzania, 2015-2020). Consequently, the annual change in extended broad money supply (M3) also decreased from 18.8% in 2015 to 5% in 2020. Strong signs of economic recovery started showing in 2016 and gained momentum in 2017 and 2018 with an average GDP growth rate of 6.7%. Nonetheless, by the end of the first quarter of 2021, the average growth rate of GDP has declined to 4.7% and it is estimated that it will remain around 4.5% throughout 2021[1]. This decline was largely due to the outbreak of COVID-19 pandemic that stormed the World as of the end of 2019. Despite that, the country's inflation rate has been the least volatile and one of the lowest in the East African Community. In December 2020, inflation reached 3.6%, up from 3.4% a year before but still below the 5% medium- term target.

[1] This information is based on the speech of the President of the United Republic of Tanzania, Honorable Samia Suluhu Hassan when she was addressing the Parliament on 22 April 2021 and A World Bank Report of Tanzania Economic Update, February 2021 Issue.

Moreover, by 2020, the Current Account Deficit (CAD) narrowed to USD 1.2 billion, down from USD 4.5 billion in 2015 whereby the value of exports reached USD 5 billion. Despite the challenges of COVID-19 pandemic, by December 2020, the value of exports of goods and services was USD 9,572.3 million in comparison to USD 8,124.9 million in 2015; representing an increase of 18%. Moreover, official gross reserves reached USD 6 billion in 2020, up from USD 4 billion in 2015; they are adequate to cover 6.4 months of imports of goods and services, above the government threshold of 4 months and the SADC and EAC requirements of 4.5 and 6 months.

In addition to that, the Tanzanian Shilling has been stable during the reform period. Following the reforms in 2015-2020, the Tanzanian Shilling depreciated by only 1.6% relative to an average depreciation of 4% during the previous regime.

Intermediate Outcomes: Fiscal Performance

During the reform period, we observe a notable increase in capital expenditure and a decrease in recurrent expenditure. In 2015-2020, capital expenditure amounted to an average of 6% of GDP whereby the largest share of development spending was directed to big infrastructure projects, transport and energy sectors. With respect to deficit, the country has improved its fiscal position since 2015 whereby on average, budget deficit has been reduced by 2.5% of GDP relative to a pre-reform period.

Final Outcomes

Tanzania has achieved some major macro fiscal and monetary improvements. A very notable achievement is the Tanzanian economy being upgraded from low to lower-middle income status in 2020 with a GNI of USD 1,080. Domestic revenue was 14.6% of GDP in the reform period. Tax revenue was short of the target by about 2.4%; however, that is much better than in pre-reform period where targets were missed by more than 10%.

Sector wise, the reforms in the mining sector have tremendously improved the growth the sector to reach 17% by the end of 2020, exceeding a target set of 3.2% by 2021. This exceeded expectations by around 14%. However, the tourism sector started very well with an annual average revenue of USD 2.6 billion. Unfortunately, by 2020, the rate of growth of the sector declined by 80% mainly due to the COVID-19 pandemic. The manufacturing sector has underperformed contrary to expectations. This has also affected the rate of FDI flows into the country whereby the government has met only 10% of the targeted FDI by 2020. Thus, there is a need to set policies that will improve FDI, boost the manufacturing sector GDP's contribution, and to launch reforms to help the recovery of the tourism sector. These are crucial sectors for economic development in Tanzania

With the exception of the maternal mortality ratio, social indicators have also tremendously improved. Before reforms power capacity was just a third of what it is now. The country was literally in darkness. More than 28% of the country was under the poverty line. Poverty has declined from 28.2% in 2015 to 26.2% in 2019. This makes a palpable difference in people's standards of living.

Lessons Learned

1. There has been a decline of the relative share of agriculture to the GDP over time, while the contribution of the service sector to the GDP has been increasing. On the other hand, the share of the manufacturing sector to GDP is very low. The main characteristic of a growing economy is the reduction of the GDP share of agriculture and a rise of the GDP share of the manufacturing sector, followed by a rise in the share of services sector. In addition to that, the industrial sector in Tanzania did not grow over time and the transfer of labour occurred mainly from agriculture to lowly paid services, rather than industries.
2. Fiscal performance has still some way to go. The gross fiscal deficit has come down from 3.4% of GDP in 2015 to 1.4% of GDP in 2020. However, this needs to go to 0.5% of GDP by 2025 in order to enable the government to sustain the economy. Moreover, tax revenue has recovered to almost 15% of GDP from 13.9%, but this needs much greater growth. According to the Economic Survey (2019), 35 to 55% of the revenue in Tanzania is not taxed. Thus, the government should focus on maximizing on untaxed sources of revenue. To increase government revenue, improving the business environment is also crucial.
3. There has been a reduction in the incidence of poverty, important impact growing income inequality has had on poverty reduction during the period. The impact of the reforms on the distribution of income is negative. The magnitude of income inequality, as measured by the Gini Coefficient, has increased over time.
4. A surge in public investment in Tanzania in the 2015-2020 period has prompted interest regarding the optimal scope of public investment. Critics have showed concern over public investment and worry that Tanzania could be investing too much in public expenditure at the expense of private investment and social services. Results derived from a two stage least square estimates show that on average, one extra dollar of public investment raises private investment by roughly 2 USD and output by 1.5 USD. These results imply a strong degree of complementarity between private and public capital because of the high economic return from development projects, and of the fact that Tanzania still faces a deficit in infrastructure.

Cross Cutting Issues

1. Effective implementation and localization of SDGs in Tanzania is constrained by a limited sense of ownership of the SDGs within the political arena. Specifically, the main gaps include: limited involvement of LGAs in the implementation framework of SDGs; the level of awareness on SDGs is low among the public; the involvement of CSOs/NGOs in SDGs implementation framework is inadequate, and the current SDGs implementation plan only considers a short-term perspective.
2. Field evidence shows that out of the 10 constraints on ease of doing business (i.e. Enabling environment, Starting a business, Dealing with construction permits, Getting electricity, Registering property, Getting credit, Protecting minority investors, Paying taxes, Trading across borders, and Enforcing contract Resolving insolvency) the private sector is most constrained by paying taxes, trading across borders, and getting credit.

3. Field data shows that more than 50% of surveyed traders use online forums to effect transactions which are not regulated and not subject to any tax payments. Traders shared with the review team that when TRA closes their businesses due to high tax estimation, they continue with online customers, which does not involve any disturbance from the government including registration of business and so on. This signifies how crucial it is for the government to start seriously considering and properly document the digital economy.
4. A survey made in five regions of Mwanza, Shinyanga, Moshi, Dodoma and Dar es salaam shows that the level of successful participation of youth in agribusiness is still low. Based on a survey, the main barriers to youth's participation in agribusiness include lack of access to market information, lack of skills, lack of access to capital, and lack of access to land.

Policy Recommendations

1. The government could use Township and village Enterprises (TVEs)[2] which involve the use of small-scale processing industries managed at the local level to add value to agricultural products. These will later become big industries. This model has been very successful in China and more than 70% of TVEs in China became very successful plants 20 years later.
2. A new approach to hub development, agglomeration and clustering will be deemed essential, with the focus on building sustainable, specialized parks that apply a plug- and-play model in order to boost industrialization.
3. The government could consider temporarily waiving the payment of TALA/license fee of USD 2,000 in the tourism sector, since most tour operators did not do significant business this year due to the COVID-19 pandemic. This was a request of 95% of tour operators surveyed in the Moshi region.
4. The government could consider designing or formulating a Unified Enterprise Law (UEL) and a Common Investment Law (CIL) to reduce bureaucracy and to improve the business environment.
5. The government should consider designing a proper digital economy strategy including the establishing a ministry of communication and digital economy.
6. The government could enhance effectiveness in the implementation and localization of SDGs by ensuring that:
7. LGAs collaborate with the National Bureau of Statistics (NBS) to develop baseline segregated local data and indicators for local monitoring and adopt the available toolkits for the localization of the SDGs.
8. An awareness raising strategy is made and tailored for targeted groups. It would be more effective than a general public approach in terms of promoting public support of SDGs.
9. All SDGs documents and materials are translated into Swahili to enable more public outreach.
10. A long-term national framework is developed, specific to the 2030 Agenda, and complementing the national sustainable development strategy under the FYDP.

[2] For more information on Township and Village Enterprises (TVEs), please visit: https://www.researchgate.net/publication/24083952_Township_and_Village_Enterprises_in_China/link/0deec525bfaf28eff8000000/download

11. There is a need to advocate and adopt the SUGECO Model[3] of engaging youths in agribusiness by the LGAs and other stakeholders. The mode has proven to be very successful in engaging youths in agribusiness in Tanzania. Moreover, this model should also be used in designing the new National Strategy for Youth Involvement in Agriculture (NSYIA for 2022-2026). To improve the model, it is important to link irrigation infrastructure/systems to block farming in order to enable an improvement of the whole value chain of agribusiness.
12. Consideration should be given to establish an integrated management information system for monitoring and evaluating the FYDP implementation and reform process in general.

CONCLUSION

During the 2015-2020, we have had a rapid economic growth which enabled Tanzania to enter into a lower middle-income country ahead of schedule; poverty has been reduced; the external sector is comfortable; and all this has been achieved with stability in the country. As a consequence of all these momentous changes, there is a new respect for Tanzania, and even more importantly other African countries are eager to use the Tanzanian model for macroeconomic stability.

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[3] For more information on the SUGECO model, please visit: https://pilot4dialogue.com/publications/policy_brief_3/