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

In the context of the fifth review under the three-year arrangement under the Poverty Reduction and Growth Facility, the following documents have been released and are included in this package:

- the staff report for the Fifth Review Under the Poverty Reduction and Growth Facility, prepared by a staff team of the IMF, following discussions that ended on February 28, 2006, with the officials of the United Republic of Tanzania on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 24, 2006. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a staff statement of April 6, 2006 updating information on recent developments.

- a Press Release summarizing the views of the Executive Board as expressed during its April 7, 2006 discussion of the staff report that completed the review.

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

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

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

*Also included in Staff Report

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

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UNITED REPUBLIC OF TANZANIA

Fifth Review Under the Three-year Arrangement Under the Poverty Reduction and Growth Facility

Prepared by the African Department

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

Approved by David Nellor and Michael T. Hadjimichael

March 24, 2006

- **Main topic.** This report recommends completion of the fifth review under Tanzania's three-year Poverty Reduction and Growth Facility (PRGF) arrangement. Completion of this review will entitle Tanzania to a disbursement of SDR 2.8 million (Table 1). The government's letter of intent (LOI) relating to this review is presented in Appendix I. This report will be discussed together with the Ex-Post Assessment (EPA) of Longer-Term Program Engagement, as well as a Joint Staff Advisory Note (JSAN) on Tanzania's second-generation Poverty Reduction Strategy Paper (PRSP), MKUKUTA.

- **PRGF performance.** The main goals of the program continue to be higher growth and further reduction of poverty, guided by MKUKUTA. The program remains broadly on track (Appendix I, Tables 1 and 2). All end-September 2005 quantitative performance criteria were met, though the net domestic assets (NDA) indicative target was missed. All quantitative indicative targets for end-December were met, except the reserve money and net domestic assets ceilings which were exceeded by small margins. The structural reform agenda is broadly on track.

- **Recent developments and prospects.** Economic growth, inflation, and the external position have been evolving in a manner broadly consistent with program assumptions. The authorities' immediate challenge is addressing the impact of drought, which will impact growth in 2006 and put pressure on the budget. For the medium term, challenges center around mobilization and efficient use of public resources, managing liquidity pressures from high aid inflows, and facilitation of private sector-led growth, while maintaining a sound macroeconomic framework. The authorities expressed interest in beginning negotiations in May on a program under the Policy Support Instrument (PSI).

- **Multilateral Debt Relief Initiative (MDRI)**. Fund debt stock relief of approximately US$336 million (including HIPC relief) was granted in January 2006. Additional debt relief from the International Development Association (IDA) and the African Development Fund (AfDF) is expected later this year.

- **Mission discussions.** Discussions were held in Dar es Salaam during December 1-15, 2005 and February 13-28, 2006 by a staff team comprising Messrs. Sharer (head), Dohlman, and Sobolev, and Ms. Everaert (all AFR), and Messrs. Tareen (PDR) and Adedeji (FAD). The mission met with President Kikwete, outgoing President Mkapa, the Minister for Finance (Mrs. Meghji), the Permanent Secretary for Finance (Mr. Mgonja), the Governor of the Bank of Tanzania (BoT) (Mr. Ballali), and other official and private sector representatives. Mr. Masawe (Executive Director's Office) also participated in the discussions. The mission was assisted by Ms. Schmitz (Senior Resident Representative).

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List of Acronyms

AfDF	African Development Fund
ASYCUDA	Automated System for Customs Data
BEST	Business Environment Strengthening in Tanzania
BFIA	Banking and Financial Institutions Act
BoT	Bank of Tanzania
CAS	Country Assistance Strategy
CPI	Consumer Price Index
DFGF	Development Finance Guarantee Facility
DFI	Development Finance Institution
EAC	East African Community
EPZ	Export Processing Zone
FSAP	Financial Sector Assessment Program
FSRP	Financial Sector Reform Program
GDP	Gross Domestic Product
HIPC	Heavily Indebted Poor Country
IDA	International Development Association
IFEM	Interbank Foreign Exchange Market
IFMS	Integrated Financial Management System
IRT	Investors' Round Table
ITRS	International Exchange Transactions Reporting System
JSAN	Joint Staff Advisory Note
LGA	Local Government Authority
LTFF	Long Term Financing Facility
LOI	Letter of Intent
LTD	Large Taxpayer Department
MDA	Ministries, Departments, and Agencies
MDGs	Millennium Development Goals
MEFP	Memorandum of Economic and Financial Policies
MKUKUTA	Swahili name for NSGRP (PRSP)
MTEF	Medium-Term Expenditure Framework
NDA	Net Domestic Assets
NDS	National Debt Strategy
NIR	Net International Reserves
NMB	National Microfinance Bank
NSGRP	National Strategy for Growth and Reduction of Poverty (PRSP)
PEFAR	Public Expenditure and Financial Accountability Review
PER	Public Expenditure Review
PRBS	Poverty Reduction Budget Support
PRGF	Poverty Reduction and Growth Facility
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
PSRP	Public Service Reform Program
PSI	Policy Support Instrument
ROSC	Report on Observance of Standards and Codes
SBAS	Strategic Budget Allocation System
SEZ	Special Economic Zone
TANESCO	Tanzania Electric Supply Company
TJAS	Tanzania Joint Assistance Strategy
TRA	Tanzania Revenue Authority
VAT	Value-Added Tax

Executive Summary

Tanzania's sustained reforms have generated strong macroeconomic performance. Nevertheless, per capita income remains very low, and Tanzania will need to maintain high growth, low inflation, and a steady pace of structural reforms for many years to achieve significant inroads against poverty. The new government, guided by Tanzania's new poverty reduction and growth strategy paper—MKUKUTA in Swahili—is committed to steadily pursuing these objectives.

The economic reform program has remained broadly on track. All end-September 2005 quantitative performance criteria were met. All quantitative indicative targets for end-September and end-December were met, except the reserve money (December only) and net domestic assets ceilings which were exceeded by small margins. The structural reform agenda is also broadly on track, notably the reform of tax and customs administration and of the financial sector.

The government is making strong efforts to implement the FY 2005/06 (July-June) program. However, the drought in late 2005 now threatens economic performance through its impact on agricultural output and availability of hydroelectric power and will necessitate additional payments from the budget. Together with the higher domestic interest costs, net domestic financing of the budget for 2005/06 is expected to reach 2.6 percent of GDP compared with 1.1 percent in the original program. The staff believes that the higher domestic financing can be accommodated in the monetary program so as not to unduly constrain strong private sector credit growth to productive sectors.

A principal challenge for monetary policy continues to be liquidity management in the face of high foreign aid inflows. The program's proposed paths for reserve money and M3 are consistent with strong private sector demand for credit and should help ease pressures on interest and exchange rates and meet growth and inflation objectives.

The government is actively considering measures to address the crisis situation in the energy sector. In this regard, the government's efforts include planned installation of additional generation capacity and development of a time bound, monitorable financial recovery plan for the state energy parastatal TANESCO as well as a medium-term plan to enhance generation capacity in support of the medium-term economic growth objectives.

The government has decided to place the Fund's MDRI resources in a special account at the BoT to be used to fund the foreign exchange component of high priority pro-poor social outlays and growth-critical economic projects. It is envisaged that some of the funds may be spent during the remainder of 2005/06 to redress the impact of the drought to alleviate food and power shortages

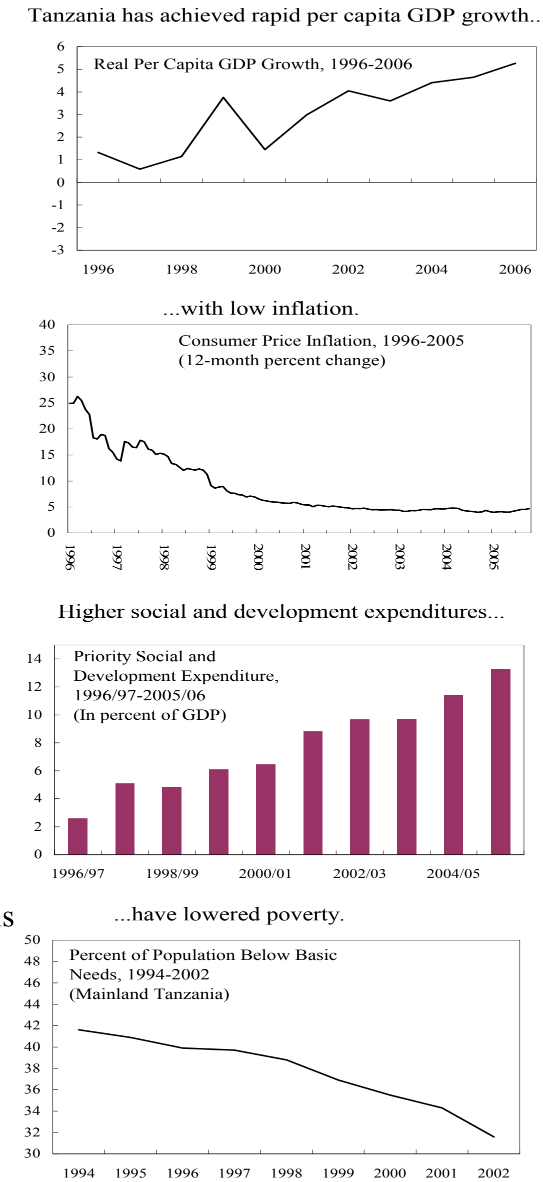
The staff supports the authorities' request for completion of the fifth review under the current PRGF arrangement.

I. Background

1. **Tanzania has made major strides over the past decade (Figure 1 and Table 2).** Per capita GDP growth has accelerated to nearly 5 percent, inflation has declined to around 5 percent, expenditures in priority areas have increased, and social indicators have improved. Institutional capacity has also improved, including stronger structures for domestic revenue mobilization, public expenditure management, and the financial sector.

2. **Achieving even faster growth and poverty reduction is high on the new government's agenda.**[1] It recognizes that, despite recent successes, Tanzania remains a very poor country with low per capita income, low trade volume, high cost of doing business, inadequate basic infrastructure, and a financial sector—while growing rapidly—that still plays only a limited role in the economy. The new government is committed to steadily pursuing its agenda in the context of a sound macroeconomic framework with strong structural reforms, guided by MKUKUTA and the Millennium Development Goals (MDGs).

Figure 1. Achievements and Challenges



Sources: Tanzanian authorities; IMF, staff estimates, World Economic Outlook, International Financial Statistics; and World Bank, World Development Indicators.

II. Recent Economic Developments and Performance Under the Program

3. **Macroeconomic performance under the program has been good, but pressures are**

[1] The elections returned the ruling CCM party to power, with former Foreign Minister Kikwete as the new President. The elections, initially scheduled for October 2005, were delayed until December 2005 due to the death of a vice-presidential candidate.

now emerging. Available data indicate that during the first half of 2005/06, growth and inflation evolved broadly as envisaged.[2] However, a severe drought now threatens economic performance through its impact on agricultural output and on the energy sector through reduced availability of hydropower. The energy sector has also been adversely affected by sharply higher fuel prices and general weakness in TANESCO's financial performance, leading to an energy crisis (Box 1). Thus, the drought will necessitate emergency outlays from the budget and will reduce economic growth and increase pressure on prices in CY 2006, as noted below.

4. **During the first half of 2005/06, all program performance criteria and most indicative targets were observed (Appendix I, Tables 1 and 2).** However, the indicative targets for end-September and end-December for the net domestic assets of the BoT and end-December reserve money were missed by relatively small margins, reflecting higher interest costs, and continued challenges to liquidity management emanating from the sometimes uneven pace of government spending and accelerated outlays by the BoT. The structural reform agenda is also broadly on track.

5. **The government is making strong efforts to implement the 2005/06 program budget** (Table 3). Revenues during the first half of 2005/06 were consistent with the program targets, underpinned by on-going tax administration reforms. On expenditures, in areas within the authorities control, there were only very minor overruns. However, delays in donor disbursements during July-December[3] led to higher domestic borrowing which, in the context of thin and imperfect financial markets, uncertainty about national elections, and possible rising inflation expectations, contributed to a marked increase in interest rates. These factors increased liquidity management costs and raised domestic interest payments in the budget, which are expected to exceed the programmed amount by about 0.6 percent of GDP. In addition, the drought in late 2005 will necessitate additional payments from the budget, and the program targets for 2005/06 net domestic financing will be exceeded.

6. **During the first half of 2005/06, monetary aggregates evolved broadly in line with projections** (Tables 4 and 5, and Figure 2). Broad money continued to grow at a robust pace, and credit to the private sector grew at about 35 percent per annum, largely to productive sectors of the economy (MEFP, para. 7). Discussions with banks and the

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[2] The authorities are receiving joint technical assistance from East AFRITAC and TGS in reviewing CPI compilation work practices carried out by the National Bureau of Statistics staff and addressing some of the issues and concerns regarding the accuracy of the published CPI.

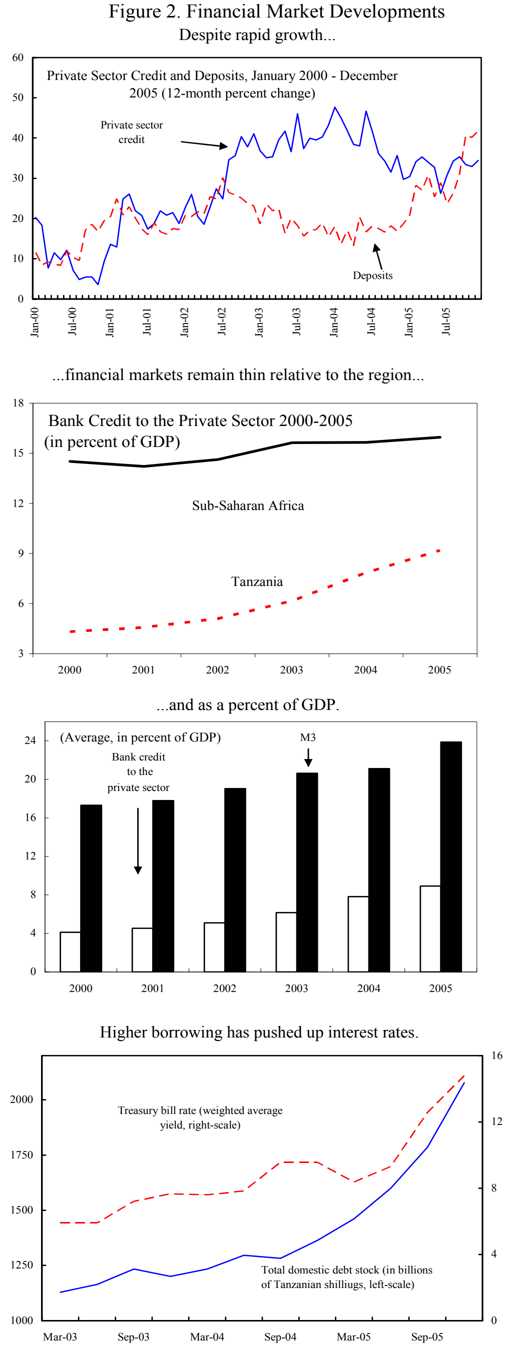
[3] There was a shortfall of US$156 million in the first half of 2005/06, mostly due to administrative delays and the impact of the Euro/U.S. dollar exchange rate. The bulk of this amount—that tied to administrative delays—is expected to be made up by the end of the fiscal year.

business community suggest that strong credit growth is likely to be sustained. Financial sector soundness indicators continued to be strong (Table 6), with the ratio of non-performing loans to gross loans remaining below five percent.

7. **A considerable build up of excess liquidity, mainly from an uneven pace of government payments and accelerated outlays by the BoT,[4] presented challenges to liquidity management.** Nonetheless, the BoT met the end-September reserve money target (performance criterion), and only narrowly missed the end-December indicative target, through scaled up sales of treasury bills, complemented by sales of foreign exchange and repurchase agreement transactions with commercial banks.[5] These actions put upward pressure on interest rates, as noted above (MEFP, para. 6).

8. **Despite a slightly weaker than expected current account performance, higher net capital inflows, resulting from the Fund's Multilateral Debt Relief Initiative (MDRI), supported the balance of payments during 2005/06** (Table 7 and Figure 3). Strong nontraditional export performance is contributing to an increase in export earnings, but the trade deficit is expected to be slightly higher than previously projected largely because of the drought-related surge in food and energy-related imports. Despite higher than expected sales of foreign exchange in the first half of 2005/06, the nominal exchange

Figure 2. Financial Market Developments



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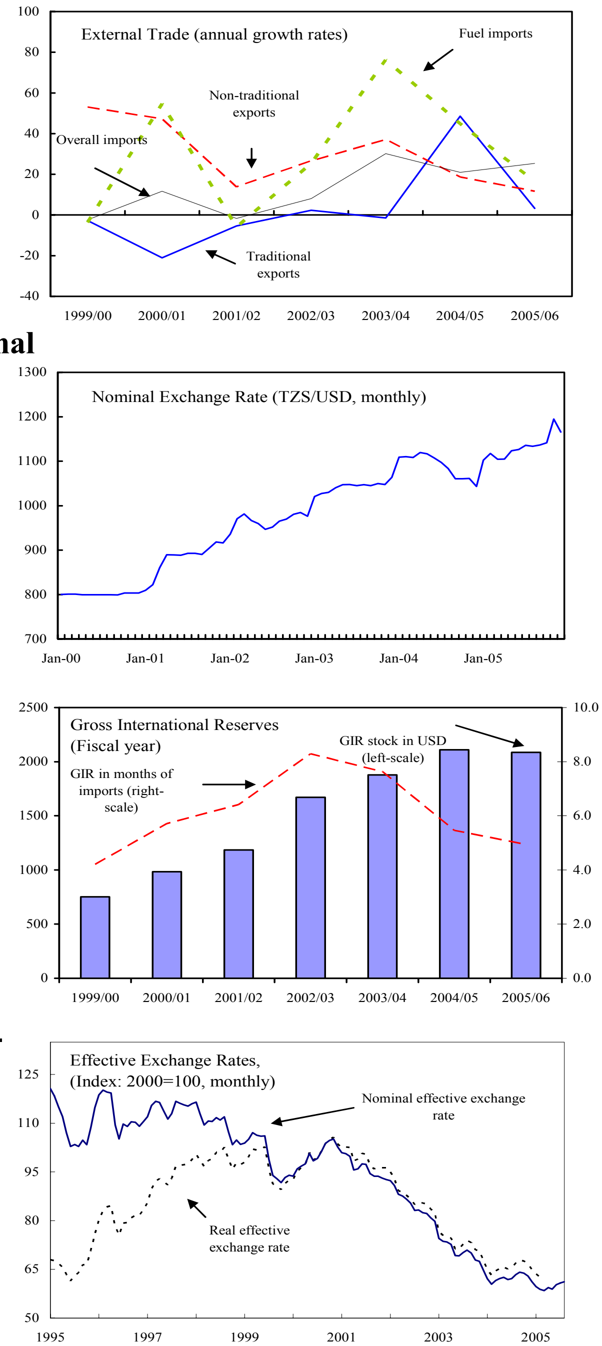
[4] These outlays were mainly related to construction of BoT headquarters.

[5] The BoT limits its interventions in the foreign exchange market to facilitate liquidity management and smoothing any short-run excessive fluctuations in the exchange rate.

rate of the shilling to the U.S. dollar depreciated by 5.3 percent from T Sh 1,126 at end-June 2005 to T Sh 1,186 at end-February 2006 reflecting the increased demand for foreign exchange due to elections, the impact of the drought, and possibly rising inflation expectations. The gross reserve coverage is projected to remain at around 5 months of next year's imports.

Figure 3. External Sector Developments



9. **Looking ahead, Tanzania's external position remains vulnerable to potential shifts in official donor inflows and external shocks**. The trends observed thus far are likely to continue in 2006/07 and beyond, namely further current account deterioration on account of higher growth of import demand, partially offset by strong non-traditional export performance and increased external inflows (particularly program assistance). Tanzania will equally remain vulnerable to weather-related shocks, given its dependency on rain-fed agriculture and hydropower. Maintaining external reserves at a prudent level will be essential to Tanzania's ability to safeguard its external position.

10. **Overall reforms under the FSAP-based second generation financial sector reform plan are also broadly on track.** The performance criteria relating to limits on government guarantees under several credit facilities were observed, and the authorities intend to require annual independent operational audits for the DFGF (end-March 2006 structural benchmark), once it becomes operational.[6]

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[6] The Development Finance Guarantee Facility (DFGF) and the Long-Term Financing Facility (LTFF) are still under development. A small SME scheme was recently launched (LOI, para. 3; MEFP, paras. 8, 24, and 25).

11. **The fiscal structural reform agenda under the program is also on track.** Substantial progress has been made in tax and customs administration, including the merger of the income tax and VAT departments at the TRA headquarters, increased coverage of taxpayers by the Large Taxpayers Department (LTD) and streamlining of customs' clearing procedure. In support of these efforts, the authorities have doubled the number of staff in the post-clearance audit section of customs (end-March 2006 structural benchmark) and integrated the destination inspection program with custom procedures in the Dar es Salaam custom offices (end-January 2006 structural benchmark). Substantial progress has been made in expenditure management, including implementation of the new Strategic Budget Allocation System (SBAS). However, the structural benchmark on approval by Cabinet of the new Anti-Corruption Law by end-April has been delayed by the prolonged period of the change of government and will not be met as envisaged. The authorities are currently in the process of reformulating their plans in this area to reinforce their anti-corruption agenda.

III. Report on the Discussions

12. **The discussions focused on updating the 2005/06 macro framework in the light of the challenges posed by the impact of the severe drought.** The authorities recognize that achieving their objectives of further accelerating economic growth and reducing poverty over the medium term will depend critically on: (i) improving mobilization of public resources and their efficient use; (ii) effectively managing liquidity in the presence of high aid inflows; and (iii) further enhancing the business environment, including strengthening the operations of the energy sector. At the conclusion of the mission, the new government expressed interest in beginning negotiations on a successor program to be supported under the PSI that would commence during the second half of 2006.

13. **The staff and the authorities have revised the projections for real GDP growth and inflation in 2006.** The inadequate short rains (November-December) adversely affected food production and resulted in a sharp reduction in hydropower generation leading to electricity rationing. While the impact of the drought is subject to considerable uncertainty, provisional estimates suggest that real GDP growth in 2006 is likely to be about 5.8 percent compared with the previously projected 7.2 percent. These estimates assume normal rainfall during the long rains season (March-May) and expeditious measures to address the deficit of power generation (MEFP paras. 12, 31-33), and will be reassessed during the next program review.[7] Energy-related price pressures are likely to increase in the coming months as businesses begin to fully pass on to consumers the increased costs, though the government's program of food distribution in the drought-affected areas and resumption of normal harvests should help dampen pressures on food prices. Under these assumptions, the annual rate of inflation in CY 2006 is expected to average about 6 percent compared with 4 percent

[7] In this regard, the mission underscored the urgency of securing additional generation capacity to minimize the impact of power rationing on economic activity.

previously projected, with some rise in 12-month inflation during the first half of the year from higher food and fuel prices, with a subsequent return to a normal path as the first round effects begin to wear off.

Mobilization and efficient use of public resources

14. **The programmed increase in revenues this fiscal year appears to be within reach.[8] However, the emergence of unplanned expenditures related to the drought, together with the higher domestic interest costs, would result in higher-than-programmed net domestic financing.** The program provides for emergency drought-related expenditures of T Sh 70 billion (0.5 percent of GDP) during the remainder of the year (MEFP, para. 15), associated with the purchase of food from the Strategic Grain Reserve and additional transfers from the budget to TANESCO. Domestic interest costs are expected to exceed the budget by 0.6 percent of GDP as noted above. Thus, total expenditure of about 28 percent of GDP (excluding use of IMF MDRI) is envisaged for 2005/06 compared with 26.8 percent of GDP in the original program. With slightly lower-than-anticipated net foreign financing and higher privatization proceeds, the staff and the authorities concurred that net domestic financing of the budget would reach about 2.6 percent of GDP, compared with 1.1 percent in the original program.

15. **The authorities recognized that achieving higher growth and poverty reduction over the medium-term will require continued improvements in public mobilization of resources.** They agreed on the importance of further boosting Tanzania's revenue-to-GDP ratio. In this regard, the authorities indicated that they will undertake further tax administration reforms, including: (i) further increasing the coverage of taxpayers by the LTD, (ii) possible merger of the LTD and Domestic Revenue Department, (iii) extending and strengthening the taxpayer segmentation approach for medium taxpayers, and (iv) further strengthening of customs post-clearance audit, risk management, and intelligence and rolling out of the Automated System for Customs Data (ASYCUDA++) to all major customs stations. The authorities indicated that the measures proposed by the recent Fund Tax Policy Review mission would be considered for inclusion in the 2006/07 budget. The staff expressed concerns about the extent of the tax incentives included in the legislation introducing Special Economic Zones (SEZs), which could adversely affect the tax base. The authorities indicated that caution would be exercised in implementing the SEZ legislation.

16. **To enhance the efficiency of spending and achieve MKUKUTA objectives, the authorities agreed on the importance of stronger linkages between costing of these objectives, the budget, the medium-term expenditure framework (MTEF), and a coherent medium-term macroeconomic framework (Box 2).** In particular, strong budget

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[8] The program target of T Sh 2,067 billion is unchanged, but revised estimates of nominal GDP have reduced it as a ratio. The revenue projection assumes normal long rains and that power rationing by TANESCO will not significantly affect key industries.

guidelines and processes will be critical to ensure that programmed expenditures are consistent with reasonable external and domestic financing of the budget, that effective criteria are used to determine sectoral priorities, and that achieving the MDGs is adequately costed. This will enable ministries to properly plan their expenditures. To further strengthen the transparency and accountability of expenditure management, the IFMS should be rolled out to eligible Local Government Authorities (LGAs) and combined with increased training of accounting staff and capacity building at the local government level. Efforts to strengthen the National Audit Office should be sustained and the staff welcomed the authorities' intention to provide sufficient funds for implementing capacity-building initiatives.

17. **The staff discussed with the authorities their provisional views for the 2006/07 budget, which should build on the progress made under the current PRGF.** In this regard, the mission agreed that the revenue projection of 14.4 percent of GDP for 2006/07 (compared with projected 14.2 percent of GDP in FY2005/06) was achievable so long as tax administration reforms continue to be vigorously pursued. Moreover, new tax policy measures could further expand the resource envelope. Presently, total expenditures of about 27 percent of GDP are envisaged for 2006/07. This should permit continued increases in MKUKUTA-related expenditures and lower expenditures on goods and services (as a ratio of GDP) as the 2005/06 budget includes a number of one-off expenditures (elections and food purchases), and energy-related emergency outlays.[9] Taking account of additional external assistance associated with the MDRI, it should be feasible to target net domestic financing in the order of 0.5 percent of GDP, consistent with the targets indicated in MKUKUTA. As discussed in Box 3, the Fund has already delivered US$336 million (including HIPC relief), or roughly 2.7 percent of GDP, in MDRI debt relief to Tanzania.[10] IDA and AfDF are still considering the modalities of their relief. The envisaged level of net domestic financing is consistent with allowing continued robust increases in credit to the private sector.

Liquidity Management

18. **There was agreement that a principal challenge to monetary policy is effectively balancing inflationary pressures associated with liquidity pressures from higher donor aid against upward pressure on interest rates and the exchange rate from sterilization operations** (Figures 2-4) [11] The authorities and the staff discussed the appropriate mix of

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[9] In this regard, the staff stressed the importance of providing any future budgetary support for TANESCO in the context of the financial recovery plan (MEFP, para. 32).

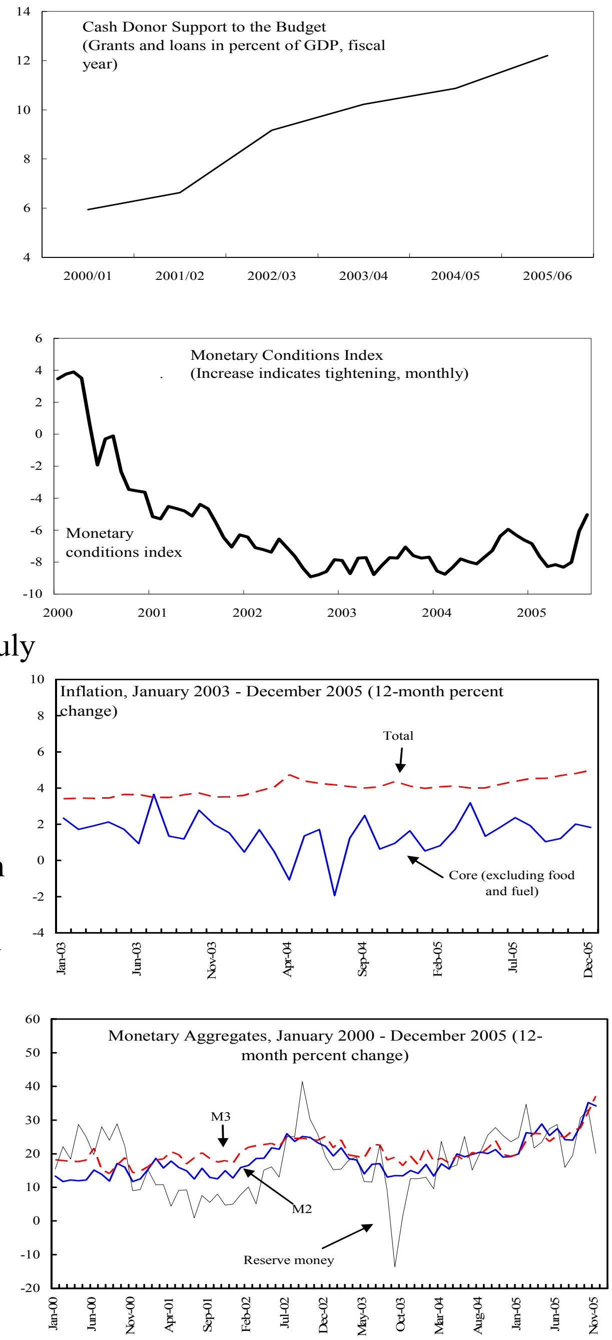
[10] The program includes adjustors for any additional use of IMF MDRI (beyond the envisaged US$50 million), as noted in Appendix I, Table 1.

[11] This issue has received considerable attention in the staff's discussions with the authorities and in recent staff reports. See Country Report No. 04/284 and Country Report No. 05/291.

intervention tools to achieve monetary targets, noting that the depreciation of the Tanzania shilling against the dollar during the first half of the year—while interest rates rose rapidly—suggested further room to increase sales of foreign exchange to complement sales of government paper in conducting liquidity operations. The authorities agreed, but continued to express concern about the potential loss of competitiveness from any appreciation of the exchange rate.[12]

19. **There was agreement that there is scope for a modest easing of monetary policy during the second half of 2005/06** to accommodate the higher net domestic financing of the government, so as to not unduly constrain strong private sector credit to productive sectors and for critical food imports.[13] It is expected that the proposed higher reserve money target (about 3.5 percent higher than originally projected by June) and M3 growth paths would, along with an unwinding of some of the pressures in the first half of the year and increased reliance on foreign exchange sales, help reverse pressure on interest rates and facilitate growth. While this accommodation risks some upward pressure on prices, thus far inflation has remained low, and driven largely by higher food and fuel prices with core inflation below 2 percent. The authorities are

Figure 4. Monetary Sector Developments



¹² They took note of staff arguments that the real exchange rate would remain around its equilibrium level and that external competitiveness is mostly affected by structural factors.

¹³ Under the revised program, M3 growth would rise by 30 percent by end-June 2006 from the previously projected 27 percent, while deposits would grow at similar pace. The projected fall in velocity is consistent with the deepening of the financial system and recent trends, and is unchanged from the program projections.

committed to closely monitor price developments and to take prompt action to contain any second-round effects on inflation (MEFP, para. 21).

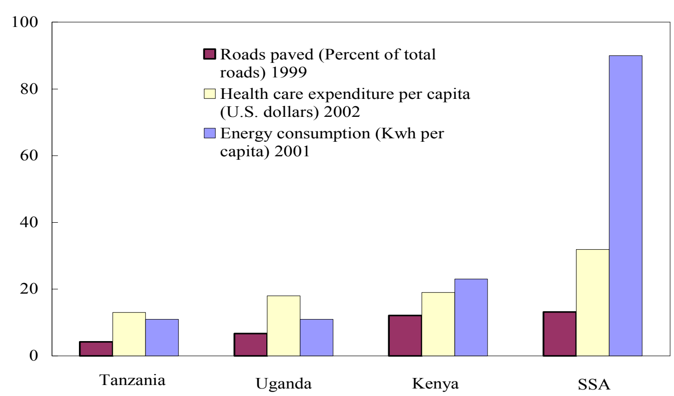
20. **The authorities agreed on the importance of strengthening liquidity management, including better forecasting and stronger measures to smooth the path of reserve money** (MEFP, paras. 18, 22).[14] The BoT and the Finance Ministry are jointly undertaking efforts to strengthen coordination regarding the flow of expenditures and are exploring means to reduce government balances in commercial banks, which would help ease liquidity pressures. Separately, the Finance Ministry is exploring measures to help reduce the large check float that occurs each year. The BoT also expressed its intention to move to some form of targeting average reserve money to help smooth its growth path.

Enhancing the environment for private sector-led growth

21. **The authorities recognize the importance of encouraging private sector led growth and investment and more effectively translating aid into higher growth to help achieve the authorities' overall growth and poverty reduction objectives.** A top priority is resolving the immediate crisis of power generation and ensuring a reliable supply of affordable energy over the medium term. In this regard, the mission emphasized the urgency for the new government to proceed expeditiously with securing additional generation capacity and finalizing the financial recovery plan for TANESCO as well as the medium-term Power Sector Strategy in consultation with the World Bank (structural benchmark, MEFP, paras. 31-33).

22. **The authorities are undertaking efforts to strengthen absorptive capacity and improve the supply response of the economy in the context of MKUKUTA** to enhance the enabling environment for productive private sector activity, and help reduce the relatively high cost of doing business (Figure 5). In this respect, a new private sector development strategy is being prepared, draft bills on Business Activities Registration and Reform of the Regulatory Licensing System are being finalized for submission to parliament by July 2006, and the government is undertaking reform of the crop boards. Anticorruption efforts are also underway to strengthen the government's ability to prosecute those suspected

Figure 5: Roads, Health Care, Energy



Source: Tanzania authorities, World Economic Outlook, International Financial Statistics, and World Bank World Development Indicators.

[14] A recent MFD mission on liquidity management and foreign exchange operations made a number of recommendations in these areas, which the BoT is currently considering.

of corruption.[15] Regarding efforts to establish SEZs, the authorities agreed to emphasize the strengthening of infrastructure and provision of efficient services.

23. **The authorities outlined their efforts to accelerate financial sector reforms designed to improve access to credit and facilitate the conduct of monetary policy** (MEFP, paras. 23-26). Specific near-term plans, undertaken in the context of the second generation financial sector reform plan, include submission of the BoT Act and the BFIA to parliament by end-April (a structural performance criterion). The acts are designed to boost the BoT's autonomy, accountability, and supervisory powers, and strengthen the financial sector. Separately, an inter-agency committee is developing a unified legal and regulatory framework and investment guidelines for pension funds for submission to government by end-June (structural benchmark).[16]

24. **In this same context, the authorities are continuing efforts to promote medium-term lending to productive sectors.** They are proceeding with plans to establish the DFGF later this year. Specifically, the authorities reaffirmed their commitment to limit the quasi-fiscal risks to the government from their medium-term lending initiatives, and to require operational audits—both structural benchmarks (MEFP, paras. 24-25). The staff was supportive of government efforts to increase term-lending, but reiterated that these initiatives should not distract from efforts to remove structural impediments to lending.

IV. Ex Post Assessment of Tanzania's Longer-Term Program Engagement

25. **An EPA of Fund-supported programs was discussed with the authorities during March 8-10, 2006.** The key findings and recommendations of the EPA are shown in the Executive Summary of that document, which is being issued with this report. The authorities were in broad agreement with the findings and recommendations of the assessment, and noted that the design of Fund-supported programs was broadly appropriate and that conditionality was both focused and balanced.

26. **Concerning program performance, the authorities provided a different perspective on certain policy issues.** On domestic revenue mobilization, they noted that the

[15] The new government is undertaking a broader review of its efforts in this area and is seeking to incorporate the recommendations of the Law Reform Commission into the new Anti-Corruption Bill prior to its submission for Cabinet approval. The new government is intending to give increased priority to efforts to combat corruption.

[16] The staff emphasized that the slight increase in 2005 over the previous year of the ratio of NPLs to gross loans (from 3.5 to 4.9 percent, Table 6) warrants close monitoring going forward.

performance reflected the nature of the economy, where a predominant share of economic activity was confined to the informal sector, because of which the tax base was narrow. They, nevertheless, recognized the need to broaden the tax base, including by promoting economic activity in the formal private sector, and for plugging loopholes and streamlining the provision of tax exemptions and incentives. The authorities considered that Fund-supported programs did not suitably prioritize spending to promote emphasis on infrastructure development. It was asserted that while the programs made a conscious effort—and rightly so—to promote social spending, greater emphasis could have been placed on boosting infrastructure spending, which they argued would have both improved the investment climate and facilitated greater aid absorption. On aid inflows, they concurred that it complicated macroeconomic management and that it required *inter alia* overcoming supply-side constraints to facilitate aid absorption. However, they also noted that channeling aid inflows for infrastructure spending is likely to be a challenge given the predisposition of donors to seek immediate impact of aid spending. On financial sector reforms, the authorities argued that the slower progress than projected under Fund-supported programs was largely because bank privatization required a change in the mindset of society at large, because of which building consensus took longer than anticipated. Regarding future relations with the Fund, the authorities concurred that a program under the PSI would be appropriate.

V. Program Monitoring

27. **The remainder of the program will be monitored through quantitative and structural performance criteria and benchmarks specified in Tables 1 and 3 of Appendix I.** Quantitative performance criteria and indicative targets for end-March 2006 are proposed, and understandings have been reached on indicative targets for end-June 2006. Structural conditionality focuses on financial sector reform, the energy sector, and governance. Program implementation will be assessed during the sixth review.

VI. Staff Appraisal

28. **Tanzania has demonstrated strong economic performance in recent years based on adoption of market-oriented, outward-looking policies within an appropriate macroeconomic framework.** Strong monetary and fiscal policies have underpinned key structural reforms, leading to accelerated growth, low inflation, and reduced poverty. Nonetheless, Tanzania remains a very poor country with serious capacity constraints and a heavy reliance on donor inflows. It is also vulnerable to further exogenous shocks, such as poor rains or higher oil prices.

29. **The staff welcomes the authorities' continued strong efforts to implement the program's macroeconomic and structural policies**. In particular, in areas within the authorities' control, fiscal policy has been kept on track despite pressures from a prolonged election campaign. These efforts will now need to be reinforced in the face of the challenges

of addressing the impact of drought on agricultural output and energy production. It will be essential that these challenges be addressed expeditiously and in a prudent manner.

30. **The staff believes that the authorities' planned response to the revised circumstances and prospects is appropriate.** The staff agrees that the higher net domestic financing should be accommodated, given the size and nature of the overruns, and that it would be imprudent to disrupt implementation of the budget at this stage. Thus, a slight loosening of monetary policy is warranted to avoid crowding out productive private sector credit demand. Nevertheless, the authorities will need to monitor closely the situation regarding inflationary pressures.

31. **Debt relief from the Fund under the MDRI is timely and will help the authorities to address pressing social and growth-critical economic challenges, especially those emanating from the drought.** The staff applauds the arrangements being introduced by the authorities to ensure that use of the MDRI relief from the Fund is channeled to these key areas of concern and does not impact domestic liquidity. The staff also applauds the planned regulations to ensure that use of these resources is subject to all regular procurement and financial management rules and can be tracked in a transparent manner, and to incorporate the use of MDRI in the budget, beginning 2006/07.

32. **Meeting the authorities' economic and social objectives will require efficient targeting of public expenditure.** In this context, the staff welcomes the authorities' efforts to better link the MKUKUTA goals to the budget process and the MTEF. This, complemented by further definition of a medium-term macroeconomic framework, should facilitate achieving key objectives, including the MDGs.

33. **The staff welcomes the authorities' ongoing and effective efforts to mobilize domestic resources.** The staff believes that these efforts are critical to providing resources for key expenditures and reducing somewhat the dependence on foreign aid. The staff strongly supports the authorities' ongoing tax administration reform efforts and believes that prospects for additional improvements, particularly in customs, are favorable. The staff welcomes the authorities' consideration of possible new tax policy measures to help support government policy objectives.

34. **The staff commends the BoT's ongoing management of liquidity pressures** and encourages the BoT to continue to use its full range of tools, including heavier reliance on foreign exchange sales and better management of government deposits in commercial banks, to help better distribute the impact of sterilization efforts on interest and exchange rates.

35. **The authorities' efforts to improve the business environment are, in the staff's view, central to enhancing growth through productive private sector activity.** Private investment is not yet increasing at a rate needed to materially reduce unemployment and poverty. Enhanced efforts are needed to stimulate private sector led investment and growth, particularly in such areas as infrastructure, energy, the business environment, and governance.

36. **In this context, the most pressing challenge to government will be resolving the supply issues of the energy sector without unduly burdening public finances.** The staff welcomes the authorities' intentions to develop a sound financial recovery plan to address the finances of TANESCO together with a Power Sector Strategy plan to address power generation over the medium term. The close involvement of the donor community in these efforts will be essential. The staff also welcomes the authorities' efforts to improve the monitoring of the preparation and implementation of these plans.

37. **The staff welcomes the government's ongoing commitment to** improve governance and limit government exposure under publicly supported bank lending schemes to support development and small and medium-sized enterprises. While also welcoming government efforts to attract investment, the staff cautions that this should be through strengthening infrastructure and providing efficient services rather than excessive new tax incentives.

38. **The staff welcomes the authorities' interest in a successor program in the context of a PSI.** This would be a logical development in light of Tanzania's position as a mature stabilizer.

39. **Based on the authorities' continued strong record of program implementation, and their commitments in the attached letter of intent, the staff recommends completion of the fifth review under the current PRGF arrangement.**

Box 1: The Energy Crisis

The crisis in the energy sector is dampening overall economic performance through shortfalls in energy production and pressure on the budget to fund current operations and investment. To maintain energy supplies to key industries and government installations, the authorities have introduced a system of power rationing that limits the supply of electricity to households and small businesses to night-time hours only.

Traditionally, Tanzania has relied on hydroelectric power for the bulk of the country's electricity supply. However, persistently dry weather conditions over the past three years together with the diversion of water for irrigation purposes resulted in steadily declining water levels in the main dams. This, coupled with the growing demand, have led to increased dependence on thermal power generation: first, by bringing on-stream the IPTL power plant using relatively expensive heavy fuel oil and, recently, through installing gas-fired generation capacity at the Ubungo plant utilizing the native gas from the Songas field. Consequently, the share of thermal power in TANESCO's generation mix has increased from 20 percent in 2003 to 60 percent in 2005.

The increased reliance on the high-cost thermal power generation together with rising fuel prices have resulted in escalating energy production costs. At the same time, tariffs have not been adjusted to fully reflect the increased costs, while network losses have increased due to system overloading and the lack of funds for critical maintenance. As a result, the financial performance of TANESCO has deteriorated significantly over the past year despite important improvements in operational efficiency following the government's implementation of energy sector reforms financed by the World Bank. TANESCO has been making a net cash loss for every unit of electricity sold and has been unable to recover even operational costs from end-user tariffs. To cover the immediate financing needs of TANESCO, the government has authorized a bank overdraft facility (0.3 percent of GDP) and, in addition to already budgeted monthly transfers for IPTL capacity charges (0.1 percent of GDP), provided financing for emergency equipment procurement and for payments to IPTL and Songas for power purchases (0.1 percent of GDP).

The failure of short rains in late 2005 greatly aggravated TANESCO's financial situation and resulted in water levels in the Mtera and Kidatu hydro systems falling below the minimum operational levels. This led to the loss of some 50 percent of hydro-generation capacity and precipitated the energy crisis.

The government is actively considering urgent measures to address the crisis through installation of additional gas-fired generation capacity to compensate for the collapse of the hydro systems and to be in a position to meet the growing demand in support of the medium-term economic growth objectives. In this regard, the government's efforts (MEFP, paras. 31-33) include developing in consultation with the World Bank a time bound, monitorable financial recovery plan for TANESCO as well as a medium-term plan to enhance generation capacity (structural benchmark). This would trigger further financial support from the Bank. In addition, the authorities are establishing an interministerial steering committee responsible for monitoring implementation of these plans.

Box 2: MKUKUTA

The government's new 5-year PRSP, MKUKUTA, was adopted in June 2005. It builds on Tanzania's experience with its first PRSP, but evolved from a priority sector spending approach to an outcomes based approach. The outcomes based approach emphasizes the contribution of all sectors toward progressing on three identified clusters in MKUKUTA: (i) growth and poverty reduction, (ii) improved quality of life and social well-being, and (iii) good governance and accountability.

The staff views MKUKUTA to be a comprehensive and integrated framework for growth and poverty reduction.[1] Major strengths of MKUKUTA are its multisector and results based approach, which has increased emphasis on growth, and that MKUKUTA implementation has been integrated with national systems for aligning donor assistance, monitoring, and budgeting. For instance, strategic linkage with the budget is ensured through the SBAS.

Achieving MDG targets is embedded in the MKUKUTA strategy. Cluster outcomes in the MKUKUTA are translated into goals and operational MKUKUTA targets that are made consistent with achieving MDG targets, often at a more ambitious pace. In recent years, Tanzania has made considerable progress and is likely to meet MDG targets on income poverty, education, gender equality, child mortality, hunger, and HIV/AIDS.

Nevertheless, there are challenges. There is a need to effectively translate growth and MDG targets into coordinated sector plans which are appropriately costed and prioritized, especially in the light of much needed key infrastructure spending. Spending on achieving MKUKUTA and MDG targets needs to be better linked to final outcomes through improved monitoring. Costing of achieving MKUKUTA objectives would also allow better integration with longer-term spending plans and mobilization of donor financing. Finally, capacity and accountability at the local government level would need to be enhanced to improve effective social service delivery.

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[1] See the Joint Staff Advisory Note being issued with this report.

Box 3: Multilateral Debt Relief Initiative (MDRI)

On January 5, 2006, the Fund delivered MDRI debt relief to Tanzania estimated at some US$336 million (or roughly 2.7 percent of GDP). Tanzania anticipates further MDRI relief from the IDA and AfDF, once the modalities are established. The MDRI is intended to free up resources to help recipients reach the MDGs.

The Tanzanian government has decided to place the IMF MDRI funds in a special account at the BoT to be used by government solely to fund the foreign exchange component of high priority pro-poor social outlays and growth-critical economic projects. It is envisaged that Tanzania will make use of the special MDRI account over a period of about 3 years. All such outlays will be subject to regular budgetary rules and procedures, with administrative regulations to be put in place to ensure full transparency and monitorability, and will be explicitly included in the government budget beginning 2006/07 (MEFP, para. 20).

The government envisages that some US$50 million may be spent during the remainder of 2005/06 to redress the drought-related emergency situation, much of which has harmed the poor. These funds will be used to help pay for food imports to provide free or heavily subsidized food to some 3.7 million food insecure citizens. It will also be used for the purchase or lease of new power generation capacity, thus alleviating power rationing, which has affected mostly households and small businesses, and has shifted the government's energy policy focus away from rural electrification towards crisis management.

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

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

Source: Fund staff.

Table 2. Tanzania: Selected Economic and Financial Indicators, 2003/04-2005/06

	2003/04	2004/05	2005/06	
			Prog.	Proj.
	(Annual percentage change, unless otherwise indicated)			
National income and prices 1/				
Nominal GDP (market prices; billions of Tanzania shillings)	10,686	12,321	13,673	13,713
Real GDP growth (factor cost)	5.7	6.7	6.9	6.9
Consumer prices (period average)	4.4	4.1	4.0	4.4
Consumer prices (end of period)	4.6	4.1	4.0	5.0
External sector				
Export, f.o.b (in U.S. dollars)	1,299	1,607	1,709	1,767
Imports, c.i.f. (in U.S. dollars)	-2,370	-2,867	-3,459	3,594
Export volume	21.3	11.0	10.6	3.6
Import volume	9.5	6.4	20.5	22.0
Terms of trade	-10.8	-2.0	4.6	3.4
Nominal effective exchange rate (end of period; depreciation -)	-10.6	-2.5	…	...
Real effective exchange rate (end of period; depreciation -)	-8.7	-0.6	…	...
Public finance				
Revenue (excluding grants)	19.9	21.5	16.5	16.5
Total expenditure	27.1	28.5	19.3	27.2
Recurrent expenditure	26.7	22.0	14.7	28.1
Development expenditure	28.3	47.6	31.9	25.0
Money and credit				
Broad money (M3)	18.0	25.5	27.0	30.0
Net foreign assets	16.8	8.4	12.1	24.2
Net domestic assets	24.3	108.3	66.4	44.8
Credit to nongovernment sector	46.7	26.2	33.2	35.3
Velocity of money (GDP/M3; average)	4.7	4.4	3.9	3.9
Treasury bill interest rate (in percent; end of period) 2/	7.7	10.4	…	…
	(In percent of GDP)			
Public finance				
Revenue (excluding grants)	12.7	13.6	14.3	14.2
Total grants	6.1	7.8	7.5	10.2
Expenditure (including adjustment to cash)	22.0	25.7	26.8	28.4
Overall balance (including grants)	-3.2	-4.2	-5.1	-4.0
Domestic financing 3/	-0.4	1.1	1.1	2.6
Of which : nonbank financing	…	0.6	0.0	1.2
Savings and investment 1/				
Resource gap	-9.0	-6.7	-11.4	-8.7
Investment	18.6	18.4	18.9	18.8
Government	7.4	7.3	7.5	7.5
Nongovernment 4/	11.2	11.1	11.4	11.4
Gross domestic savings	9.7	11.7	7.5	10.2
External sector				
Current account balance (excluding current transfers)	-6.9	-8.6	-12.4	-13.2
Current account balance (including current transfers)	-1.7	-2.6	-7.0	-7.9
	(In millions of U.S. dollars, unless otherwise indicated)			
Balance of payments				
Current account balance (excluding current transfers; deficit -)	-738	-1,028	-1,661	-1,652
Overall balance of payments (deficit -)	162	263	173	334
Gross official reserves	1,878	2,109	2,247	2,086
In months of imports of goods and nonfactor services	6.0	5.5	5.7	4.9
Exchange rate (eop, T Shillings per U.S. dollar)	1,115	1,126	…	...
Exchange rate (period average, T Shilling per U.S. dollar)	1,077	1,090	…	...

Sources: Tanzanian authorities and Fund staff estimates and projections.

1/ Data are on calendar year basis. 2003/04 data are for calendar year 2003.
2/ Weighted-average yield of 35, 91-, 182-, and 364-day treasury bills.
3/ Excluding new debt issued to recapitalize government-owned banks.
4/ Including change in stock.

Table 3. Tanzania: Central Government Operations, 2003/04-2005/06 1/
(In billions of shillings)

	2003/04	2004/05		2005/06	
		Prog.	Actual	Prog.	Proj.
Total revenue	1,459	1,739	1,774	2,067	2,067
Tax revenue	1,343	1,599	1,615	1,869	1,881
Import duties	137	142	112	148	148
Value-added tax	504	615	680	776	794
Excises	215	243	239	268	265
Income taxes	364	458	453	531	530
Other taxes	123	141	132	146	144
Nontax revenue	117	140	158	198	186
Total expenditure	2,528	3,211	3,248	3,882	4,131
Recurrent expenditure	1,886	2,379	2,300	2,724	2,945
Wages and salaries	463	551	551	682	692
Interest payments	109	170	143	171	260
Domestic	70	95	87	101	184
Foreign	38	76	56	70	76
Goods and services and transfers	1,314	1,657	1,606	1,871	1,993
of which: Food imports (MDRI)	…	…	…	…	35
Development expenditure	642	832	949	1,158	1,186
Domestically financed	133	234	240	370	370
Foreign financed	509	598	709	788	793
Gas-fired generating capacity (MDRI)	…	…	…	…	23
Overall balance before grants	-1,069	-1,472	-1,475	-1,815	-2,064
Grants	697	963	1,021	1,080	1,482
Program (including basket grants) 2/	371	561	548	549	508
Project	248	312	400	461	510
HIPC grant relief	77	90	72	70	73
MDRI grant relief	…	…	…	…	391
Overall balance after grants	-372	-508	-454	-735	-582
Adjustment to cash 3/	-28	-31	-87	0	0
Overall Balance	-400	-539	-541	-735	-582
Financing	400	539	541	735	582
Foreign (net)	434	388	396	561	512
Foreign loans	479	523	503	683	644
Program (including basket loans) 2/	218	236	194	356	361
Project	261	286	309	327	282
Amortization	-45	-135	-107	-122	-131
Domestic (net)	-44	157	145	164	371
Bank financing	…	97	63	164	201
Nonbank financing	…	60	82	0	170
Amortization of parastatal debt	0	-16	0	0	-12
Privatization proceeds	10	10	0	10	43
MDRI Account	…	…	…	…	-333
Memorandum items:					
Treasury vouchers	21	31	16	31	31
Share of expenditures financed from foreign sources 4/	46	44	45	44	42
Share of current expenditures financed by foreign program assistance 5/	31	34	32	33	30
Public domestic debt 6/	14.5	14.1	15.5	12.7	15.5
Ratio of recurrent expenditures to total revenues (percent)	129	137	130	132	142
Nominal GDP	11,504	12,457	13,017	14,458	14,523

Table 3. (contd.) Tanzania: Central Government Operations, 2003/04-2005/06 1/

	2003/04	2004/05		2005/06	
		Prog.	Actual	Prog.	Proj.
Total revenue	12.7	14.0	13.6	14.3	14.2
Tax revenue	11.7	12.8	12.4	12.9	13.0
Import duties	1.2	1.1	0.9	1.0	1.0
Value-added tax	4.4	4.9	5.2	5.4	5.5
Excises	1.9	2.0	1.8	1.9	1.8
Income taxes	3.2	3.7	3.5	3.7	3.6
Other taxes	1.1	1.1	1.0	1.0	1.0
Nontax revenue	1.0	1.1	1.2	1.4	1.3
Total expenditure	22.0	25.8	25.0	26.8	28.4
Recurrent expenditure	16.4	19.1	17.7	18.8	20.3
Wages and salaries	4.0	4.4	4.2	4.7	4.8
Interest payments	0.9	1.4	1.1	1.2	1.8
Domestic	0.6	0.8	0.7	0.7	1.3
Foreign	0.3	0.6	0.4	0.5	0.5
Goods and services and transfers	11.4	13.3	12.3	12.9	13.7
Of which: Food imports (MDRI)	…	…	…	…	0.2
Development expenditure	5.6	6.7	7.3	8.0	8.2
Domestically financed	1.2	1.9	1.8	2.6	2.5
Foreign financed	4.4	4.8	5.4	5.5	5.5
Gas-fired generating capacity (MDRI)	…	…	…	…	0.2
Overall balance before grants	-9.3	-11.8	-11.3	-12.6	-14.2
Grants	6.1	7.7	7.8	7.5	10.2
Program (including basket grants) 2/	3.2	4.5	4.2	3.8	3.5
Project	2.2	2.5	3.1	3.2	3.5
HIPC grant relief	0.7	0.7	0.6	0.5	0.5
MDRI grant relief	…	…	…	…	2.7
Overall balance after grants	-3.2	-4.1	-3.5	-5.1	-4.0
Adjustment to cash 3/	-0.2	-0.2	-0.7	0.0	0.0
Overall Balance	-3.5	-4.3	-4.2	-5.1	-4.0
Financing	3.5	4.3	4.2	5.1	4.0
Foreign (net)	3.8	3.1	3.0	3.9	3.5
Foreign loans	4.2	4.2	3.9	4.7	4.4
Program (including basket loans) 2/	1.9	1.9	1.5	2.5	2.5
Project	2.3	2.3	2.4	2.3	1.9
Amortization	-0.4	-1.1	-0.8	-0.8	-0.9
Domestic (net)	-0.4	1.3	1.1	1.1	2.6
Bank financing	…	0.8	0.5	1.1	1.4
Nonbank financing	…	0.5	0.6	0.0	1.2
Amortization of parastatal debt	0.0	-0.1	0.0	0.0	-0.1
Privatization proceeds	0.1	0.1	0.0	0.1	0.3
MDRI Account	…	…	…	…	-2.3

Sources: Ministry of Finance and Fund staff projections.

1/ Fiscal year: July-June.

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

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

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

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

6/ Including contingent liabilities, largely consisting of nonguaranteed parastatal debt and liquidity paper of BoT for managing liquidity.

Table 4. Tanzania: Summary Accounts of the Bank of Tanzania, June 2005 - June 2006
(In billions of shillings, unless otherwise indicated; end of period)

	2005 1/					2006 1/			
	June	Sept		Dec		March		June	
	Actual	Prog.	Actual	Prog.	Actual	Prog.	Proj.	Prog.	Proj.
Net foreign assets	1,726	2,027	1,797	2,198	2,072	2,056	2,300 2/	1,943	2,154 2/
Net international reserves	1,765	2,066	1,835	2,237	2,107	2,095	2,335 2/	1,982	2,190 2/
(in millions of U.S. dollars)	1,567	1,913	1,615	2,071	1,808	1,940	1,979 2/	1,835	1,856 2/
Medium- and long-term foreign liabilities	-39	-39	-38	-39	-35	-39	-35	-39	-35
Net domestic assets	-696	-894 4/	-669	-963 4/	-836	-806 4/	-971	-641 4/	-806
Credit to government	-690	-290	-730	-415	-1,118	-300	-871	-120	-795
Other items (net)	-6	36	61	65	282	98	-100	112	-11
o/w IMF MDRI	---	---	---	---	---	---	396	---	337
Reserve money	1,030	1,133	1,128	1,235	1,236	1,250	1,328	1,302	1,348
Currency outside banks	735	785	791	857	843	854	910	905	932
Bank reserves	295	348	337	378	393	396	418	397	416
Currency in banks	80	63	85	65	90	65	95	65	95
Deposits	215	285	252	313	303	331	323	332	321
Required reserves (calculated) 3/	213	247	232	265	264	276	280	288	284
Excess reserves (calculated)	2	38	20	48	39	55	44	43	37

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

1/ The changes between program and revised projections and actual outturns (including other items net--"OIN") include IMF MDRI and a revised accounting presentation that treats liquidity paper as T-bills. OIN is also higher due to outlays by the BoT, including construction of new BoT headquarters and allocations for new bank notes.

2/ Includes IMF MDRI. The use of IMF MDRI increases other items net and reduces NFA (to pay for the foreign exchange component of government expenditures), consistent with para. 20 of the MEFP.

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

4/ Includes liquidity paper.

Table 5. Tanzania: Monetary Survey, June 2005 - June 2006
(In billions of shillings, unless otherwise indicated; end of period)

	2005 1/					**2006** 1/			
	June	Sept		Dec		Mar		June	
	Actual	Prog.	Actual	Prog.	Actual	Prog.	Proj.	Prog.	Proj.
Net foreign assets	2,340	2,647	2,480	2,814	2,853	2,725	3,061 2/	2,636	2,905 2/
Net domestic assets	927	924	1,056	1,021	1,082	1,212	1,123	1,479	1,342
Domestic credit	1,206	1,398	1,324	1,459	1,200	1,666	1,688	1,959	1,838
Credit to government (net)	-13	21	-66	-22	-226	80	121	286	188
Credit to nongovernment sector	1,219	1,377	1,390	1,481	1,425	1,586	1,567	1,672	1,650
Other items (net)	-279	-475	-268	-438	-117	-454	-565 2/	-480	-496 2/
M3	3,266	3,570	3,536	3,835	3,935	3,937	4,184	4,115	4,246
Foreign currency deposits	900	1,037	996	1,058	1,127	1,112	1,204	1,118	1,215
M2	2,367	2,534	2,540	2,777	2,808	2,825	2,980	2,997	3,031
Currency in circulation	735	785	791	857	843	854	910	905	932
Deposits (in Tanzania shillings)	1,632	1,748	1,749	1,920	1,965	1,970	2,071	2,092	2,099
Memorandum items:									
M3 growth (12-month percent change)	25.5	27.7	26.5	34.6	38.2	26.0	33.9	27.0	30.0
Foreign currency deposits (12-month percent change)	20.5	27.0	22.1	32.8	41.3	21.9	31.9	27.0	35.0
M2 growth (12-month percent change)	27.5	28.0	28.3	35.4	37.0	27.7	34.7	27.1	28.1
Credit to nongovernment sector (12-month percent change)	26.2	34.1	35.3	39.7	34.4	38.3	36.6	33.2	35.3
Reserve money (12-month percent change)	28.7	31.2	30.6	27.6	27.7	27.9	35.9	26.6	30.9
Currency/M3 (in percent)	22.5	22.0	22.4	22.3	21.4	21.7	21.7	22.0	22.0
Reserve money multiplier (M3/reserves)	3.2	3.1	3.1	3.1	3.2	3.1	3.1	3.2	3.2
Velocity of money (M3; average)	4.4	...	...	4.1	4.0	...	...	3.9	3.9
Velocity of money (M3; end-period)	4.0	...	...	3.6	3.5	...	...	3.5	3.4
Nonbank financing of the government 3/	82	0	163	0	185	0	175	0	170

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

1/ The changes between program and revised projections and actual outturns (including other items net--OIN-- and nonbank financing) include IMF MDRI, and a revised accounting presentation that treats liquidity paper as T-bills.

2/ Includes IMF MDRI. The use of IMF MDRI increases other items net and reduces NFA (to pay for the foreign exchange component of government expenditures), consistent with para. 20 of the MEFP.

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

Table 6: Financial Soundness Indicators, 2002-05
(In percent, end of year)

	2002	2003	2004	2005
Access to bank lending				
Claims on the private sector to GDP	6.0	7.7	8.6	10.4
Capital adequacy				
Capital to risk-weighted assets	20.6	21.0	21.2	22.0
Capital to assets	8.6	9.9	10.2	10.0
Asset composition and quality				
Total loans and advances to total assets	25.4	30.2	33.7	33.7
Sectoral distribution of loans to total loans				
Trade	22.1	23.8	22.4	23.5
Mining and manufacturing	24.4	27.3	22.2	22.0
Agricultural production	12.9	14.1	12.8	12.7
Building and construction	3.6	5.5	3.8	5.7
Transport	11.8	10.3	8.3	7.4
Foreign exchange loans to total loans	28.1	27.2	28.9	32.7
Gross nonperforming loans (NPLs) to gross loans	8.3	4.5	3.5	4.9
NPLs net of provisions to total capital	22.0	9.3	8.2	14.6
Large exposures to total capital	58.2	59.3	64.1	53.3
Earnings and profitability				
ROA	1.8	2.1	2.9	3.3
ROE	20.6	20.7	28.4	33.1
Interest margin to gross income	48.0	51.5	54.8	60.9
Noninterest expenses to gross income	70.1	67.1	61.6	56.9
Personnel expenses to noninterest expenses	41.3	39.9	39.0	39.6
Trading and fee income to total income	45.2	42.3	39.1	33.6
Interest rate earned on loans and advances	15.7	13.8	14.8	15.0
Interest rate paid on nonbank deposits	3.1	3.2	3.5	3.9
Spread (lending vs. deposit rates)	12.6	10.7	11.3	11.0
Liquidity				
Liquid assets to total assets	58.0	56.3	53.6	55.0
Liquid assets to total short term liabilities	68.9	62.8	62.0	62.4
Total loans to customer deposits	34.0	41.2	44.4	42.4
Foreign exchange liabilities to total liabilities	34.1	36.5	34.7	34.9

Sources: Bank of Tanzania and Fund staff estimates.

Table 7. Tanzania: Balance of Payments, 2003/04-2008/09

(In millions of U.S. dollars, unless otherwise indicated)

	2003/04	2004/05	2005/06		2006/07	2007/08	2008/09
			Prog.	Proj.	Proj.	Proj.	Proj.
Current account	-182.6	-315.5	-937.7	-985.8	-1,244.4	-1,248.4	-1,255.6
Trade balance	-859.9	-1,004.0	-1,438.6	-1,505.7	-1,743.3	-1,807.2	-1,869.8
Exports, f.o.b.	1,298.7	1,606.9	1,708.9	1,767.2	1,865.2	2,169.2	2,346.6
Traditional	220.4	327.3	409.5	338.2	352.9	384.7	419.3
Nontraditional	1,078.4	1,279.6	1,299.4	1,429.0	1,512.3	1,784.5	1,927.3
Imports, f.o.b	-2,158.6	-2,610.9	-3,147.5	-3,272.9	-3,608.5	-3,976.4	-4,216.3
Services (net)	196.1	66.4	-160.6	-66.5	-119.2	-143.3	-123.0
Income (net)	-74.7	-90.8	-62.0	-79.8	-57.3	-38.9	-22.0
Of which : interest payments due	-130.1	-134.7	-102.9	-122.1	-103.9	-89.4	-77.4
Of which : interest on public debt	-95.0	-99.4	-67.9	-91.5	-84.8	-74.3	-64.3
Of which : interest on central government debt	-59.9	-56.1	-64.8	-65.2	-70.2	-66.9	-60.0
Current transfers (net)	555.8	712.9	723.4	666.2	675.4	741.0	759.2
Of which : official transfers	550.6	711.2	713.0	664.4	673.6	739.1	756.3
Of which : program grants	338.0	509.4	507.9	464.3	480.1	518.3	514.3
HIPC relief	71.8	64.3	64.9	59.8	46.0	66.7	83.9
Capital account	348.6	409.8	543.5	820.9	498.9	550.4	571.4
Of which : project grants	310.0	368.3	496.0	437.7	450.0	500.0	520.0
IMF MDRI debt relief	…	…	…	335.7	0.0	0.0	0.0
Financial account	442.6	440.9	567.6	499.1	865.5	814.6	789.6
Direct investment	498.4	495.0	510.0	550.0	580.0	600.0	620.0
Other investment	-55.8	-54.1	57.6	-50.9	285.5	214.6	169.6
Of which : program loans	204.4	181.6	329.7	302.8	364.0	400.0	440.0
project loans	242.9	283.1	334.7	242.1	250.0	300.0	320.0
Government scheduled amortization	-108.0	-123.2	-119.2	-500.7	-95.0	-121.0	-124.0
Of which : central government	-97.1	-99.4	-113.2	-112.4	-95.0	-108.9	-111.6
Errors and omissions	-446.7	-271.9	0.0	0.0	0.0	0.0	0.0
Overall balance	161.9	263.4	173.4	334.2	120.0	116.6	105.4
Financing	-161.9	-263.4	-173.4	-334.2	-120.0	-116.6	-105.4
Change in BoT reserve assets (increase, -)	-207.1	-231.2	-110.2	22.5	-124.0	-116.6	-105.4
Use of Fund credit	-3.1	-32.2	-63.2	-356.7	4.0	0.0	0.0
Exceptional financing	48.3	0.0	0.0	0.0	0.0	0.0	0.0
Change in arrears (increase +) 1/	48.3	0.0	0.0	0.0	0.0	0.0	0.0
Debt rescheduled	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:							
Gross official reserves (BoT)	1,877.5	2,108.7	2,246.8	2,086.2	2,210.2	2,326.8	2,432.2
In months of imports of goods and services (next year)	6.0	5.5	5.7	4.9	4.8	4.7	4.7
Current account deficit (as percent of GDP)							
Excluding official current transfers	-6.9	-8.6	-12.4	-13.2	-13.9	-13.7	-13.1
Including official current transfers	-1.7	-2.6	-7.0	-7.9	-9.0	-8.6	-8.2
Aid dependency 2/	12.2	12.9	14.0	13.2	12.6	13.3	13.3
Foreign direct investment (as percentage of GDP)	4.7	4.1	3.8	4.4	4.2	4.1	4.0
Nominal GDP	10,694	11,937	13,387	12,475	13,773	14,530	15,329

Sources: Tanzanian authorities and Fund staff estimates and projections.

1/ Arrears are on non-Paris Club official and commercial debt subject to rescheduling.

2/ Program and project assistance as percent of GDP.

Table 8. Tanzania: Disbursements of Program Assistance, 2004/05 - 2005/06 1/

(In millions of U.S. dollars)

	2005/06								2004/05	2005/06	
	Prog.	Act.	Prog.	Act.	Prog.	Proj.	Prog.	Proj.	Act.	Prog.	Proj.
	Sep.	Sep.	Dec.	Dec.	Mar.	Mar.	Jun.	Jun.	FY	FY	FY
Grants	316.8	119.8	140.0	247.5	36.1	36.6	14.9	60.5	509.4	507.9	464.3
Multilateral	47.1	39.1	0.0	0.0	0.0	0.0	0.0	0.0	155.2	47.1	39.1
EU PRBS grants 2/	47.1	39.1	0.0	0.0	0.0	0.0	0.0	0.0	38.3	47.1	39.1
World Bank (PRBS)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	116.9	0.0	0.0
Bilateral	269.7	80.8	140.1	247.5	36.1	36.6	14.9	60.5	354.2	460.9	425.2
PRBS 2/	215.0	48.8	57.9	191.3	6.7	4.2	0.0	26.9	208.8	279.5	271.3
Canada	0.0	0.0	21.6	0.0	0.0	0.0	0.0	21.6	0.0	21.6	21.6
Denmark	9.0	8.2	1.8	1.6	0.0	0.0	0.0	0.0	13.4	10.8	9.8
Finland	5.4	4.9	0.0	0.0	0.0	0.0	0.0	0.0	3.9	5.4	4.9
Germany	0.0	0.0	0.0	0.0	6.7	0.0	0.0	5.3	6.2	6.7	5.3
Ireland	13.5	13.5	0.0	0.0	0.0	0.0	0.0	0.0	6.5	13.5	13.5
Japan	5.2	5.0	0.0	0.0	0.0	0.0	0.0	0.0	4.5	5.2	5.0
Netherlands	0.0	0.0	13.5	12.0	0.0	0.0	0.0	0.0	18.1	13.5	12.0
Norway	13.2	12.5	3.3	3.0	0.0	0.0	0.0	0.0	14.6	16.5	15.4
Sweden	0.0	0.0	17.8	25.8	0.0	0.0	0.0	0.0	15.8	17.8	25.8
Switzerland	5.2	4.8	0.0	0.0	0.0	0.0	0.0	0.0	5.0	5.2	4.8
United Kingdom	163.5	0.0	0.0	148.9	0.0	4.2	0.0	0.0	120.7	163.5	153.2
Sectoral baskets	54.8	31.9	82.2	56.1	29.4	32.4	14.9	33.6	145.4	181.3	154.0
Belgium	0.0	0.0	5.4	0.0	0.0	5.4	0.0	0.0	5.4	5.4	5.4
Canada	2.5	0.0	4.1	0.0	0.0	0.0	11.6	18.2	18.0	18.2	18.2
Denmark	16.9	3.4	0.0	13.4	1.2	0.0	0.0	0.0	17.2	18.1	16.8
EU	0.0	0.0	8.7	0.5	4.1	1.7	0.0	0.0	18.5	12.8	2.2
France	0.0	0.6	1.2	0.0	0.0	0.2	0.0	0.4	3.8	1.2	1.2
Finland	2.6	5.5	0.0	0.0	2.6	0.0	0.0	4.0	0.6	5.2	9.5
Germany	4.2	3.1	1.7	0.0	1.5	1.5	1.5	1.5	0.0	8.9	6.1
Ireland	10.1	3.6	0.1	5.4	0.0	0.0	0.0	0.0	7.0	10.2	9.0
Italy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.8	0.0	0.0
Japan	0.0	0.0	0.5	0.0	0.0	0.5	0.0	0.0	0.0	0.5	0.5
Netherlands	0.9	1.1	28.2	15.5	0.0	12.5	0.0	0.0	32.6	29.1	29.1
Norway	2.3	0.0	9.9	1.6	4.7	0.0	0.0	0.0	4.6	16.9	1.6
Sweden	0.0	0.0	21.5	14.5	0.0	0.0	0.0	7.0	16.3	21.5	21.5
Switzerland	0.1	0.0	0.6	4.6	0.0	0.0	0.0	0.7	4.7	0.7	5.3
United Kingdom	10.9	14.7	0.3	0.0	15.3	10.6	1.8	1.8	18.9	28.3	27.1
Others	0.0	0.0	0.0	0.6	0.0	0.0	0.0	0.0	-3.0	0.0	0.6
Loans	125.6	82.7	175.0	151.3	29.1	50.0	0.0	18.8	181.6	329.7	302.8
Multilateral	15.6	82.7	175.0	151.3	29.1	50.0	0.0	18.8	181.6	219.7	302.8
World Bank	50.0	9.0	175.0	151.3	29.1	50.0	0.0	18.8	181.6	254.1	229.1
PRBS loans	0.0	0.0	175.0	151.3	0.0	0.0	0.0	18.8	60.1	175.0	170.1
Baskets Loan	50.0	9.0	0.0	0.0	29.1	50.0	0.0	0.0	121.5	79.1	59.0
African Development Bank	75.6	73.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	75.6	73.7
Bilateral	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total program assistance	442.4	202.5	315.1	398.8	65.2	86.6	14.9	79.3	691.0	837.7	767.0
Cumulative from beginning of fiscal year	442.4	202.5	757.6	601.2	822.8	687.8	837.7	767.0	...	...	...

Sources: Tanzanian authorities and donors.

1/ Fiscal years run from July to June.

2/ Poverty reduction budget support.

Table 9. Tanzania: Status of HIPC Initiative Agreements by Creditor

	Debt Relief in Nominal Terms (US$ mil.)	Agreement to Provide Relief Beyond HIPC?	Comments
Multilateral Creditors			
IMF	120	n/a	Provided grants through PRGF-HIPC Trust fund.
AfDB/AfDF	190.7	n/a	Debt service reduction by 80% annually until debt relief delivered.
IDA/IBRD	1,157.10	n/a	Debt-service relief of 69.1 and 63.6 percent on debts outstanding at end-June 1999 and 2001, respectively.
IFAD	24.5	n/a	Reduction of 100% of debt -service due.
BADEA	14.7	n/a	Concessional rescheduling of the debt and reduced interest rate.
OPEC	9.8	n/a	Concessionnal loans and restructuring of existing debt.
NDF	3.2	n/a	Contribution to HIPC initative trust fund , to pay 100% debt service.
EADB	0.6	n/a	Reduced interest rate and extension of repayment period.
EU	37.9	n/a	Provided grants at the complition point to pay off outstanding loans.
Paris Club Creditors			
Austria	31.3	Yes	Bilateral Agreement for PC VII was signed on May 7, 2002.
Belgium	74.3	No	Bilateral Agreement for PC VII was signed on November 29, 2002.
Brazil	-	No	Reminder letter to submit draft agreement for PC VII sent May 19, 2004. Awaiting reply.
Canada	31.1	Yes	Bilateral Agreement for PC VII was signed on October 16, 2002.
France	89.9	Yes	Bilateral Agreement for PC VII was signed on March 6, 2003.
Germany	60.6	Yes	Bilateral Agreement for PC VII was signed on April 29, 2003.
Italy	132.0	Yes	Bilateral Agreement for PC VII was signed on May 7, 2002.
Japan	108.9	n.a.	Bilateral Agreement signed on March 2, 2004; cancelled 100% of ODA loans. Not yet offered debt relief on commercial and part of bilateral (Japanese Food Agency) debts.
Norway	11.1	Yes	Bilateral Agreement for PC VII was signed on December 5, 2002.
Netherlands	99.1	Yes	Bilateral Agreement for PC VII was signed on March 17, 2002.
Russia	69.6	No	Bilateral Agreement for PC VII was signed on July 18, 2003.
United Kingdom	129.2	Yes	Bilateral Agreement for PC VII was signed on July, 2002.
United States	21.3	Yes	Bilateral Agreement for PC 7 was signed on July 4, 2002.
Non-Paris Club Bilateral Creditors			
Algeria	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Angola	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Bulgaria	15.1	No	Bilateral Agreement was signed on December 12, 2003.
China	37.7	n.a.	15 interest-free loans maturing 31 Dec 1999 cancelled.
Czech Republic	-	No	The debt has been assigned to Lazard.
Egypt	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Hungary	10.4	No	Granted debt relief.
India	19.7	No	Bilateral Agreement signed on September 14, 2004 has cancelled all intergovernmental loans.
Iran	-	No	In active negotiations.
Iraq	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Kuwait	31.8	n.a.	Signed bilateral agreement on March 8, 2003. Rescheduled 9 pre-CD loans.
Libya	101.0	No	Granted debt relief.
Romania	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
United Arab Emirates	-	No	In active negotiations.
Yugoslavia	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.
Zambia	-	No	Request letter for debt relief under PC VII terms sent April 17, 2002. Awaiting reply.

Source: Bank of Tanzania

Table 10. Tanzania: External Debt Indicators, 2001/02–2011/12 1/
After bilateral relief beyond the enhanced HIPC Initiative

	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12
Debt Indicators at the HIPC Completion Point 2/											
NPV of debt-to-GDP ratio	14.2	14.7	14.8	14.8	14.9	15.1	15.1	15.1	15.0	14.9	14.9
NPV of debt-to-exports ratio 3/ 4/	105.2	112.1	115.6	117.0	117.3	117.5	116.8	116.2	115.2	114.3	114.4
NPV of debt-to-revenue ratio 5/	126.5	125.2	124.4	123.4	120.7	118.7	116.8	113.5	110.5	106.5	103.9
Debt-service-to-export ratio 6/	6.4	5.7	6.2	6.9	6.4	5.7	5.6	5.3	5.6	5.6	4.9
Debt service-to-revenue ratio 5/	8.0	6.6	7.1	7.9	7.1	6.3	6.0	5.6	5.8	5.6	4.8
Updated Debt Indicators 7/											
NPV of debt-to-GDP ratio	20.7	20.7	20.9	19.9	20.0	19.0	19.7	19.3	19.3	19.2	18.7
NPV of debt-to-exports ratio 3/ 4/	137.6	135.1	124.5	105.2	91.7	86.5	87.1	82.7	79.5	77.3	73.4
NPV of debt-to-revenue ratio 5/	171.2	171.5	162.5	147.1	145.5	135.2	141.0	137.8	126.8	126.3	123.0
Debt-service-to-export ratio 6/	6.0	4.8	4.2	3.1	3.4	3.4	3.1	2.8	3.0	2.8	2.3
Debt service-to-revenue ratio 5/	8.0	6.8	7.1	5.4	6.0	5.7	5.5	5.1	5.2	4.9	4.2
					(In millions of U.S. dollars)						
Memorandum items:											
NPV of debt after bilateral debt relief beyond Enhanced HIPC Initiative assistance	1,941	2,090	2,235	2,377	2,500	2,616	2,869	2,957	3,117	3,276	3,366
Debt service after bilateral relief beyond Enhanced HIPC Initiative assistance	90	83	97	88	104	110	112	110	128	127	114
GDP	9,378	10,077	10,694	11,937	12,475	13,773	14,530	15,329	16,172	17,062	18,000
Exports of goods and services	1,495	1,716	2,310	2,811	3,058	3,205	3,617	3,910	4,231	4,579	4,955
Exports of goods and services (3-year mvg. avg.)	1,411	1,547	1,794	2,259	2,726	3,025	3,293	3,577	3,919	4,240	4,588
Government revenue	1,134	1,219	1,375	1,616	1,719	1,934	2,034	2,146	2,458	2,593	2,736

Sources: Tanzanian authorities; and IMF staff estimates.

1/ All debt indicators refer to public and publicly guaranteed debt and are defined after rescheduling, unless otherwise indicated. All years on July-June basis.
2/ Estimated in November 2001 based on end-June 2001 debt data.
3/ Based on a three-year average of exports (e.g., export average over 2001/02-2003/04 for NPV of debt-to-exports ratio in 2003/04).
4/ Assuming full delivery of HIPC Initiative assistance at end-June 2001.
5/ Revenue is defined as central government revenue, excluding grants.
6/ Based on current year exports.
7/ Estimated in February 2006 based on completion point debt data, new disbursements, and other macroeconomic developments and full delivery of Enhanced HIPC Initiative assistance. It also incorporates the IMF debt cancellation under the MDRI.

Table 11. Tanzania: Millennium Development Goals, 1990-2003

	1990	1995	2001	2002	2003
1. Eradicate extreme poverty and hunger	2015 target = halve 1990 $1 a day poverty and malnutrition rates				
Population below $1 a day (percent)	..	..	..	..	..
Poverty gap at $1 a day (percent)	..	..	..	..	..
Percentage share of income or consumption held by poorest 20 percent	..	..	..	..	..
Prevalence of child malnutrition (percent of children under 5)	..	..	..	..	..
Population below minimum level of dietary energy consumption (percent)	..	..	..	44.0	..
2. Achieve universal primary education	2015 target = net enrollment to 100				
Net primary enrollment ratio (percent of relevant age group)	49.6	..	54.4	68.8	..
Percentage of cohort reaching grade 5 (percent)	78.8	..	99.0	82.0	..
Youth literacy rate (percent ages 15-24)	..	..	..	78.4	..
3. Promote gender equality	2015 target = education ratio to 100				
Ratio of girls to boys in primary and secondary education (percent)	95.5	..	..	..	..
Ratio of young literate females to males (percent ages 15-24)		..	..	94.2	..
Share of women employed in the nonagricultural sector (percent)	28.5	..	..	..	..
4. Reduce child mortality	2015 target = reduce 1990 under 5 mortality by two-thirds				
Under 5 mortality rate (per 1,000)	163.0	164.0	..	..	165.0
Infant mortality rate (per 1,000 live births)	102.0	103.0	..	..	104.0
Immunization, measles (percent of children under 12 months)	80.0	78.0	83.0	89.0	97.0
5. Improve maternal health	2015 target = reduce 1990 maternal mortality by three-fourths				
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	..	..
Births attended by skilled health staff (percent of total)	..	..	..	..	..
6. Combat HIV/AIDS, malaria, and other diseases	2015 target = halt, and begin to reverse, AIDS and other major diseases				
Prevalence of HIV, female (percent ages 15-24)	..	..	8.1	..	..
Contraceptive prevalence rate (percent of women ages 15-49)	..	..	..	..	..
Number of children orphaned by HIV/AIDS (thousands)	..	..	790.0	..	980.0
Incidence of tuberculosis (per 100,000 people)	183.5	277.2	356.5	363.8	371.2
Tuberculosis cases detected under Direction of Trade Statistics (percent)	..	55.0	45.9	43.1	42.8
7. Ensure environmental sustainability	2015 target = various				
Forest area (percent of total land area)	45.0	..	..	..	..
Nationally protected areas (percent of total land area)	..	..	..	..	29.8
GDP per unit of energy use (PPP dollars per kg oil equivalent)	1.1	1.2	1.4	1.4	..
CO2 emissions (metric tons per capita)	0.1	0.1	..	..	..
Access to an improved water source (percent of population)	38.0	..	..	73.0	..
Access to improved sanitation (percent of population)	47.0	..	..	46.0	..
Access to secure tenure (percent of population)	..	..	..	..	..
8. Develop a Global Partnership for Development	2015 target = various				
Youth unemployment rate (percent of total labor force ages 15-24)	..	..	..	..	..
Fixed-line and mobile telephones (per 1,000 people)	3.1	3.3	17.1	24.1	29.5
Personal computers (per 1,000 people)	..	..	3.6	4.2	5.7
General indicators					
Population (millions)	25.5	29.6	34.4	35.2	35.9
Gross national income (billions of U.S. dollars)	4.8	4.9	9.4	9.9	10.7
GNI per capita (U.S. dollars)	200.0	180.0	290.0	300.0	310.0
Adult literacy rate (percent of people ages 15 and over)	..	..	..	69.4	..
Total fertility rate (births per woman)	6.3	..	..	5.0	5.0
Life expectancy at birth (years)	50.1	..	..	43.1	42.7
Aid (percent of GNI)	28.8	17.1	13.6	12.7	16.3
External debt (percent of GNI)	158.5	144.6	72.3	75.5	73.4
Investment (% of GDP)	26.1	19.8	17.0	19.1	18.6
Trade (percent of GDP)	50.1	59.3	41.0	41.6	45.6

Source: http://www.developmentgoals.org.

March 24, 2006

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

Dear Mr. de Rato:

1. The Government of the United Republic of Tanzania has been implementing a financial and economic programme with support from the Fund's Poverty Reduction and Growth Facility (PRGF), under a three-year low access arrangement. Following the discussions we recently had with the Fund staff covering the fifth review of the PRGF programme, I hereby transmit the attached Memorandum of Economic and Financial Policies (MEFP), which reviews recent economic developments and progress in the implementation of the programme in the first half of 2005/06, and sets out policies the Government intends to pursue during the remainder of the fiscal year and beyond.

2. Progress under the 2005/06 programme has been satisfactory. All quantitative performance criteria and most indicative targets for the first two quarters were observed, except for the end-December indicative target for reserve money, which was missed by a tiny margin, and the end-September and end-December indicative targets on net domestic assets of the Bank of Tanzania because of difficulties in managing liquidity pressures in the banking system emanating from unanticipated outlays by the Government and the Bank of Tanzania.

3. Implementation of structural performance criteria and benchmarks during the period under review was broadly on track. However, approval by cabinet of the Anti-Corruption bill, an end-April 2006 structural benchmark, has been delayed by the prolonged period of the change of government. This has also delayed establishment of the planned DFGF.

4. The Government reaffirms its commitment in implementation of MKUKUTA**,** which sets economic growth, social well being of Tanzanians, good governance and accountability as the pillars of the country's development agenda. The Government underscores the need for continuation of appropriate monetary and fiscal policies, combined with key structural reforms which are essential to achieving MKUKUTA goals.

5. The Government believes that the policies and measures described in the attached MEFP are adequate to achieve the objectives of the 2005/06 programme. Throughout the programme, we will continue to provide the Fund with the required information to assess progress in implementing the programme. We shall also consult with the Fund on the adoption of any measures that may be appropriate at the initiative of Tanzania or the Fund.

We are therefore seeking completion of the fifth review under the PRGF arrangement and the consequent disbursement of the sixth tranche in an amount equivalent to SDR 2.8 million. The sixth and final review of the programme is contemplated for completion no later than early August 2006. Noting that the PRGF expires in August 2006, we would like to inform you of our intention to seek further support from the IMF in the context of the Policy Support Instrument.

6. The Government of Tanzania intends to make the contents of this letter and those of the attached MEFP available to the public and authorizes its publishing on the IMF website, together with Fund staff reports on the fifth review under the PRGF and MKUKUTA, once the Executive Board completes the review.

Yours Sincerely,

/s/

Zakia Hamdani Meghji (MP),
Minister for Finance,
United Republic of Tanzania.

Attachment: Memorandum of Economic and Financial Policies.

Memorandum of Economic and Financial Policies for 2005/06 and the Medium Term

I. Recent Economic Developments and Progress Under the Programme

Real Sector Performance

1. Tanzania's sustained economic reforms have generated strong macroeconomic performance characterized by strong GDP growth and low inflation. Preliminary estimates show that the economy performed well in the year 2005, with a GDP growth of around 7 percent in line with projections. The sectors that are estimated to have grown strongly during the year include, trade and tourism, manufacturing, mining and construction, which together contributed about 40 percent of GDP.

2. As noted below, the drought experienced during the last quarter of 2005 has adversely affected food production and hydropower generation. This, coupled with the persistent increase in oil prices throughout 2005, exerted upward pressure on inflation. After having successfully kept the inflation rate close to 4 percent, it began inching upward, from 4.2 percent in June 2005 to the annual inflation rate of 5.0 percent at end-December 2005.

Fiscal policy and public resource management

3. Fiscal revenues during the first half of FY 2005/06 were broadly in line with the targets, while expenditures were running ahead of programme targets. Strong revenue performance was sustained during the first half of FY 2005/06, mainly reflecting continued tax administration reforms. Higher-than-programmed expenditures were due to: additional costs associated with the postponement of the national elections, accelerated transfers to TANESCO to help mitigate the increased costs of power generation, procurement and distribution of food aid, and higher pension outlays. The lower outturn of external support to the budget culminated in increased domestic financing of the budget.

4. Tax and customs administration reforms continue to show remarkable progress. The VAT and Income Tax departments at TRA headquarters were merged into the Domestic Revenue Department (DRD) in July 2005 and technical staff were made to undergo 'total tax person' training. Other areas of progress with tax administration reform include: increased coverage of taxpayers by LTD; strengthened staffing of the LTD and the post clearance audit unit in the Customs Department; and issuance of practice notes for the implementation of the Income Tax Act of 2004. Beginning October 2005, customs procedures have been streamlined through, among others, building capacity for risk profiling of import consignments as a basis for post clearance audits. Significant progress was made in implementing the ASYCUDA++ system and there are indications that customs clearance times have been reduced at both the airport and Customs Service Centre (formerly Dar es

Salaam Customs Longroom) and the problem of electronically transferring data between TISCAN and ASYCUDA ++ has been resolved.

Monetary Policy

5. During the first half of 2005/06, the economy witnessed a considerable build up of excess liquidity mainly from an uneven pace of government payments and accelerated outlays by the Bank of Tanzania. The situation was exacerbated by the sizable shortfall (US$157 million) in donor funds inflows, which forced the Government to draw down its deposits in the banking system.

6. The excess liquidity in the economy was reflected by the persistent increase in reserve money above projections. In response, the Bank of Tanzania scaled up its sales of treasury bills, which were complemented by sales of foreign exchange, and repurchase agreement transactions with commercial banks. The tender size for treasury bills was steadily increased from T Sh 48.6 billion per week during July 2005 to T Sh 70 billion during December 2005. Together with robust credit demand from the private sector this led to upward pressure on interest rates. The weighted average yield for treasury bills moved from an average of 10.4 percent in July 2005 to 14.8 percent in December 2005. The weighted average time deposit rate rose from 4.4 percent to 5.3 percent, while the average lending rate and the average negotiated lending rate, were maintained at around 15 percent and 11 percent, respectively.

7. During the past six months, private sector credit grew at an average annual rate of 32.1 percent, which is in line with the envisaged momentum of economic activities. The major factors behind the strong growth include strong economic expansion, a noticeable increase in the number of credit worthy clients, and improvement in the business environment. The trade sector has been the largest borrower receiving about 22.9 percent of total private sector loans, followed by manufacturing (20.9 percent). Lending to agricultural production has been growing rapidly in recent years. Outstanding loans for agricultural production stood at T Sh 177 billion at end-December 2005, compared with T Sh 21 billion in December 2000.

8. We believe that the demand for credit will continue to expand in particular for small and medium sized enterprises, as well as exporters. The recently established credit guarantee schemes for exporters and SMEs should help enhance access to credit. Thus, we need to continue to steer fiscal and monetary policies in a way to accommodate continued strong private sector credit growth in an environment of financial stability.

External Sector performance

9. In the first half of 2005/06 the current account deficit widened substantially, owing to a rising trade deficit and a significant shortfall in programme assistance. A noticeable increase in export earnings and tourism receipts was offset by an expansion in merchandise imports.

10. Official and private inflows, together with HIPC debt relief resulted in an increase in gross official reserves to US$ 2.2 billion at end-December 2005, the equivalent of 5 ½ months of next year's imports. In the same period, the nominal exchange rate of the shilling to the U.S. dollar depreciated from an average of T Sh 1,117 in the last quarter of 2004/05 to T Sh 1,161 in the second quarter of 2005/06.

11. During the period under review, Tanzania expects to benefit substantially from debt relief under the Multilateral Debt Relief Initiative (MDRI). The IMF has already finalized its assistance under this initiative. In January 2006 the Fund granted Tanzania relief on debt to the IMF in the amount of US$336 million (including HIPC relief) and as noted in paragraph 20 below, we are considering how best to use these funds for the benefit of the Tanzanian people. The Government also continued negotiations with bilateral creditors for debt relief. Among the Paris Club member countries, relief is sought from the remaining creditors, namely Brazil and some Japanese agencies (EID/MITI and the Japanese Food Agency). Relief amounting to US$101 million was received from Libya, and Hungary granted debt relief amounting to US$10.4 million.

II. THE PROGRAMME FOR THE REMAINDER OF 2005/06

12. Looking forward, economic performance during 2006 is expected to be affected by the impact of drought on agriculture and the availability of hydroelectric power. While the extent of the impact is not yet fully known, our provisional estimates suggest that the real GDP growth rate for 2006 is likely to be in the order of 5.8 percent compared to 7.2 percent previously projected. These estimates assume normal rainfall during the long rains season and expeditious introduction of measures in the power sector to address the deficit of hydropower generation in order to limit the adverse effect of electricity supply shortfalls on industry and manufacturing.

13. The Government's programme of food distribution from its Strategic Grain Reserve together with commercial grain imports temporarily exempted from import duty are expected to dampen pressures on food prices. However, given persistently high world market prices of oil and fuel, energy related price pressures are likely to accelerate somewhat in the coming months as producers and businesses begin to fully pass on to consumers the higher fuel costs. With monetary policy remaining prudent, and geared towards not accommodating second round price adjustments, the annual rate of inflation in 2006 is expected to average about 6 percent compared to 4 percent previously projected.

14. We expect revenue to continue performing as projected during the second half of FY 2005/06, and that the programme target of T Sh 2,067 billion will be attained, reflecting on-going tax administration reforms and expectations of normal long rains. This assumes that the selective power rationing by TANESCO will remain limited and will not greatly harm revenue collections.

15. In light of the emergence of unexpected outlays associated mainly with the drought, total expenditure of about 28 percent of GDP (excluding use of IMF MDRI) would be needed for 2005/06 compared with 26.8 percent of GDP originally envisaged. Specifically, it is provisionally projected that an additional T Sh 42 billion (0.3 percent of GDP) is needed to purchase food from the Strategic Grain Reserve for free or heavily subsidized distribution to vulnerable families. In addition, the crisis that has emerged in the energy sector requires additional transfers from the budget for supporting system maintenance and current operations of TANESCO (as discussed below). We are provisionally envisaging about T Sh 28 billion (0.2 percent of GDP) of such support. Thus about T Sh 70 billion (0.5 percent of GDP) is envisaged for the impact of the drought.

16. Taking into account slightly lower net foreign financing and higher privatization proceeds and amortization requirements, net domestic financing is expected to reach a maximum of 2.6 percent of GDP compared with 1.1 percent in the original programme. Since some of these unexpected expenditures are expected to be one-off, a marked decline in NDF is envisaged for FY 2006/07.

17. Continued prudent macroeconomic management will be underpinned by tax administration reforms. In the area of customs administration reforms, the two structural benchmarks (integrating the destination inspection programme with customs procedures at all customs offices in the Dar es Salaam region and increasing to 32 the number of staff in the post-clearance section of customs) were met. To further strengthen the operations of customs, the following measures are envisaged: further strengthening of post-clearance audit and risk management and intelligence and rolling out of ASYCUDA++ to all major customs stations. Domestic tax administration reforms will continue, including: (i) increasing the coverage of the LTD; (ii) development of an action plan with a view to possible establishment of a single department with responsibility for all domestic taxes; and (iii) extending and strengthening the taxpayer segmentation approach for medium taxpayers.

18. Improving expenditure management will remain a priority for the remainder of the year and in the medium term. The Government will strengthen the transparency and accountability of expenditure management, consistent with the objectives of the MKUKUTA by rolling out the IFMS to eligible Local Government Authorities and continue with training of accounting staff and capacity building at the local government level. With support from AFRITAC, we are addressing the persistent end year float problem through a joint Ministry of Finance and Bank of Tanzania capacity building programme. The plan includes monitoring closely, and limiting, the amount of idle cash held by MDAs and LGAs outside of the Bank of Tanzania (BoT). Also, it is expected that MDAs will have a smooth pattern of spending and all payments that fall due beyond the financial year will be budgeted under the subsequent year. The effort to strengthen the National Audit Office will continue, with the Government providing sufficient funds for it to implement the key elements of its capacity building initiatives. The Government will continue to urge donors to channel aid through the budgetary system, and move to general budget support as a desired modality of channeling foreign assistance.

19. The external current account deficit is expected to widen significantly in FY 2005/06, owing mainly to a sharp increase in the value of oil imports and drought related imports. However, a notable improvement in non-traditional export performance, especially the pick up in mining and manufacturing sectors, and high level of donor assistance and debt relief from the Fund under the MDRI are expected to mostly cushion the adverse impact of these exogenous shocks. As a result, the external reserve position of the BoT will remain at comfortable levels. The BoT will continue to allow the exchange rate to be market determined and limit its interventions to liquidity management and smoothing out excessive fluctuations.

20. The expected increase in net foreign assets includes the impact of the MDRI relief from the Fund. The counterpart has been placed in a special account at the Bank of Tanzania and will be passed on to the Government solely to fund the foreign exchange component of high priority pro-poor social outlays and growth-critical economic projects. All such outlays will be subject to regular procurement and financial management laws and regulations. Administrative regulations will be introduced to ensure that disbursements are made from the account in a transparent manner that can be easily tracked. It is envisaged that the MDRI account will be utilized over a period of about 3 years. The whole process of using MDRI funds will be properly structured and closely monitored. At this stage, it is provisionally envisaged that about US$50 million could be used during 2005/06 to address the emergency situation caused by the drought, namely for a one-year lease of an emergency electricity generator and food imports. The rest of the payments from the MDRI account at the Bank of Tanzania will take place beginning in fiscal year 2006/07, and will be fully taken into account in our annual budgets and the IMF supported programme.

21. Monetary policy for the remainder of 2005/06 remains focused on containing any broadening of inflation from higher fuel and food prices, while facilitating sufficient credit to the private sector for emergency food imports and for productive activities, and maintaining adequate foreign reserves. To this end, we envisage M3 growth (12-month) of about 34 percent through end-March, slowing to 30 percent by end-June. This growth would be consistent with private sector credit growth (12-month) of about 37 percent by end-March and 35 percent by end-June. In line with these objectives, the BoT will target reserve money growth (12-month) of 35.9 percent by end-March, falling to 30.9 percent by end-June. Velocity is expected to continue to decline, consistent with the ongoing expansion of financial intermediation. The Government recognizes the potential risks to inflation from higher money growth, and we are committed to adjusting our policies as appropriate to meet our inflation and growth targets in a manner consistent with the programme supported by the PRGF.

22. The BoT recognizes that the path of liquidity has been uneven, and is studying means to improve liquidity management. It intends to shift to some form of average reserve money targeting, perhaps within a band, beginning July 2006. In support of these efforts, the BoT and the Finance Ministry are undertaking a joint capacity building programme to help smooth spending patterns, as noted in para. 18 above. Other measures to boost liquidity

forecasting, and to strengthen domestic markets to facilitate liquidity management, will also be implemented.

23. The Government is continuing its efforts to implement broad-based second-generation financial sector reforms aimed at increasing the financial sector's contribution to investment and growth of the economy, within the context of the Financial Sector Reform Implementation Action Plan. A top priority is strengthening the BoT's capacity, cementing in law its current operating practices, and enhancing accountability through submitting to parliament the BoT Act and the Banking and Financial Institutions Act by end-April, which will be a structural performance criterion of the programme. The BoT Act will include provisions for three deputy governors, determination of exchange rate policy by the BoT, and strong provisions for transparency and accountability.

24. The Government is undertaking other efforts to further improve the availability of medium-term credit to key sectors of the economy, and in this connection intends to launch the Development Finance Guarantee Facility (DFGF), and is continuing efforts to facilitate the creation of a privately owned and managed Long Term Financing Facility to channel longer-term funds from nonbanks, banks, and development partners to be on-lent to commercial banks. The Government intends to limit its involvement under these facilities and the Development Finance Institution (DFI) consistent with paragraphs 42-44 of the MEFP attached to the Government's letter of intent dated July 14, 2005 (continuous structural benchmark).

25. The end-March structural benchmark to ensure that the instruments establishing the DFGF and the DFI require an annual independent operational audit to verify that the funds are being used for the purposes intended and that proper governance procedures have been followed was met for the DFI but was delayed for the DFGF due to the transition to a new government. The Government will include this requirement in relevant DFGF instruments (structural benchmark).

26. The inter-agency committee on financial reform is proceeding with development of a proposed unified legal and regulatory framework for all pension funds, and investment guidelines. It is intended that this be submitted to Government by end-June 2006 (structural benchmark), with technical support from the World Bank. This effort is expected to facilitate the channeling of pension funds' resources into longer term lending through commercial banks.

III. MKUKUTA Medium-Term Objectives

27. In implementing economic and financial policies, the Government will continue the policy direction charted in the MKUKUTA, which aims at attaining broad-based economic growth of at least 6-8 percent annually over the medium term and the Millennium Development Goals (MDGs). The MKUKUTA's emphasis on shared economic growth translates into particular attention to stimulating private investment, developing

infrastructure, building human capacity and a competitive economy. The Government intends to continue to gear its economic policies to the three clusters of outcomes delineated in MKUKUTA, namely: growth and reduction of income poverty; improved quality of life and social well-being; and good governance and accountability.

28. A complete matrix of indicators that would allow measurement of progress towards goals in the three cluster areas is being prepared through broad based stakeholder consultations. In parallel, the Government, together with development partners, is working on (i) costing the MDGs, and (ii) putting together multi-year costed programmes for infrastructure and other priority areas. When completed, these building blocks should allow to fully operationalize the MKUKUTA and become part of a road map for scaling up of aid and measuring success.

29. We are well aware of the fact that strong performance of revenues over the medium term is critical to protecting key MKUKUTA-related expenditures and reducing Tanzania's aid dependence. Achieving the revenue projections of 14.4 percent of GDP for 2006/07 hinges on continued implementation of our tax administration reforms. In order to further enhance revenue performance during FY 2006/07, we are considering the proposals of the Tax Policy Review mission for inclusion in the FY 2006/07 budget. In addition, caution will be exercised in the implementation of Special Economic Zones legislation, particularly regarding possible revenue loss implications.

30. In light of the need for increased credit to the private sector, further financial sector development and the increasing costs of domestic financing, budgeted expenditure for 2006/07 would be consistent with envisaged available resources and minimal use of domestic financing. In this regard, total expenditures of about 26.5 percent of GDP are provisionally envisaged for 2006/07 assuming that net donor support is sustained at about 11.1 percent of GDP, with domestic revenue of about 14.4 percent of GDP. This envisaged envelope would permit continued increase in MKUKUTA-related expenditures in view of one-off expenditures (elections and drought-related emergency outlays) projected for 2005/06. The possible additional external assistance associated with the MDRI should permit reducing domestic financing to about 0.5 percent of GDP, consistent with the targets in MKUKUTA, compared with preliminary estimates of 1.0 percent of GDP.

31. As noted above, the deficit of hydropower generation resulted in electricity supply shortages and is adversely affecting economic activity. The Government is actively considering ways to address the crisis situation in the energy sector through installing additional gas-based generation capacity to compensate for the loss of hydro-based generation capacity and to meet the growing demand for power over the medium-term.

32. In addition, the Government will finalize by end-June a financial recovery plan for TANESCO (structural benchmark) to close its operational deficits and to provide room for undertaking critical expenditures for transmission and distribution network maintenance, upgrading and refurbishment. The plan will include tariff increases to reflect the increased cost of power generation as well as a number of efficiency enhancing measures to be

implemented by TANESCO, including improvements in revenue and arrears collection rates and reduction of system losses. Nonetheless, the Government recognizes that, given the high fixed cost of power generation and limited scope for increasing supply and revenue in the short run, public involvement in the form of budgetary support for TANESCO will be unavoidable over the course of the next two years. In this regard, the Ministry of Finance has established a monthly reporting and monitoring procedure to ensure TANESCO's adherence to the revenue-enhancing and cost-reducing targets agreed under its financial recovery plan.

33. The Government will also finalize and agree on a medium-term Power Sector Strategy by end-June 2006 (structural benchmark), which it expects to share with key stakeholders. To ensure hands-on strategic steering of the energy sector reform and investment agenda, the Government will establish an inter-ministerial inter-agency committee responsible for defining and monitoring implementation of a comprehensive power sector restructuring plan and monitoring TANESCO's financial performance.

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

	2005						2006			
	September			December			March		June	
	Performance Criteria	Adjusted	Actual	Indicative Targets	Adjusted	Actual	Indicative Targets	Performance Criteria	Indicative Targets	Revised Indicative Targets
Net domestic financing of the government of Tanzania										
(ceiling) 1/ 2/ 3/	-101	171	110	-144	37	-27	-42	309	164	371
Accumulation of budgetary arrears (ceiling; indicative target only)	0	0	0	0	0	0	0	0	0	0
Net domestic assets of the Bank of Tanzania										
(ceiling; indicative target only) 2/ 3/	-894	-622	-578	-963	-782	-682	-806	-735	-641	-570
Reserve money (ceiling)	1,133	1,133	1,128	1,235	1,235	1,236	1,250	1,328	1,302	1,348
Net international reserves of the Bank of Tanzania (floor) 3/ 4/	1,763	1,523	1,615	1,921	1,765	1,808	1,790	1,779	1,685	1,656
Accumulation of external payments arrears (ceiling) 5/	0	0	0	0	0	0	0	0	0	0
Contracting or guaranteeing of external debt on										
nonconcessional terms (ceiling)	0	0	0	0	0	0	0	0	0	0
Memorandum item:										
Foreign program assistance (grants and loans) 1/	442	442	202	758	758	601	823	688	838	767

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

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

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

3/ Excludes any use of IMF MDRI funds held at the Bank of Tanzania (beyond the US$50 million already envisaged) for the foreign exchange component of government outlays, consistent with para. 20 of the MEFP.

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

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

Table 2. Tanzania: Structural Performance Criteria and Benchmarks Under the Poverty Reduction and Growth Facility Arrangement, July 2005-June 2006

Measure	Date of Implementation	Status
Tax policy and administration		
Integrate the destination inspection program with customs procedures at all customs offices in the Dar es Salaam region as described in paragraph 27 of the MEFP. 1/	End-January 2006.	Observed
Increase the number of staff in the post-clearance audit section of customs to 32 as described in paragraph 27 of the MEFP. 1/	End-March 2006.	Observed
Financial sector reform		
Limit Government guarantees under the three medium-term credit facilities as described in paragraphs 42-44 of the MEFP. 2/	Continuous.	Observed.
Inter-agency committee on financial sector reform will submit to government a proposed unified legal and regulatory framework for all pension funds, and investment guidelines, as described in paragraph 46 of the MEFP. 1/	End-June 2006.	Recruitment of technical assistant through World Bank is proceeding.
Governance		
The Government will ensure that the instruments establishing the Development Finance Guarantee Facility and Development Finance Institution require an annual independent operational audit to verify that the funds are being used for the purposes intended and that proper governance procedures have been followed, as indicated in paragraph 45 of the MEFP. 1/	End-March 2006.	Met for the DFI. However, establishment of the DFGF has been delayed.
Cabinet approval of the new Anti-Corruption Law, as described in paragraph 47 of the MEFP. 1/	End-April 2006.	Not met.
Publish the list of companies, individuals, and NGO's that have received tax exemptions each quarter under the Treasury voucher scheme. 1/	Quarterly.	Observed

1/ Structural benchmark.

2/ Performance criterion.

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

Measure	Date of Implementation
Financial sector reform	
Submit to parliament the Bank of Tanzania Act and the Banking and Financial Institutions Act, consistent with paragraph 23 of the MEFP. 2/	End-April 2006.
Limit Government guarantees under the three medium-term credit facilities as described in paragraphs 42-44 of the MEFP attached to the Government's July 14, 2005 letter of intent. 1/	Continuous.
Inter-agency committee on financial sector reform will submit to government a proposed unified legal and regulatory framework for all pension funds, and investment guidelines, as described in paragraph 46 of the MEFP attached to the Government's July 14, 2005 letter of intent. 1/	End-June 2006.
Energy Sector	
The Government will finalize a financial recovery plan, including tariff increases as appropriate, and a medium-term Power Sector Strategy through FY 2008/09 for TANESCO, consistent with paras. 32-33 of the MEFP. 1/	End-June 2006.
Governance	
The government will ensure that the instruments establishing the Development Finance Guarantee Facility require an annual independent operational audit to verify that the funds are being used for the purposes intended and that proper governance procedures have been followed, as indicated in paragraph 45 of the MEFP attached to the Government's July 14, 2005 letter of intent. 1/	Continuous.
Publish the list of companies, individuals, and NGO's that have received tax exemptions each quarter under the Treasury voucher scheme. 1/	Quarterly.

1/ Structural benchmark.
2/ Performance criterion.

Tanzania: Relations with the Fund
(As of February 28, 2006)

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

		SDR million	Percent Quota
II.	**General Resources Account:**	SDR million	Percent Quota
	Quota	198.90	100.00
	Fund holdings of currency	188.90	94.97
	Reserve position in Fund	10.00	5.03
III.	**SDR Department:**	SDR million	Percent Allocation
	Net cumulative allocation	31.37	100.00
	Holdings	0.26	0.81
IV.	**Outstanding Purchases and Loans:**	SDR million	Percent Quota
	Poverty Reduction and Growth Facility Arrangements	5.60	2.82

V. Latest Financial Arrangements:

Type	Approval date	Expiration date	Amount approved (SDR million)	Amount drawn (SDR million)
PRGF	08/16/2003	08/15/2006	19.60	14.00
PRGF	04/04/2000	08/15/2003	135.00	135.00
PRGF	11/08/1996	02/07/2000	181.59	181.59

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

	Forthcoming				
	2006	**2007**	**2008**	**2009**	**2010**
Principal					0.28
Charges/interest	0.84	1.09	1.09	1.09	1.09
Total	0.84	1.09	1.09	1.09	1.37

VII. Implementation of HIPC Initiative:

	Enhanced framework
Commitment of HIPC assistance	
Decision point date	Apr 2000
Total assistance (US$ million)	2,026.00
Of which: Fund assistance (US$ million)	119.80
Completion point date	11/21/01
Delivery of Fund assistance (SDR million)	
Amount disbursed	88.95
Interim assistance	26.68
Completion point balance	62.27
Additional disbursement of interest income[1]	7.45
Total disbursements	96.40

VIII. Implementation of MDRI Assistance:

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

2. Debt relief by facility (SDR million)

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

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

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

IX. Safeguards Assessments:

Under its safeguards assessment policy, the Fund assessed the Bank of Tanzania (BoT) with respect to the PRGF arrangement that was approved on August 16, 2003, and is scheduled to expire on August 15, 2006.

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

X. Exchange Arrangements:

The currency of Tanzania is the Tanzania shilling. The official exchange rate is determined in relation to the rate established in the interbank market for foreign exchange. The middle rate in terms of the U.S. dollar, the intervention currency, was T Sh 1,186 per U.S. dollar as of end-February 2006. The exchange system is free of restrictions on the making of payments and transfers for current international transactions.

XI. Article IV Consultation:

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

XII. Technical Assistance, 2002–06:

Department	Date	Form	Purpose
Fiscal Affairs	2001–02	Long-term consultant	Strengthen fiscal analysis at the Ministry of Finance
	October 2002	Mission	Tax administration
	2002–03	Long-term consultant	Public expenditure management
	Mar.–May 2003	Peripatetic advisor	Tax administration
	April 2003	Mission	Inspection and tripartite review
	June–Sep. 2003	Long-term consultant	Public expenditure management
	Sep.–Oct. 2003	Peripatetic advisor	Tax administration
	Oct 2003	Mission	Tax administration
	November 2003	Multicountry mission	EAC tax harmonization
	April 2004	Mission	Customs administration
	July 2004	Peripatetic advisor	Tax administration
	July 2004	Mission	Public Expenditure Management Assessment and Action Plan
	September 2004	Mission	Review of mining taxation
	September 2004	Mission	Tax administration (Zanzibar)
	April 2005	Mission	Customs administration
	July 2005	Mission	Improve the effectiveness of the Ministry of Finance
	Aug.- Sep. 2005	Mission	Tax administration
	Oct.–Nov. 2005	Mission	Strengthen macrofiscal analysis at

			the Ministry of Finance
	December 2005	Mission	Tax policy
Legal	Oct. 21–Nov. 2, 2002	Mission	Income tax law
	March 17–April 3, 2003	Mission	Income tax law
	Sept. 15–27, 2003	Mission	Income tax law
	June 6–13, 2004	Mission	Income tax law
	July 2004	Mission with MFD	Central and commercial bank legislative reform
	July–November 2004	Desk review	Foreign Exchange Act, Evidence Act, Bills of Exchange Ordnance, National Payment System bill, Electronic Transactions bill
Monetary and Financial Systems	March 2001	Mission	Monetary policy operations
	June 2001	Mission	Public debt and domestic market management
	2001–2002	General Advisor	General advice to the BoT
	Feb. 2003	Mission	Pre-FSAP mission
	May 2003	Mission	FSAP
	November 2003	Mission	FSAP follow-up workshop
	March 2004	Mission	Accounting and banking supervision
	June 2004	Mission	BoT accounting
	July 2004	Mission	Central and commercial banking legislation reform with LEG
	August 2004	Mission	Financial sector reform/FSAP follow-up
	November 2004	Mission	BoT accounting
	December 2004	Mission	Second FSAP follow-up workshop
	May 2005	Mission	Financial sector reform/FSAP follow-up
	September 2005	Mission	Credit reference database and IFRS-generated reports
	January 2006	Mission	Monetary Operations and Forex
	January 2006	Mission	Problem bank resolution
	February 2006	Mission	Prudential regulations
Statistics	May 2002	Mission	Balance of payments statistics
	2002–03	Long-term consultant	Multisector statistics
	October 2002	Mission	Data ROSC
	August 2003	Mission	Government finance statistics
	Jan./Feb. 2005	Mission	Monetary statistics
	December 2005	Mission	Technical assistance evaluation

XIII. Resident Representative:

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

Tanzania: Relations with the World Bank Group

Partnership in Tanzania's Development Strategy

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

Bank Group Strategy

The Bank's Board approved the current Country Assistance Strategy (CAS) for Tanzania on June 15, 2000. Government is preparing a new Tanzania Joint Assistance Strategy (TJAS), which is expected to provide the framework for the Bank's next CAS as well as for the assistance strategies of other development partners. The TJAS is expected to be finalized in FY2006. The current CAS emphasizes higher economic growth, poverty reduction, and institutional reforms to improve governance. It conforms with the government's main strategy of adherence to macroeconomic stability, increased private sector participation in the economy, a renewed emphasis on rural development, and improved delivery of social services. It also supports the government's desire to enter into new relationships with its development partners, phasing in a switch from projects to programs, for more effective and efficient use of aid resources.

The Bank is supporting implementation of the Poverty Reduction Strategy through a series of Poverty Reduction Support Credits and Grants (PRSC). The source of the Bank's PRSC is the General Budget Support (GBS) program, which is also supported by 13 other donors. There is joint performance assessment and a common review process. The GBS focuses on scaling up pro-poor growth, especially through rural development and improvements in the business environment. The GBS also supports strengthening public expenditure management and public service delivery, especially in the priority sectors for poverty reduction, and putting in place a system to ensure that sectoral programs are accountable for their results. The first PRSC (total US$132 million, of which US$32 million in grants) was approved by the Bank's Board on May 29, 2003. The second (US$150 million, of which US$90 million in grants) was approved by the IDA Board on July 29, 2004. PRSC 3, a credit of US$ 150 million was approved by the Bank's Board on September 8, 2005. The implementation of policy reforms agreed upon under the PRSC is supported by a series of technical assistance and investment projects, such as project support to improve tax administration, reform the public sector, and build the financial sector, including rural finance and microfinance. A new multiyear Poverty Reduction Budget Support (PRSC4) program, to be aligned with the NSGRP, is expected to be presented to the Board in May 2006.

In the social sectors, the Bank approved adjustment lending operations for primary education between October 2001 and October 2004 and, more recently, for secondary education (US$150 million each). The objectives are to improve education, expand school access, and increase school retention at both primary and secondary levels. Bank support has already facilitated a significant increase in school enrollments. The Bank contributes to the health sector multidonor "basket fund," which supports sector reforms and funds nonwage expenditures. A multisector

HIV/AIDS project supports Tanzania's efforts to reduce HIV transmission and mitigate the adverse consequences of AIDS. In the water sector, one project supports technical, commercial, and financial rehabilitation of the water supply and sanitation services in Dar es Salaam. Another supports access to improved and sustained water and sanitation services in rural communities. The objective of the IDA-funded Tanzania Social Action Fund (TASAF) is to enhance the capacities of communities and other stakeholders to prioritize, implement, and manage sustainable development initiatives and in the process improve socioeconomic services and opportunities. The Bank's Board approved the Tanzania Second Social Action Fund (US$150 million) on November 30, 2004, to continue the successful outcomes from TASAF-1.

In agriculture, the Bank supports policy reforms through analysis and the policy dialogue under the PRSC. The Bank also supported the country's efforts from January 1998 to June 2004 to strengthen agriculture research and extension services. The Bank's Board approved a Participatory Agricultural Development and Empowerment Project Credit in May 2003 to support investments in technologies to reduce soil fertility decline.

A Forest Conservation and Management Project helps the government implement policy, particularly by building a framework for long-term sustainable management and conservation of Tanzania's forests. The Marine and Coastal Environment Management Project, covering Tanzania, Uganda, and Kenya, was approved in 2005. It is working to improve management of the Lake Victoria ecosystem.

Efforts to improve Tanzania's infrastructure are supported by road and railway projects and an urban rehabilitation project. In April 2004, the Bank's Board approved a credit of US$122 million to (1) upgrade strategic road links, (2) enhance road management capacity, and (3) improve the operations of Tanzanian Railways (TRC and TAZARA). The policy dialogue is now helping prepare a new Road Act, which will be the basis for strengthening the policy and institutional framework for road development and maintenance.

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

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

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

An accountability and transparency project is being prepared for presentation to the Board in May 2006.

The International Finance Corporation (IFC) has a committed portfolio in Tanzania that stands at $36 million, including investments in agribusiness, manufacturing, tourism, and finance. Recent transactions were a $10 million investment in Bonite Bottlers, a carbonated soft drinks manufacturer, and a $3 million subordinated loan to Exim Bank, a leading SME financial institution. At present, the Multilateral Investment Guarantee Agency (MIGA) has no exposure in Tanzania and no projects planned for FY06.

Tanzania joined the World Bank Group in 1962. Beginning with an IDA credit for education in 1963, it has received a total of 138 credits, 7 grants and 27 loans, totaling US$5.7 billion (US$5.4 billion from IDA). Total disbursements amounted to US$4.7 billion as of December 31, 2005 (US$4.1 billion from IDA, US$355.6 million from the IBRD, and US$274 million IDA grants). Currently, the portfolio comprises 23 active projects, with commitments of US$1.6 billion, in all major sectors; the undisbursed balance is US$880 million.

Statement of Loans, Credits, and Grants (As of December 31, 2005; in U.S. dollars)

	IBRD	IDA Credits	IDA Grants	Total
Original Principal	361,030,400	5,080,469,393	274,400,000	5,715,899,793
Cancellations	5,477,944	232,216,272	0	237,694,216
Disbursed	355,552,456	4,141,021,532	190,895,970	4,687,469,958
Undisbursed	0	830,547,033	88,844,958	919,391,992
Repaid	355,462,456	439,140,902	0	794,603,358
Due	0	3,860,938,633	0	3,860,938,633
Exchange Adjustment	0	0	0	0
Borrower Obligation	0	3,860,938,633	0	3,860,938,633

Source: World Bank Group

Bank-Fund collaboration in specific areas

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

- **Public expenditure management.** Improvements in public expenditure management have been a top priority of the Tanzanian government since 1995. The Bank, the Fund, and other donors have worked closely together to give the government needed support for institutional and policy reforms. The Fund is leading the dialogue on fiscal policy; the Bank concerns itself with strategic resource allocation and operational efficiency of public expenditures. In the area of fiscal policy, reducing domestically financed deficits has brought sustained macroeconomic stability over the past five years. To enhance strategic resource allocation and operational efficiency, the Bank is supporting a government-led, participatory public expenditure review/medium-term expenditure framework (MTEF) process. This effort helped to strengthen and open up the budget process and the allocation of resources to pro-poor priority areas. The Bank is also involved in the fiscal decentralization process through analytical work and the Local Government Support Project. The Bank and the Fund work together to support institutional budget and expenditure management reforms. The annual Bank-led Public Expenditure and Financial Assessment Report (PEFAR), the first of which was issued in May 2005, is the main instrument for the donor community to assess progress. A joint Bank-IMF assessment of capacity to track poverty-reducing expenditure noted the improvements in public financial management and fiduciary systems in recent years. The Bank also prepared a Country Procurement Assessment Report, which acts as an agenda for strengthening procurement systems in Tanzania.

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

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

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

- **Energy sector.** The Bank and the Fund liaise closely to find ways to address the crisis in the energy sector. The Bank takes the lead in assisting the authorities with developing emergency power generation plans to alleviate power supply shortages and prepare a financial recovery plan for the state electricity utility, TANESCO.

- **Trade reforms.** The Bank and the Fund are working closely to help Tanzania establish a pro-growth trade program. Within the context of the Integrated Framework, the Bank led the preparation of a Diagnostic Trade Integration Study, which was issued in July 2005. The Bank is working toward trade expansion though its regional trade facilitation project. It is also active at the regional level in the dialogue on trade reforms within the East African Community.

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

Statement by the IMF Staff Representative
April 7, 2006

This statement provides information that has become available since the staff report was issued. The thrust of the staff appraisal remains unchanged.

1. **Preliminary indications are that the authorities met the end-March 2006 quantitative performance criteria for reserve money, net international reserves, and net domestic financing of the government, and also met the quantitative indicative target for net domestic assets of the Bank of Tanzania.** Staff have not yet received information regarding other quantitative targets.

2. **Interest rates have continued to fall, and inflation has increased.** The weighted average yield on T-bills fell to 12.4 percent at end-March, down from 15.3 percent at end-December. The 12-month headline inflation rate increased in February—to 5.8 percent from 5.0 percent at end-December—driven mainly by food prices. Nevertheless, core inflation (excluding food and fuel) has remained below 2 percent.

3. **Regarding food security, reports from Tanzania indicate that the onset of the long rains season (March-May) has been normal.** The World Food Programme is coordinating information on food availability and is working closely with the authorities to monitor the situation.

4. **Regarding energy, the water levels in TANESCO's dams have risen slightly but are still critically low.** The bidding process for the leasing of additional thermal generation capacity needed to resolve the problem of power shortages have started and the government has received and is currently evaluating a draft financial recovery plan for TANESCO, including the magnitude and timing of proposed tariff adjustments.

Press Release No. 06/71
FOR IMMEDIATE RELEASE
April 7, 2006

International Monetary Fund
Washington, D.C. 20431 USA

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

The Executive Board of the International Monetary Fund (IMF) today completed the fifth review of Tanzania's economic performance under a three-year Poverty Reduction and Growth Facility (PRGF) arrangement (see Press Release No. 03/127.) The completion of the review enables a further release of an amount equivalent to SDR 2.8 million (about US$4.1 million) under the arrangement, and will bring the total disbursements under the program to the equivalent of SDR 16.8 million (about US$24.4 million.)

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

“The Tanzanian authorities deserve credit for sustaining strong economic performance through market-oriented policies within an appropriate macroeconomic framework. Despite recent successes, Tanzania will need to maintain sound policies and steadily pursue key structural reforms and capacity building for many years to remove key impediments to broad-based growth and achieve lasting inroads against poverty. Sustained reform efforts will be needed to stimulate private-sector led growth, particularly in such areas as infrastructure, energy, governance, and the business environment.

“The authorities’ strong efforts to maintain prudent economic policies are commendable, particularly in light of the challenges posed by the impact of the drought on agricultural output and energy production. In this context, it will be critical to resolve the energy supply issues without unduly burdening public finances, while, at the same time, developing a sound financial recovery plan to address the finances of TANESCO and a Power Sector Strategy to address power generation over the medium term.

“In response to the drought, a more accommodative policy stance is warranted, including a higher net domestic financing of the budget and a modest upward adjustment in money growth, to avoid crowding out private sector credit to productive sectors. Nevertheless, the authorities will closely monitor prices for signs of emerging inflationary pressures and the Bank of Tanzania will continue to use its full range of tools, including heavier reliance on foreign exchange sales and better management of government deposits in commercial banks, to help better distribute the impact of sterilization efforts on interest and exchange rates.

"The authorities' ongoing efforts to mobilize further domestic resources are critical to provide resources for key development programs and to reduce the dependence on foreign aid. In this regard, it will be important to deepen the tax and customs administration reform efforts to help support government policy objectives. The extent of tax incentives for Special Economic Zones and the potential for revenue loss are worrisome and addressing structural impediments to private sector growth would be a more effective and less costly way of attracting private sector investment. The effectiveness of government spending will be enhanced by better linking the goals of MKUKUTA, Tanzania's new five-year PRSP, to the budget process and the Medium-Term Expenditure Framework.

"The Fund commends the authorities' decision to ensure that the MDRI relief from the Fund is channeled to addressing pressing social and growth-critical economic challenges, especially those emanating from the drought, and without affecting domestic liquidity. In this regard, it will be important to ensure that the use of these resources is subject to all regular procurement and financial management rules and is incorporated in the budget, beginning in 2006/07.

"The authorities' interest in a successor program in the context of a PSI is a logical development in light of Tanzania's position as a mature stabilizer," Mr. Carstens said.

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

**Statement by Peter J. Ngumbullu, Executive Director
for the United Republic of Tanzania and
Joseph L. Masawe, Senior Advisor to Executive Director
April 7, 2006**

Introduction

1. The Tanzanian authorities express their appreciation to the Fund Board and Management and the international community for their continued support and involvement in the ongoing reform agenda in Tanzania. They also appreciate staff for preparation of well balanced reports on the fifth review of the PRGF program and Ex Post Assessment of Longer Term Engagement, the PRSP Joint Staff Advisory Note, as well as the candid exchange of views they had with staff during discussions. They take note of staff's comments and recommendations and broadly agree with the analysis, findings and recommendations made.

Recent Macroeconomic Developments

2. Tanzania's economy continued to perform outstandingly well during 2005, as characterized by a strong growth in GDP and sustained low level of inflation. During the year, GDP grew strongly by around 7 percent, driven by good performance in trade and tourism, manufacturing, mining and construction, which accounted for a combined total of 40 percent of the GDP. However, inflation inched upwards from 4.2 percent in June 2005 to 5 percent in December 2005, following the impact of persistent rising oil prices and a countrywide drought, which affected food production and hydropower generation. Despite this instability, Tanzania continued to enjoy an impressive record of macroeconomic stability, supported by stable political environment.

3. While the long record of Tanzania's macroeconomic and political stability is widely appreciated, the Tanzanian authorities recognize that several challenges and downside risks still remain going forward and notwithstanding this performance, these achievements have not translated into real gains to the people. As also appreciated by staff in their Ex-Post Assessment of Longer Term Program Engagement report, strong performance in Tanzania has not translated into significant decline in poverty, or positive impact on increase in private investment and poverty still remains pervasive. The new government, following Tanzania's general election end of last year, has reaffirmed its commitment to sustained implementation of the ongoing reforms, particularly the consolidation of macroeconomic stability and debt sustainability, and deepening of structural reforms while strengthening government-private sector partnership to enable Tanzanians benefit from the current positive macroeconomic achievements.

Performance Under the Program

4. In spite of the negative impact of bad weather and the energy crisis during 2005, all quantitative performance criteria and most indicative targets for the first six months of the 2005/06 have been met. The indicative target for base money and end-September and end-December targets were missed by slight margins because of difficulties associated with the high liquidity in the banking system. The unanticipated liquidity was caused by increased

outlays by the government and the Bank of Tanzania, mainly to offset the impact of the drought and power generation shortfalls. Implementation of structural targets was broadly on track.

Fiscal Policy Developments

5. During the first half of the fiscal year 2005/06, fiscal performance was generally on track as revenues remained in line with projections, following improved tax administration. Reforms at the Tanzania Revenue Authority (TRA) continued during the review period, with the VAT and Income Tax Departments being put under one new department of Domestic Revenue Department (DRD). This measure was aimed at increasing the efficiency of TRA. However, during the period, expenditures were higher than programmed, having been driven by additional costs associated with the postponement of the national elections and increased transfers to TANESCO to mitigate increased costs of power generation. This was further worsened by increased cost for procurement and distribution of food to areas affected by drought and increased pension payments.

Monetary Policy

6. The economy continues to face the problem of excess liquidity, with considerable build up being recorded during the first six months of 2005/06. To mitigate the problem, the Bank of Tanzania (BOT) stepped up its sales of treasury bills complemented with foreign exchange; and to facilitate this objective, the treasury bills tender size for liquidity management was increased by 44 percent between July and December 2005. The Bank also continued to use short term repurchase agreements to fine-tune liquidity in the economy.

7. The prudent monetary policy stance of the BOT facilitated increased flows of credit to the economy, with private sector credit growing by an impressive 32.1 percent over the first six months. The authorities are taking additional measures to ensure that the vibrant credit growth is maintained without compromising financial sector stability. A credit guarantee scheme for exporters and small- and medium-size enterprises (SMEs) has been established to facilitate this important objective.

External Sector Developments

8. Given a significant shortfall in program support disbursement, the current account deficit widened during the first six months of 2005/06, despite a noticeable increase in export earnings and tourism receipts. However, the official reserves position continued to strengthen, reaching a comfortable level of the equivalent of 5½ months of import cover. The nominal exchange rate remained stable over the six months period, depreciating by only 3.9 percent.

9. The authorities would like to take this opportunity to thank the international community for extending generous debt relief to Tanzania, both under the HIPC Initiative and the MDRI, which will enhance debt sustainability and provide the much needed fiscal space to meet pro-poor expenditures and challenges following the drought and the current energy crisis. The government continues to negotiate with the few remaining Paris Club creditors to extend their commitments for debt relief to Tanzania.

Policies for 2006/07 and Medium-Term Outlook

10. Growth of the economy is projected to slow down slightly during the second half of 2005/06, to real GDP growth of around 5.8 percent, compared to 7.2 percent originally projected under the program. The projected slowdown is due to the impact of the current drought on agriculture and the shortfall of electricity generation. These projections are based on the assumption that long rains, which normally begin around April, will continue and also additional measures will be taken to address problems of power generation.

11. Inflation is projected to edge upwards to around 6 percent, following impact of persistent high world market prices of oil and fuel. The authorities will continue to exercise prudent monetary policy, which together with increased government subsidized food imports, is expected to dampen pressure on food prices.

Fiscal Policy

12. The authorities will continue to strengthen measures aimed at increasing government revenue. With the expected normal long rains and ongoing improvements in tax administration, the authorities are confident that the projected revenue targets will be attained. On the expenditure side, however, outlays may be higher than projected. In light of the increased drought and energy supply related expenditures, the authorities estimate that total expenditure of about 28 percent of GDP may be incurred during 2005/06, above the originally projected level of 26.8 percent of GDP.

13. The authorities will continue to implement reforms in tax administration during the remaining part of the fiscal year. These will include increasing the coverage of the Large Tax Payers Department (LTD), and development of an action plan following the merger of the two domestic revenue departments under one roof. The taxpayer segmentation approach for medium taxpayers will also be extended and strengthened.

14. On the expenditure side, strengthening of the expenditure management system will continue to remain a top priority of the government. Transparency and accountability in expenditure management will be enhanced, in line with the objectives of the government's second generation Poverty Reduction Strategy Paper (PRSP), also referred to as MKUKUTA. Over the period, IFMIS will be rolled out to eligible Local Government Authorities (LGAs), while continuing with capacity building efforts, especially in accounting, at LGAs level. On the other hand, efforts to strengthen the National Audit Office will be enhanced, especially with respect to capacity building.

15. While drought and power shortfall continue to be a major challenge to the authorities, several measures have already been implemented to mitigate severe negative effects. The authorities have developed a financial recovery plan for TANESCO together with a Power Sector Reform Strategy to address power generation over the medium term. An inter-ministerial committee at the Permanent Secretaries level has been established to monitor on daily basis, developments in the energy sector. The committee which is under the chairmanship of the Ministry of Finance reports to the Cabinet. The authorities are also contemplating a small tariff increase to improve TANESCO's cash flow and they intend to

use part of the savings from MDRI to address the impact associated with the current drought and power generation in a manner that will not pose adverse liquidity impact on the economy. The proposal is to use the resources on direct imports of additional electricity generating capacity to alleviate the current electricity crisis and also for humanitarian food imports to be distributed to poor families impacted by the drought, especially those in rural areas.

16. Recent information from the authorities indicates that long rains have started and are proceeding well. TANESCO has announced a relaxation of the power rationing following improvement in water levels in the major dams for hydro generation. The authorities are optimistic that if the current long rains continue, the impact of the drought on the budget will be reduced.

Monetary and Financial Policies

17. The government intends to keep monetary policy focused towards containing liquidity pressures in the economy, while promoting credit growth, especially to the productive sector. In this respect, the BOT will continue to sharpen its liquidity forecasting, while maintaining base money as its operating target. The BOT recognizes that the path of liquidity has been uneven and is looking at the ways to improve liquidity management. Collaboration between the central bank and the finance ministry will be further strengthened, to ensure that fiscal policy continues to remain supportive to monetary policy. In this spirit, the Bank of Tanzania and the Ministry of Finance have initiated a joint capacity building program which would help, among other things, to smoothen spending patterns.

18. The authorities are continuing with efforts to implement broad based second generation financial sector reforms, which will increase the contribution of the financial sector to investment and growth. Strengthening the autonomy of the central bank while increasing its accountability will be given top priority. The government submitted to Parliament, amendments to the BOT Act and the Banking and Financial Institutions Act (BFIA) in early April this year, to facilitate this objective. The bills amending the BOT Act and the BFIA were tabled and passed by Parliament this week.

19. The authorities intend to launch a Development Finance Guarantee Facility (DFGF) to improve the availability of medium-term credit to the productive sector. Likewise, measures are being implemented to facilitate the establishment of a Development Finance Institution (DFI) with limited government involvement, to channel multilateral and bilateral donor funds through commercial banks to individual borrowers. The DFI will operate under the principles of good governance and transparency.

20. In addition, the Tanzanian authorities will continue to implement its policies as spelt out in the MKUKUTA which aims at developing a competitive national economy, driven by private sector investment, infrastructure development and investment in human capital. Economic policies will be geared towards three clusters of outcome, viz; growth and reduction of income poverty, improved quality of life and social being and good governance and accountability. The authorities are preparing a matrix of indicators that would allow measurement of progress attained in the three clusters. As a first step, Tanzanian authorities,1 in collaboration with UNCTAD and the Japan Bank for International Cooperation (JBIC)

have completed preparation of the Investment Blue Book for Tanzania, to disseminate widely, Tanzania's investment opportunities and efforts being made to improve the country's investment environment.

Conclusion

21. In conclusion, as stated earlier, medium and long term challenges to the authorities entail implementing policies that will facilitate transferring of the current gains in macroeconomic and political stability into real gains to the Tanzanian people, as despite a decade of impressive growth in Tanzania, poverty remains widespread, particularly in rural areas and private sector expansion has been weak. In his first address to the Tanzania National Business Council (TNBC) early this year, the President of the United Republic of Tanzania, **Honorable Jakaya Kikwete** observed that **the benefits of correct macroeconomic policies have not reached the majority of Tanzanians, and that the remaining challenges to both the political leadership as well as the business community is how the right macroeconomic fundamentals can speedily and consistently be sent to the micro level, especially to the poor rural dwellers.** The President expressed the commitment of the current government towards staying the course of reform and openness to alleviate poverty, as guided by Tanzania's new poverty reduction and growth strategy, the MKUKUTA.

22. In this regard, the authorities of the new government have reaffirmed their strong commitment to prudent and market-oriented policies aimed at attaining higher growth, employment creation and poverty reduction. Having achieved macroeconomic stability, they are aware that strong performance of domestic revenues will be key towards achieving the objectives of MKUKUTA and reducing Tanzania's aid dependence. They will continue to implement medium term revenue enhancing measures, to enable achievement of the projected revenue of at least 14.4 percent of GDP by 2006/07. They look forward to continued relationship with the Fund and other development partners to meet these challenges.

23. As the current PRGF arrangement expires in August 2006, the authorities have requested for a nonborrowing arrangement from the Fund under the Policy Support Instrument (PSI) as a successor program. They look forward to continued Fund's assistance in the areas of fiscal, monetary and financial sector policies for institutional strengthening and promotion of transparency, governance and accountability of public resources.