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TANZANIA ECONOMIC UPDATE

The Efficiency and Effectiveness of Fiscal Policy in Tanzania

Issue 19
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Tanzania Economic Update

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ACRONYMS AND ABBREVIATIONS

AEs	Advanced Economies
AGO	Angola
BoT	Bank of Tanzania
BWA	Botswana
CAD	Current Account Deficit
CAG	Controller and Auditor General
CCT	Conditional Cash Transfer
CEQ	Commitment to Equity
CG	Central Government
CIT	Corporate Income Tax
CMR	Cameroon
COVID-19	Coronavirus Disease of 2019
CPI	Consumer Price Index
CY	Calendar Year
DEA	Data-envelopment Analysis
DR	Dominican Republic
DSA	Debt Sustainability Analysis
EFD	Electronic Fiscal Device
EFF	Extended Fund Facility
EMBI	Emerging Markets Bond Index
EMDEs	Emerging Markets and Developing Economies
FDI	Foreign Direct Investment
FY	Fiscal Year
FYDP	Five-Year Development Plan
GDP	Gross Domestic Product
GHA	Ghana
HBS	Household Budget Survey
HCI	Human Capital Index
H1	First Half
IMF	International Monetary Fund
KEN	Kenya
LGA	Local Government Authority
SSA	Sub-Sharan Africa
TADAT	Tax Administration Diagnostic Assessment Tool
TRA	Tanzania Revenue Authority
Tsh	Tanzania Shilling
TZA	Tanzania
UAE	United Arab Emirates
UGA	Uganda
UMICs	Upper-Middle Income Countries
US	United States
US$	United States Dollars
LHS	Left Hand Side
LICs	Low-Income Countries
LMICs	Lower-Middle Income Countries
LSO	Lesotho
MFO	Macro, Finance, Outlook
MoFP	Ministry of Finance and Planning
MOZ	Mozambique
MPO	Macro Poverty Outlook
MUS	Mauritius
MUSE	Mfumo wa Ulipaji Serikalini
M3	Extended Broad Money Supply
NAM	Namibia
NBS	National Bureau of Statistics
NDA	Net Domestic Assets

NFA	Net Foreign Assets
NGA	Nigeria
No.	Number
OCGS	Office of the Chief Government Statistician
PAYE	Pay As You Earn
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PFMRP	Public Financial Management Reforms
PIT	Personal Income Tax
PMI	Purchasing Managers' Index
PPG	Public and Publicly Guaranteed
PPP	Purchasing Power Parity
ppt.	Percentage Points
Q1/4	Quarter 1/4
RHS	Right-hand Side
RWA	Rwanda
SMEs	Small and Medium Enterprises
SOE	State-owned Enterprises
VAR	Vector Autoregressive
VAT	Value Added Tax
WB	The World Bank
WDI	World Development Indicators
WEF	The World Economic Forum
y/y	Year-over-Year or Year-on-Year
ZAF	South Africa
5M	The first five Months
4-qma	Four Quarter Moving Average

PREFACE

The Tanzania Economic Update (TEU) is a biannual report describing the recent evolution of Tanzania's economy, and each edition highlights a subject of critical interest to policymakers. The TEU series is also designed to reach a broader audience of stakeholders that includes the private sector, the government's development partners, and the public. To ensure that the TEU is accessible to as wide a readership as possible, each edition is presented in a relatively nontechnical style.

This nineteenth edition of the TEU was prepared by a team from the World Bank's Macroeconomics, Trade and Investment (MTI) Global Practice, with contributions from several other Global Practices. The overall effort was led by Saadia Refaqat (Senior Country Economist, EAEM1) and Emmanuel Mungunasi (Senior Economist, EAEM1). The analysis benefited from advice provided by William Battaile (Program Leader, EAEDR).

Saadia Refaqat (Senior Country Economist, EAEM1) authored the sections on monetary policy and inflation, balance-of-payments position and macroeconomic outlook and risks, while the sections on recent economic activity, fiscal and debt developments, and Zanzibar recent economic synopsis were co-authored by Xu Dong (Consultant, EAEM1) and Saadia Refaqat (Senior Country Economist, EAEM1). Pedro Olinto (Senior Economist, EAEPV), Rob Swinkels (Lead Country Economist, EAWDR), and Revocatus Washington Paul (ET Consultant, EAEPV) provided input on poverty trends. Sergiy Kasyanenko (Economist, EPGDR) prepared the section on global economic conditions. Box 1 (The State of Tanzania's Economy in Six Charts), Box 2 (Recent Inflation in Tanzania vs. Regional Countries: Some Observations) and Box 5 (External Competitiveness in Tanzania – Where Does it Stand?) were prepared by Saadia Refaqat (Senior Country Economist, EAEM1), while Box 3 (Government Expenditure Arrears: Current Status) and Box 4 (Preliminary Budget Analysis for FY2023/24) were prepared by Xu Dong (Consultant, EAEM1) and Saadia Refaqat (Senior Country Economist, EAEM1). Box 6 (Tanzania's Declining Official Foreign-exchange Reserves: Challenges and Solutions) was written by Xu Dong (Consultant, EAEM1) and Emmanuel Mungunasi (Senior Economist, EAEM1) and Box 7 (Tanzania PFM System Challenges) was authored by Benjamin Ndazi Mtesigwa (Governance specialist, EAEG1) and Emmanuel Mungunasi (Senior Economist, EAEM1).

Salman Zaidi (Consultant, EAEM1) adapted the special focus section of the report from the World Bank's Tanzania Public Expenditure Review FY2022 *titled the efficiency and effectiveness of fiscal policy in Tanzania*. The expenditure-benchmarking section in the larger report was authored by Emmanuel Mungunasi (Senior Economist, EAEM1) and Irina Capita

(Consultant, EMFTX). The revenue-benchmarking section was co-authored by Jaffar Al-Rikabi (Senior Economist, EMFTX), and Joseph Massad (Consultant, EMFTX). The section on the distributional impact of fiscal policy was written by Rob Swinkels, Ercio Munoz (Consultant, EAEPV), Elineema Kisanga (Consultant, EAEM1), Vincent Leyaro (Consultant, EAEPV), and Josephat Hongoli (Consultant, EAEPV).

Hassan Zaman (Regional Director, EAEDR), Asad Alam (Regional Director, EECDR), Abha Prasad, (Practice Manager for MTI, EAEM1), Nathan M. Belete (Country Director, AECE1), and Preeti Arora (Operations Manager, AECE1) provided guidance and leadership throughout the preparation of the report. Rehema Mercy Mashayo, Catherine Audax Mutagwa, Juma Bruno Ngomuo, and Karima Ladjo managed the printing process for this edition of the TEU, with support from Loy Nabeta, who assisted with external communications. Sean Lothrop was responsible for the overall editing of the report. The pictures used were procured for this report unless otherwise acknowledged.

The findings, interpretations, and conclusions expressed in this publication do not necessarily reflect the views of the World Bank's Executive Directors or the countries they represent. The report is based on information current as of early August 2023.

The World Bank team welcomes stakeholder feedback on the content of the TEU. Please direct all correspondence to Saadia Refaqat (srefaqat@worldbank.org) and Emmanuel Mungunasi (emungunasi@worldbank.org).

EXECUTIVE SUMMARY

Global growth is projected to slow significantly in 2023 as continued monetary tightening constrains the credit supply. Inflationary pressures remain strong across much of the world, and headline inflation rates continue to exceed policy targets in most inflation-targeting economies. Stubbornly high inflation has resulted in higher borrowing costs, tighter credit conditions, and elevated financial stress, particularly in commercial real estate and other sectors that are highly sensitive to interest rates. Global economic activity is expected to weaken substantially in 2023, with the global growth rate projected to fall to just 2.1 percent before recovering modestly to 2.4 percent in 2024. Growth in emerging markets and developing economies (EMDEs) is also expected to slow significantly this year due to softening external demand, intensifying credit constraints, and weaker spillovers from China. The aggregate growth rate among EMDEs excluding China is projected to drop from 4.1 percent in 2022 to 2.9 percent in 2023. Meanwhile, the risk of debt distress is rising across EMDEs, especially low-income countries.

Tanzania's economy has performed relatively well despite a challenging external environment. The GDP growth rate reached 4.6 percent in 2022 and is expected to rise to 5.1 percent in 2023, supported by an improving business climate and the implementation of structural reforms. Growth is forecast to average about 5.8 percent over the medium term, as weakening demand, persistent inflationary pressures, and high interest rates prevent a more robust expansion. The headline inflation rate is expected to remain moderate and close to the central bank's target, though elevated global food and fuel prices will continue to exert upward pressure. The current-account deficit is projected to decline gradually over the medium term and will be largely financed by concessional external borrowing and foreign direct investment. The fiscal deficit is expected to narrow as the economic recovery boosts domestic revenues while the growth of public spending slows, and the public debt stock should fall from 43.8 percent of GDP in 2022 to about 38 percent over the medium term.

Tanzania has enjoyed a strong post-pandemic recovery, but recent growth has been concentrated in sectors that employ few workers from poor households. Wealthier households with greater human capital and productive assets have been better positioned to seize the opportunities generated by rapidly growing sectors such as construction, information and communications technology, and real estate. This imbalance in economic opportunities has widened the income gap. Meanwhile, job creation is becoming increasingly urgent as a young and growing workforce intensifies pressure on the labor market. Nevertheless, Tanzania's prospects for reducing poverty are cautiously optimistic, and the national headcount poverty rate is projected to gradually decline as the recovery continues, though unstable external conditions, delays in implementing pro-poor economic policies, and the escalating effects of climate change could threaten the country's hard-won progress on poverty reduction.

The anticipated recovery of agricultural output, coupled with an expanding services sector, is expected to stimulate growth and poverty reduction over the medium term. The government has significantly increased the budget for the agricultural sector, which employs nearly 70 percent of rural workers. As the regional drought subsides, the sector's growth rate is expected to rise from 3 percent in 2022 to 5 percent in 2025. Greater agricultural output will boost household incomes in rural areas, with positive implications for poverty and inequality. Meanwhile, the rapid expansion of retail and repair services is expected to drive growth in the services sector, bolstering the incomes of informal urban workers. Finally, the continued growth of tourism should support further poverty reduction both in urban and rural areas.

The government recognizes that a dynamic private sector fueled both by domestic and international investment is crucial to increase productivity, accelerate job creation, and support more inclusive and resilient growth. In 2018, the authorities adopted the Blueprint for Regulatory Reforms to Improve the Business Environment, which focuses on increasing administrative efficiency and promoting transparency in the public sector. The country's Third Five Year Development Plan prioritizes macroeconomic stability, industrial development, and trade integration, emphasizing the private sector's role in leveraging Tanzania's geographic position and resource endowments to boost production and support inclusive growth. These initiatives are consistent with the National Development Vision 2025, which envisages Tanzania as a middle-income country in which well-developed human capital and an ample supply of high-quality livelihoods yield broad-based gains in living standards.[1]

Tanzania has several macroeconomic advantages that could support a successful transition to middle-income status. It is one of the few economies in the region that did not experience a contraction in 2020. Its modest risk of debt distress offers some space to prudently utilize debt financing. The government's fiscal position remains relatively strong and stable, and international reserves are at a comfortable level. To capitalize on its sound macroeconomic policy environment and to lay the foundation for robust, inclusive, and sustainable long-term growth, the government should seize the opportunity to implement a more ambitious human capital development agenda. Creating adequate fiscal space to invest in human capital in a context of persistently high poverty rates, significant downside risks to the economic outlook, and limited budgetary resources will require reforms both to revenue administration and public spending. Given the indispensable role of fiscal policy in realizing Tanzania's ambitious development vision, this report devotes special attention to understanding how policymakers can effectively mobilize additional resources while maintaining stable budgetary and debt dynamics.

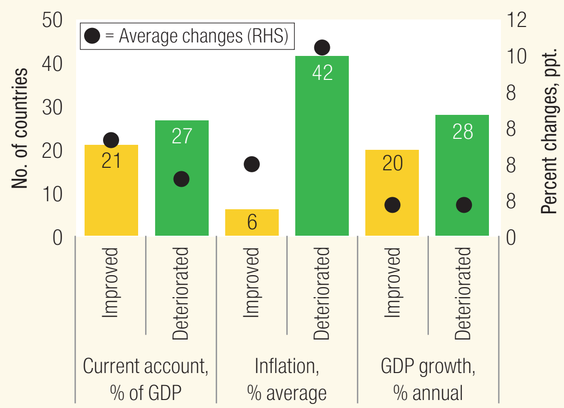
Closing compliance gaps can help bolster revenues while establishing a fairer, more efficient tax system. Improved tax collection helped narrow the tax gap from 8 percent of GDP in 2000 to 5.6 percent of GDP in 2017. The government can further increase tax productivity by adjusting rates, rationalizing exemptions, expanding the tax base, leveraging digital technologies to enhance tax administration, and improving compliance management. Introducing a more rigorous system for taxing income from capital and immovable property could bolster the government's revenue position, while updating cross-border taxation policies could reduce the risks associated with base erosion and profit-shifting by multinational corporations. Strengthening tax administration at the top of the income distribution would improve the tax system's equity while increasing revenue mobilization and reinforcing the social contract. Building the capacity of the tax authorities will be essential to expand collection efficiently and equitably and could lay the groundwork for further reforms. The authorities can complement the ongoing e-filing rollout by enhancing the integrity of the taxpayer database, which will

[1] https://mof.go.tz/mofdocs/overarch/vision2025.htm.

BOX 1: THE STATE OF TANZANIA'S ECONOMY IN SIX CHARTS

FIGURE B1.A • Spillovers from Russia's war in Ukraine have significantly altered the macroeconomic outlook across Sub-Saharan Africa.

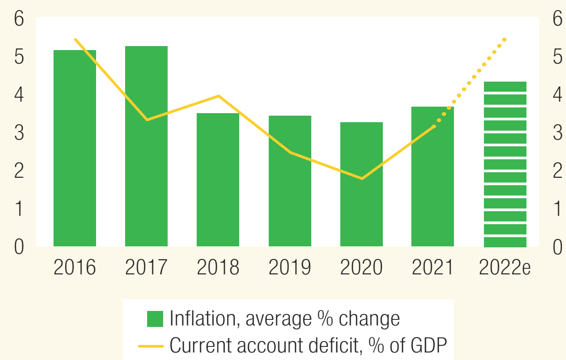
Sub-Saharan Africa Outlook – Anticipated vs Realized
2022 outcome relative to annual meetings MPO, 2021



Source: WB-MPO, Annual 2021 and Springs 2023, WB staff estimates.

FIGURE B1.B • Tanzania's import-dependent economy continues to face challenges on the external front due to the war, the global economic slowdown, and elevated commodity prices.

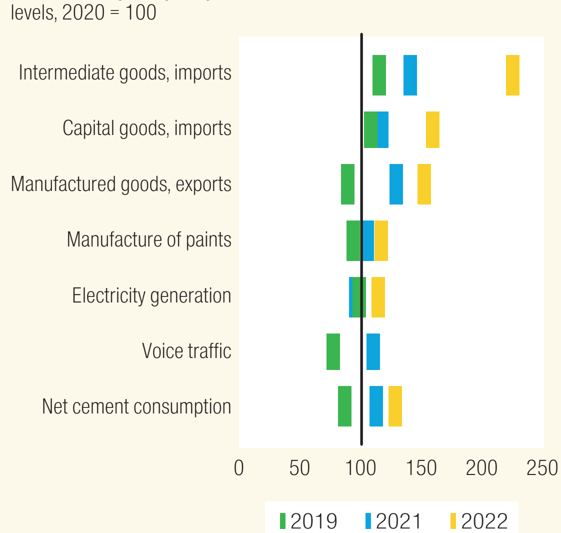
Tanzania – Current Account and Inflation



Source: NBS, WB staff estimates.

FIGURE B1.C • Despite these external headwinds, economic activity remains strong, with prudent macroeconomic management contributing to sustained increases in output.

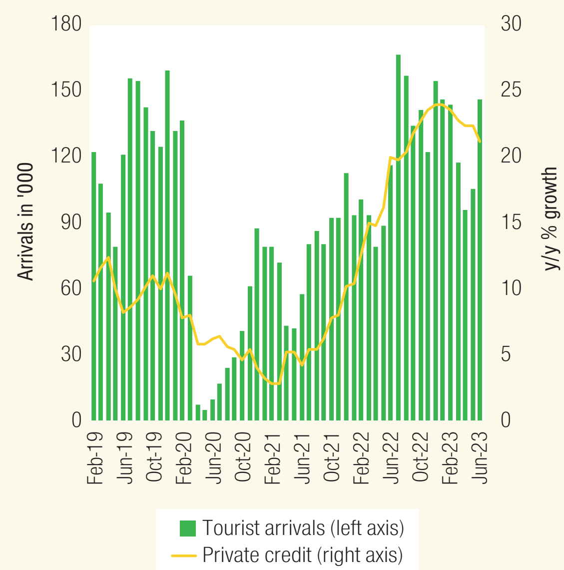
Tanzania – High-frequency Economic Inidcators
levels, 2020 = 100



Source: NBS, BoT, WB staff estimates.

FIGURE B1.D • A robust recovery in the tourism sector, coupled with elevated demand for private credit, continues to support growth.

Tanzania – Tourist Arrivals & Private Credit

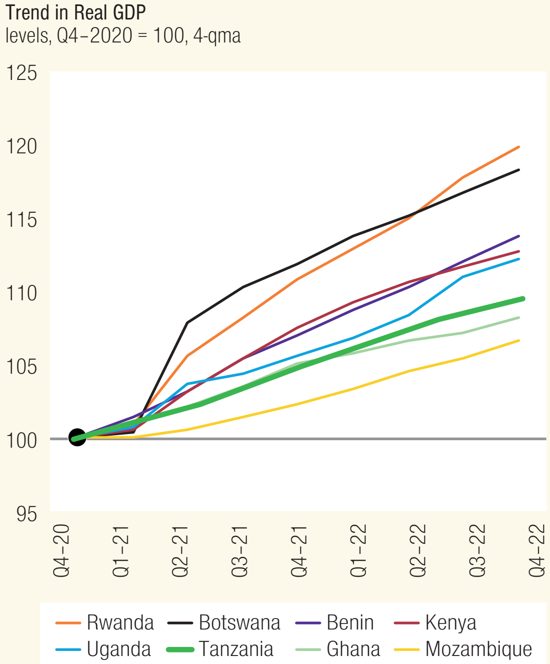


Source: NBS, BoT, WB staff estimates.

(continued on next page)

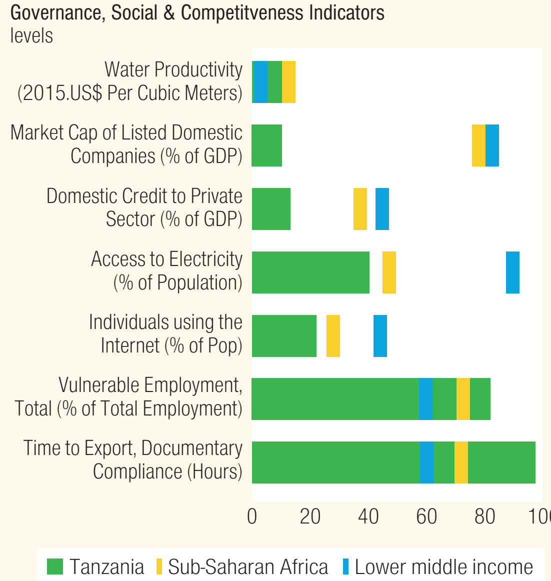
BOX 1: THE STATE OF TANZANIA'S ECONOMY IN SIX CHARTS *(continued)*

FIGURE B1.E • These improvements notwithstanding, Tanzania's recent growth momentum continues to lag many of its peers.



Source: Haver Analytics, WB staff estimates.

FIGURE B1.F • To unlock the economy's full potential, the government will need to deepen reform implementation with support from its development partners.



Source: WDI-WB, WEF, WB staff estimates.
Note: CBM stands for Cubic Meters, Pop stands for Population, and Emp stands for Employment.

be necessary to expand registration. Improving data collection and data analytics, adopting a risk-based approach to compliance management, and hiring and training more auditors could help ensure that all registered taxpayers report and pay their true tax liabilities.

A combination of limited fiscal transparency, low budget-execution rates, and a weak public financial management system undermines the impact of public spending in Tanzania. While the government has increased expenditures in recent years, total public spending remains well below the averages for Sub-Saharan Africa and lower-middle-income countries worldwide. Moreover, low spending levels do not necessarily imply that expenditures are efficient, and a recent report from the Controller and Auditor General's office highlighted key weaknesses in budget credibility, cash management, and commitment controls. These issues can be addressed by improving the reliability of the budget, strengthening internal controls, and allocating resources on a medium-term basis in line with national priorities.

Tanzania's fiscal system substantially reduces income inequality, while public spending on social services more than offsets a moderate increase in poverty. By international standards, Tanzania's fiscal system has a highly positive impact on inequality, and the modest observed increase in poverty is consistent with the experience of comparable countries. Tanzania's direct taxes are highly progressive, and its value-added tax (VAT) also appears to be moderately progressive, unlike VATs in many comparable countries. Several excise taxes are regressive, including those on wine, spirits, tobacco, and kerosene, but these taxes may reduce the consumption of products associated with negative social and health consequences. Broadening the VAT base would reduce inequality, and the additional VAT revenue could be used to offset a marginal increase in the poverty rate. Implementing a standard VAT rate for water and petroleum products would slightly increase poverty by expanding tax liability, but its distributional impact would be progressive. Expanding the VAT base is consistent with improving its fiscal efficiency, as exemptions distort relative prices, and it could generate additional revenue to finance social services, but an increase in conditional cash transfers will be necessary to shield poor households against rising tax liability.

Tanzania's conditional cash transfers are progressive, as are public education and the healthcare services provided at outpatient facilities. Consistent with their core purpose, conditional cash transfers are the most progressive government expenditure. Other expenditures that disproportionally benefit poor households include the provision of public primary education, public preschool, and healthcare at outpatient facilities, as well as public assistance for school uniforms. Spending on most forms of post-secondary public education is slightly progressive, except for public vocational schools. Once the public provision of social services has been accounted for, fiscal policy reduces the poverty rate.

Tanzania's most urgent reform priorities include measures to improve efficiency and effectiveness of expenditure programs and boost tax-revenue mobilization. The government should assess and regulate budget transfers to state-owned enterprises to ensure their sustainability. An analysis of the implementation capacity of ministries with low expenditure execution rates could inform efforts to improve procurement systems and strengthen monitoring and evaluation. Improved data collection at the local level could help assess the efficiency of local government spending on education and healthcare. The government should adjust VAT, corporate income tax, and excise tax rates to increase revenue mobilization, and excise taxes on tobacco should be reevaluated to balance revenue and public health objectives. Strengthening taxation on wealthier households is vital to improve the equity of the tax system. Reinforcing the tax administration's auditing capacity will be necessary to boost collection efficiency and enhance distributional equity, and registration thresholds should also be adjusted to broaden the tax base. The Commitment to Equity (CEQ) methodology could be used to assess the impact of proposed fiscal policy changes on household income, poverty, and inequality.

TABLE 1 • Priority Reforms to Improve the Efficiency and Effectiveness of Fiscal Policy

Issue	Recommendation	Time Frame
Public Expenditures		
Development expenditures	• Carry out a rapid assessment of the implementation capacity of ministries with low rates of expenditure execution, especially for donor-financed development spending. • Improve public procurement planning to accelerate project implementation. • Strengthen the process for conducting mid-term reviews of budget execution and improve the execution of donor-funded development spending.	🔴
Local government spending	• Improve data collection on actual public spending by local governments.	🔴
Government spending on education and healthcare	• Assess the efficiency of public spending on education and healthcare at the local level to identify the causes of the poor performance of social spending.	🟡
Budget transfers to state-owned enterprises (SOEs)	• Assess the sustainability of recurrent and capital transfers to SOEs based on regulatory fees and standard operating costs. • Based on this assessment, adjust fees or reduce SOEs operating costs within an agreed timeframe. • Gradually eliminate budgetary transfers to commercial SOEs, or, where justified, convert such transfers to loans with specific and transparent tenures and rates. • Require regular financial reporting by all SOEs.	🟢
Tax Revenues		
Excise taxes on tobacco	• Re-evaluate excise taxes on tobacco to increase revenue and support public health objectives.	🔴
Productivity of indirect and direct taxes	• Consider adjusting the VAT, CIT, and excise tax rates to boost their productivity and mobilize additional revenue.	🟡
Equity of the tax system	• Strengthen taxation on households at the top of the income distribution to improve the tax system's equity and mobilize additional revenue.	🟡
Tax administration capacity	• Strengthen the tax administration's auditing capacity to expand collection efficiently and equitably.	🟢
Tax registration thresholds	• Broaden the tax net by realigning registration thresholds.	🟢
Distributional Impact of Fiscal Policy		
CEQ analysis	• Use the CEQ methodology to review proposed changes in taxation and public expenditure policies, including subsidies, to assess their potential impact on household income, poverty, and inequality.	🟡
VAT base	• Broaden the VAT base and use a portion of the revenue generated to increase funding for social services.	🟢
Conditional cash transfers	• Consider increasing conditional cash transfers to compensate poor households for the negative impact of an expanded VAT base or other fiscal policy changes.	🟢

Key 🔴 Short term 🟡 Short to medium term 🟢 Medium term

1 RECENT ECONOMIC DEVELOPMENTS

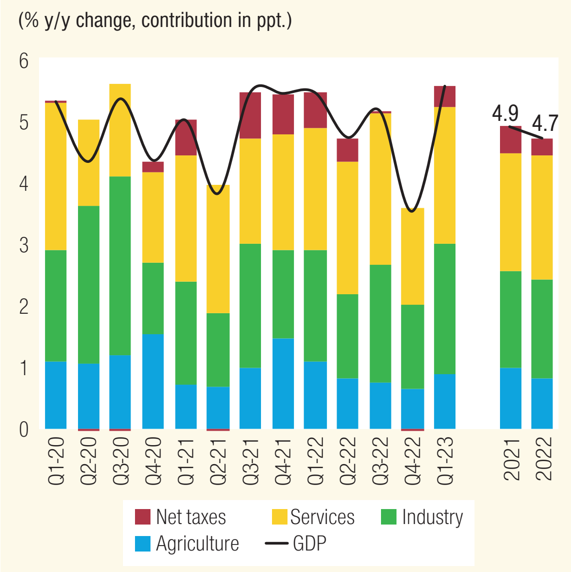
Economic Activity and Poverty Trends

Despite unfavorable global and regional developments, Tanzania's economy continues to expand at a moderate pace. During 2022, the real GDP growth rate was 4.7 percent year-on-year (y/y), slightly down from 4.9 percent in 2021. This slight deceleration reflected a modest decline in the contribution of the agricultural sector, while all other sectors broadly sustained their contributions from the previous year (Figure 1). However, growth was not constant across all subsectors, and accelerations in some compensated for slowdowns in others (Figure 2). On a sequential basis, real GDP growth bottomed out at 3.5 percent in the fourth quarter (Q4) of 2022 before rebounding to 5.6 percent, the highest y/y quarterly growth rate since 2020, in the first quarter (Q1) of 2023.

Irregular rainfall negatively affected Tanzania's major crops during 2022. According to the National Bureau of Statistics (NBS), crop production—which represents 13 percent of GDP—grew by an average of 2 percent in the second half of 2022, down from 6 percent in the second half of 2021. As a result, the overall growth of crop production slowed from 3.6 percent in 2021 to 2.7 percent in 2022. Due to the government's involvement in the production of forest products to ensure sustainable harvesting, the growth of the forestry subsector ticked down from 3.5 percent in 2021 to 3.1 percent in 2022. Meanwhile, the growth of fishery output fell from 2.6 percent to 1.9 percent. By contrast, livestock production, which accounts for about 7 percent of total output, has grown steadily at a rate of about 5 percent per year over the past two years. Consequently, the aggregate value of agricultural production declined from 3.9 percent in 2021 to 3.3 percent in 2022. In recent years, the Tanzanian authorities have taken important steps to address the country's climate-related challenges.[2] Tanzania is a major food producer in East Africa, but the increasing

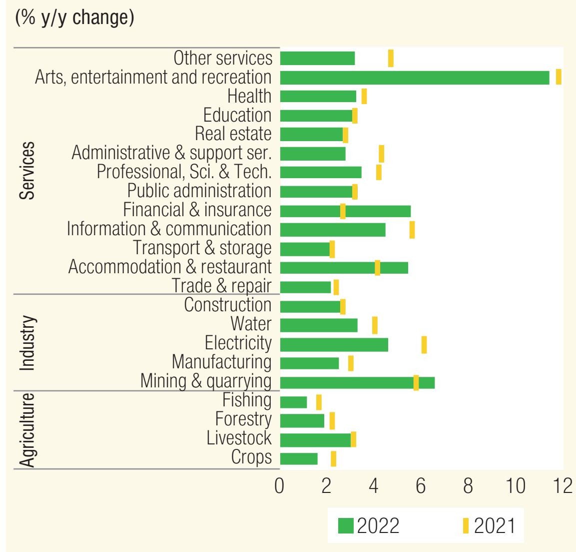
[2] This included the preparation of *National Climate Change Response Strategy 2021–26*, which entails a set of adaptation and mitigation interventions in major economic sectors. In addition, through national planning envisaged under the Third National Development Plan, authorities are prioritizing the strengthening of the systems for environmental protection and sustainable use of natural resources.

FIGURE 1 • GDP Growth



Source: NBS, WB staff estimates.

FIGURE 2 • GDP Growth by Sector



Source: NBS, WB staff estimates.
Note: Sci. refers to Science and Tech. refers to Technology.

frequency and severity of extreme weather events and other climate-related economic disruptions pose a serious threat to its agricultural sector.[3]

The growth of the industrial sector edged up from 5.4 percent in 2021 to 5.5 percent in 2022. Construction led the sector, followed by mining and manufacturing. Construction grew by 4.4 percent during the year, representing about two-fifths of the total increase in industrial output. As construction activity expanded, domestic cement manufacturing rose by 14.9 percent, with a similar increase in cement consumption during 2022. Meanwhile, the related credit offtake also surged by 25 percent. Accelerated coal production continued to drive growth in the mining sector. According to the NBS, coal output increased by almost 2.5 times between 2021 and 2022 amid shortages of crude oil and natural gas caused by Russia's war in Ukraine.[4] As a result, the mining sector's total output growth accelerated from 9.4 percent in 2021 to 10.9 percent in 2022. By contrast, the growth of manufacturing output slowed from 4.8 percent in 2021 to 4.2 percent in 2022, which was partly evident in a deceleration of the growth of manufacturing exports from 32.9 percent in 2021 to 18.3 percent in 2022.

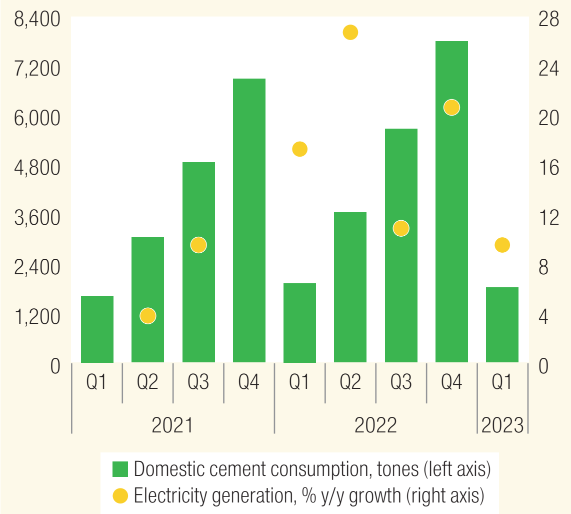
The services sector was responsible for almost half of overall GDP growth in 2022. The sector's annual growth rate rose from 5.0 percent in 2021 to 5.2 percent in 2022, driven by the strong performance of the finance and insurance, accommodation and restaurant, transportation and storage subsectors (Figure 2). Broadly, the underlying increase in transport, accommodation, and trade reflected the impact of easing travel restrictions adopted during the pandemic and normalizing domestic and international demand for trade-related services, as underscored by the rapid growth of transport and tourism during the year.[5] However, despite a sustained recovery in economic activity and rising commodity production, the growth of subsectors such as information and communication, and administrative and support services slowed between 2021 and 2022.

3 According to the IMF database, the number of flood-related climate disasters in Tanzania rose from 10 reported during 2000-10 to 21 in the last ten years.

4 According to the Ministry of Minerals, coal production increased from 0.98 million tons in 2021 to 2.5 million tons in 2022. According to the Bank of Tanzania, export of coal recorded at US$160.4 million in 2022, compared to only US$13.2 million in 2021.

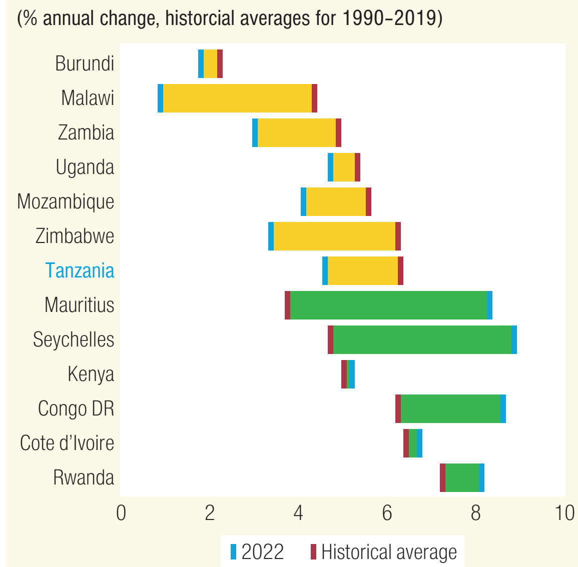
5 According to export data from Bank of Tanzania, transport-related exports grew by 20.2 percent in 2022, while travel receipts nearly doubled from the previous year.

FIGURE 3 • Cement Consumption and Electricity Generation



Source: NBS, WB staff estimates.
Note: Only positive electricity generation growth was represented in the yellow dots.

FIGURE 4 • Deviation in Growth, Historical vs. 2022



Source: WB-WDI, MPO Springs 2023, WB staff estimates.

After slowing in Q4 2022, economic activity accelerated in Q1 2023, driven by the industrial and services sectors. Real GDP rebounded to a robust 5.6 percent in Q1 2023, up from a low of 3.5 percent y/y in Q4 2022 and 5.5 percent in Q1 2022. The industrial sector's growth rate rose from 6.6 percent in Q1 2022 to 7.7 percent in Q1 2023, reflecting a 6.2 percent surge in the construction subsector and a double-digit expansion in the mining and quarrying subsector. Supported by the rapid growth of the trade and repair (+6 percent, y/y) and finance and insurance (+13 percent, y/y) subsectors, the growth rate for the services sector rose from 5.0 percent in Q1 2022 to 5.7 percent in Q1 2023.

High-frequency data confirmed the accelerating expansion. The average output index for selected industrial subsectors was higher in Q1 2023 than in Q1 2022, consistent with the growth of manufacturing. While domestic cement consumption contracted by 1 percent in Q1 2023 due to base effects, demand remained robust by historical standards, driven by the growth of related construction industries. Electricity generation increased by 9.3 percent in Q1 2023, albeit down from 17 percent in Q1 2022 (Figure 3). Meanwhile, skyrocketing tourism-related services and communications activity helped boost overall services output and net exports in Q1 2023. Since July 2022, tourism arrivals have consistently surpassed their pre-pandemic averages, rebounding by 41.4 percent in Q1 2023. Meanwhile, travel receipts rose by 51.6 percent in Q1 2023. The growth of voice-traffic minutes (a proxy for value addition in the information and communications subsector) rose to 24.3 percent in Q1 2023, up from a still-robust 22.3 percent in Q4 2022.

Although Tanzania has experienced a sustained post-pandemic recovery, the economy is still operating below its long-term potential. Between 2009 and 2019, Tanzania's annual real GDP growth rate averaged about 6.3 percent, close to the average for the previous ten years. While economic growth has accelerated in the wake of the pandemic, driven by two years of strong domestic demand, it has yet to return to its historical long-term trajectory (Figure 4). Supported by rising investment, the growth of domestic demand rose from 4.9 percent in 2021 to 6.8 percent in 2022.[6] Moreover, Tanzania's post-pandemic recovery continues to lag those of many regional peers. The deviation of the country's growth path from those of its closest comparators reflects

6 Domestic demand is defined as the sum of total consumption and investment. These estimates were prepared by World Bank staff.

the country's large infrastructure and social-spending needs, including mounting health and education costs driven by rapid population growth.[7]

Robust economic growth in the pre-pandemic era had only a modest impact on reducing poverty rates. Between 2012 and 2018, GDP per capita surged by 21 percent, yet the poverty rate fell by just two percentage points. The weak effect of economic growth on poverty reduction is due to growth being primarily focused in sectors that employ relatively few workers, especially those from poor households. Furthermore, urban areas have seen poverty rates increased from 16 percent in 2012 to 21 percent in 2018, while rural areas continued to grapple with lower welfare levels than their urban counterparts. By 2021, the economic downturn caused by the pandemic had reduced median consumption per adult equivalent by 10 percent from its 2014 level while increasing the national basic-needs poverty rate from 26 to 27 percent. In 2022, no significant change in the poverty rate is anticipated.

Looking ahead, the prospects for poverty reduction in Tanzania are modestly optimistic. The GDP growth rate is forecast to rise to 5.1 percent in 2023 and reach its long-term potential rate of 6 percent by 2025. The poverty rate is expected to gradually decline from 27 percent in 2022 to 26.5 percent in 2023, 26.3 percent in 2024, and 25.9 percent in 2025.[8] However, major threats to the macroeconomic outlook, including an unstable external environment, delays in domestic policy implementation, and the adverse effects of climate change, could derail the anticipated decline in poverty rates. Poverty-reduction policies should concentrate on investing in human capital, enhancing agricultural productivity among smallholder farmers, fostering job creation by improving the business climate, and expanding women's access to economic opportunities and productive assets.

Monetary Policy and Inflation

Driven both by global and domestic factors, headline inflation in Tanzania has risen, albeit at a slower pace than in many peer countries. Cumulatively, headline consumer price index (CPI) inflation rose from 3.7 percent in 2021 to 4.4 percent in 2022—exceeding 4 percent for the first time since 2017. Almost 40 percent of the increase in domestic inflation during 2022 can be attributed to higher food prices (Figure 5),[9] as the spike in food-price inflation caused by Russia's war in Ukraine compounded the effects of a protracted regional drought. Food makes up about 28 percent of Tanzania's consumer basket, and cumulative food-price inflation increased from 4.3 percent in 2021 to 7.3 percent in 2022. During the same period, the energy, fuel, and utilities components of headline inflation increased by 6 percentage points, from 3.1 percent in 2021 to 9.1 percent in 2022, reflecting rising global energy prices.[10]

While headline inflation accelerated, core inflation remained subdued throughout 2022. Cumulatively, the core inflation rate fell from 4.1 percent in 2021 to 3 percent in 2022.[11] Retail prices for clothing and footwear, which make up about 11 percent of the CPI basket and are a major component of core inflation, fell from 4.6 percent in 2021 to 2.5 percent in 2022. Similar trends were observed in other core prices, especially those related to services. In aggregate, services-related inflation dropped from 3.1 percent in 2021 to 2.8 percent in 2022. By contrast, goods prices increased from 4.1 percent to 5.3 percent over the period. Despite its subdued growth, core inflation accounted for half the increase in headline inflation during 2022, as core prices represent a large share of Tanzania's CPI basket.

Despite headwinds, inflation in Tanzania remained substantially lower than in many other regional economies. According to the latest IMF

7 Tanzania's population growth rate was estimated at 3 percent in 2022, versus a 2.6 percent average for East Africa and a 2.4 percent average for all of Africa. Source: United Nations World Population Prospects.

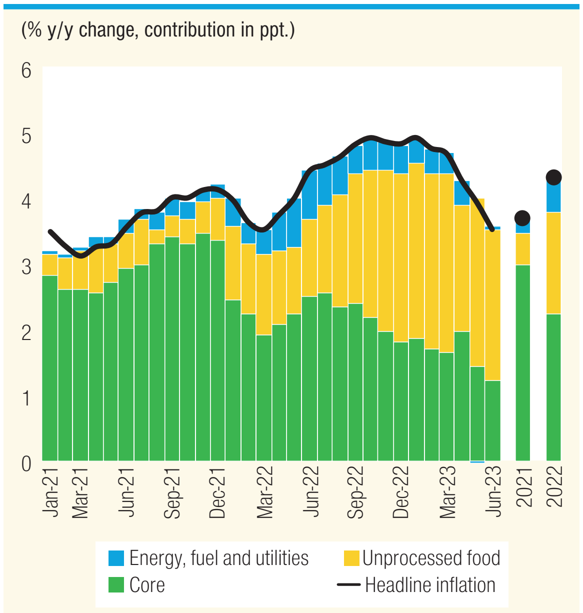
8 An upcoming comprehensive household budget survey in FY2023/24 will provide fresh data on the official poverty rates.

9 For example, as against general decline observed in 2021, domestic maize prices on average increased by 73 percent while rice prices grew by 52 percent in 2022. Similar trends were reported in other food crop prices. Source: Bank of Tanzania.

10 Domestic pump prices for petrol and diesel experienced 28 percent and 38 percent increase in 2022, respectively.

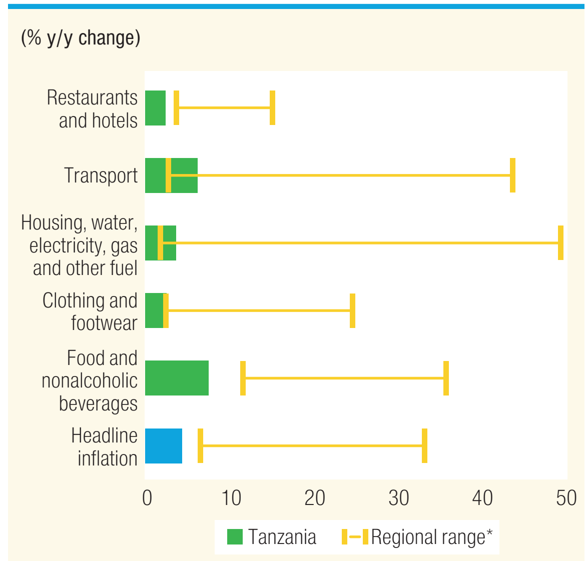
11 According to Bank of Tanzania, core inflation excludes unprocessed food, maize flour, energy, and fuel.

FIGURE 5 • Headline Inflation by Component



Source: NBS, WB staff estimates.

FIGURE 6 • Drivers of Inflation, Tanzania and Sub-Saharan Africa, 2022



Source: NBS, WB staff estimates.
* Includes Uganda, Mozambique, Kenya, Rwanda, Ghana, Cameroon, Botswana.

estimates, headline inflation rates in Sub-Saharan Africa (SSA) averaged about 14.5 percent in 2022, almost 3.3 times higher than in Tanzania.[12] Cross-country data show that all major inflation components were lower in Tanzania than in SSA during 2022. Food-price inflation, for example, ranged between 13 percent and 37 percent across the region, while reaching just 7.3 percent in Tanzania (Figure 6). Similar trends were observed for fuel-price inflation, core inflation, and other components. Policy interventions, including price subsidies for fuel and fertilizer, contributed to Tanzania's lower inflation rates.[13] In addition, the relative stability of the Tanzanian shilling vis-à-vis the US dollar contrasts with the broad depreciation observed across other regional countries (Box 2).

Inflation has slowed since the start of 2023. Driven by the core and non-core components of the CPI basket, headline CPI inflation hovered at around 4.9 percent between Oct-2022 and Jan-2023. However, following five consecutive monthly declines, the CPI inflation rate fell to 3.6 percent in Jun-2023, down almost a full percentage point from Jun-2022. Complemented by inflation-reducing policy measures, the easing of global commodity prices has helped slow the growth of domestic prices, especially for energy and transportation.[14] A year ago, energy, fuel, and utilities accounted for one-quarter of the overall increase in consumer prices, but by June these items were no longer a source of significant price pressures. Nevertheless, rising domestic food prices continue to keep overall inflation elevated (Figure 5). Cumulatively, CPI inflation rose from 3.9 percent in H1-2022 to 4.4 percent in H1-2023.

Though inflation remains well below the central bank's medium-term target of 5 percent, monetary policy remained relatively tight in early 2023. The central bank's less-accommodative stance is slowing the growth of monetary aggregates. The growth of reserve money, a key policy target, slowed from 17.3 percent at end-2021 to 15.8 percent at end-2022. Similarly, the growth rate of the extended broad money supply (M3), an intermediate target for the central

12 IMF, World Economic Outlook April 2023.

13 The FY2022/23 budget included a Tsh50,000 subsidy for each bag of fertilizer purchased by farmers, according to the agriculture minister. Media reports and the FY2023/24 budget speech also indicate that the government provided a Tsh100 billion monthly fuel subsidy.

14 According to the World Bank Commodity Price Database, global energy, food, and raw material price indexes fell by 30 percent, 10.5 percent, and 12 percent, respectively, y/y in H1-2023.

BOX 2: RECENT INFLATION IN TANZANIA VS. REGIONAL COUNTRIES: SOME OBSERVATIONS

Since the end of the acute phase of the pandemic, countries in SSA have faced significant economic challenges due to unprecedented spike in inflation, which has been exacerbated by Russia's war in Ukraine and its disruptive effects on global prices. To address inflationary pressures, central banks across the region have tightened their monetary policies (Table B2). However, Tanzania's policy rate remained unchanged in 2022—due in part to the absence of an interest-rate-targeting monetary regime—while the growth of the money supply slowed to a lesser extent than in many other SSA countries. Nevertheless, inflation in Tanzania was significantly lower than in many peer countries in 2022 (Table B2.A).

One of the driving factors behind Tanzania's lower inflation rates may be the economy's post-pandemic output gap, which likely contributed to the subdued trend in core inflation. Exchange-rate stability is another important factor, as the Tanzanian shilling has remained broadly unchanged against the US dollar since 2020 (Figure B2.B). In contrast to the depreciations observed among many regional currencies, exchange-rate stability has helped moderate prices in Tanzania and kept inflation within its target range. A vector autoregressive (VAR) analysis reveals that a 1 percentage-point appreciation in the nominal exchange rate leads to a 0.19 percentage-point decrease in inflation in Tanzania over a two-year period (Figure B2.C). The effect of exchange-rate stability is much more pronounced than the effect of the output gap.

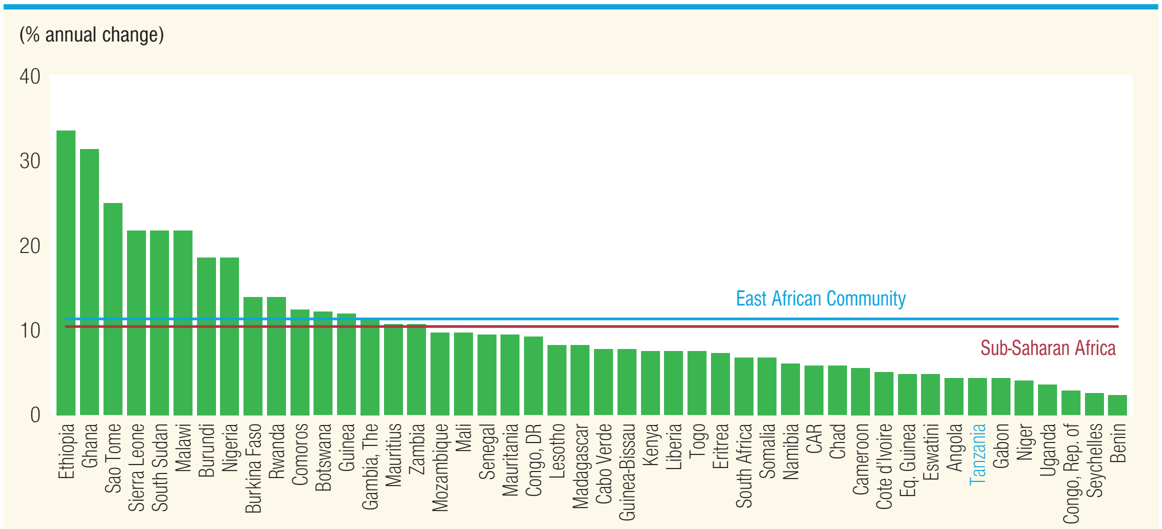
However, in the absence of further reforms, an extended period of exchange-rate stability may have adverse implications for the Tanzanian economy. For example, the lack of significant depreciation could erode the economy's external competitiveness, weakening its external account position and putting additional pressure on foreign-exchange reserves. Tanzania's import-dependent economy is especially vulnerable to this risk.

TABLE B2.A • Changes in Monetary Policy Instruments, Selected SSA Countries *(cumulative changes during 2022)*

	AGO	BWA	CMR	GHA	KEN	LSO	MUS	MOZ	NAM	NGA	RWA	ZAF	TZA	UGA
Policy rate hike	−50	100	100	1250	175	325	265	400	300	500	200	235	0	350
y/y Δ in Money supply	−11.7	−4.8	6.0	6.1	−0.8	−13.3	−20.1	−4.8	1.7	−5.0	3.4	−2.3	−3.5	−1.6

Source: Haver Analytics, WB staff estimates.
Note: Policy rate change is presented in basis points; for money supply, y/y change is in percentage points and denote cumulative delta on y/y growth at end of both 2021 and 2022.

FIGURE B2.A • Headline Inflation Rates, Sub-Sahara Africa, 2022

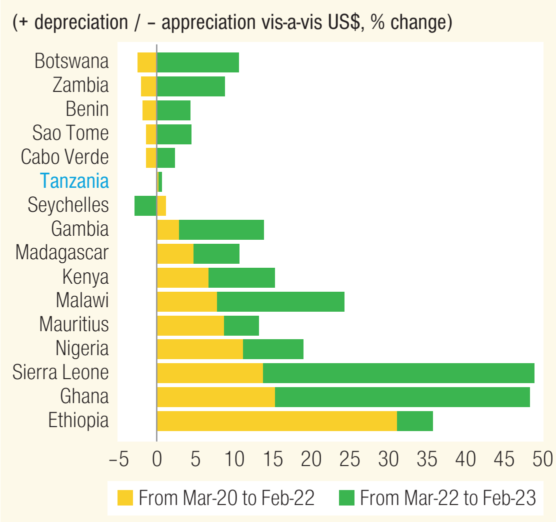


Source: MPO Springs 2023, WB staff estimates.
Note: Simple average after excldung Sudan and Zimbabwe where annual inflation reached to 164 percent and 193 percent in 2022, respectively.

(continued on next page)

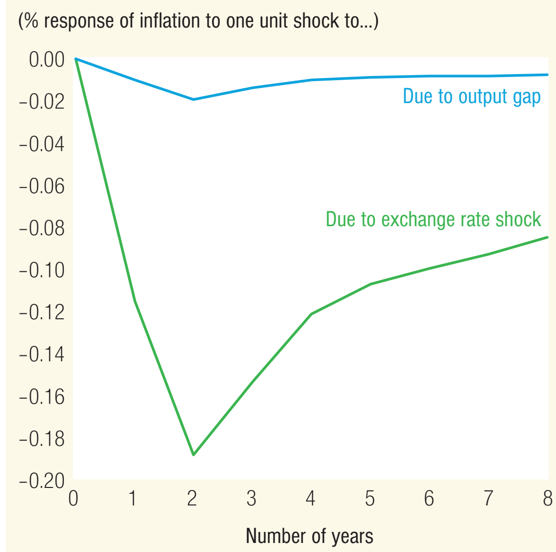
BOX 2: RECENT INFLATION IN TANZANIA VS. REGIONAL COUNTRIES: SOME OBSERVATIONS *(continued)*

FIGURE B2.B • Nominal Exchange-Rate Depreciation



Source: Bloomberg, WB staff estimates.

FIGURE B2.C • Drivers of Inflation in Tanzania



Source: WB staff estimates.

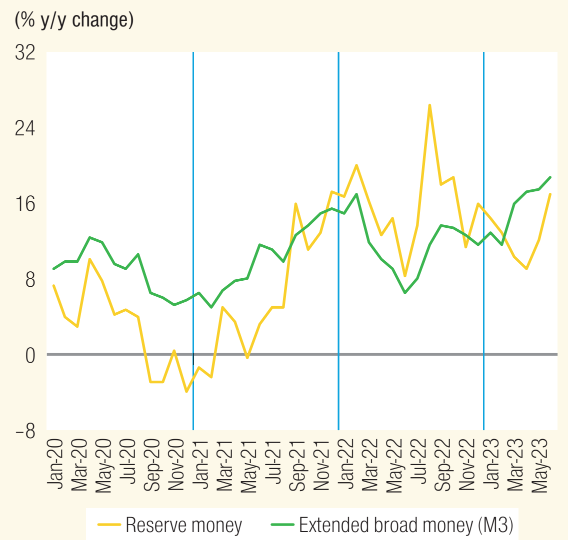
bank, declined from 15.5 percent at end-2021 to 11.6 percent at end-2022. Combined with other policy interventions, the slowing growth of monetary aggregates kept domestic inflation below the central bank's target. Interestingly, these downward trends continued into the early months of 2023 before abruptly reversed, with the growth of reserve money and M3 accelerating to 16.9 and 18.8 percent, respectively, in June, primarily driven by the rapid expansion of net domestic assets (Figure 7).

Trends in monetary aggregates indicate that external pressures remain elevated, as liquidity has primarily come from domestic sources. After expanding by 30.2 percent in 2021, the net foreign assets (NFA) of the banking system contracted by 32.4 percent in 2022. While this decline was mainly led by a decrease in NFA held by the central bank, NFA held by commercial banks also experienced a sharp decline. Together, these developments reflected the widening current-account deficit (CAD), low levels of official inflows amid debt amortization, and the central bank's interventions to partially support the balance of payments needs, which may have reduced foreign reserves. Unlike NFA, the net domestic assets (NDA) of the banking sector expanded by 41.5 percent in 2022, building on a 7.3 percent increase in 2021. Despite its relatively modest contribution to overall NDA, net credit to the central government increased substantially in 2022, driven both by lending from the central bank and from commercial banks, further highlighting the low level of official external inflows. Meanwhile, credit to subnational governments increased by 22.5 percent, accounting for about three-fifths of the total increase in the banking system's NDA during 2022.

In mid-2023, the decline in NFA slowed while NDA kept increasing. NFA fell by 7.4 percent in June, modest compared to the 12.4 percent contraction observed in June 2022 and the 32.4 percent decline at end-2022. This trend was driven by an increase in central bank reserves, while NFA held by commercial banks continued to shrink. By contrast, NDA grew by almost 30 percent in Jun-2023, up sharply from 18 percent in Jun-2022. The growth of net credit to the government and private-sector credit contributed 30 and 70 percent, respectively, to the overall increase in NDA.

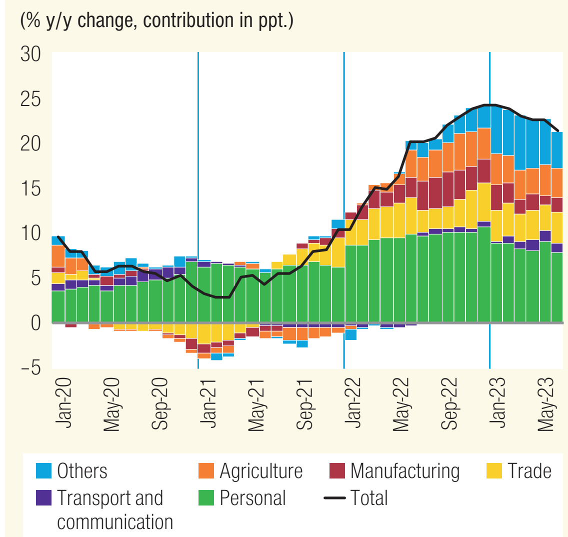
Despite the moderating growth of monetary aggregates, credit to the private sector exhibited a broad-based expansion. The growth of private credit

FIGURE 7 • Monetary Aggregates



Source: Bank of Tanzania, WB staff estimates.

FIGURE 8 • Growth in Private Credit and Its Drivers



Source: Bank of Tanzania, WB staff estimates.

accelerated from 10 percent in Dec-2021 to 22.5 percent in Dec-2022. This trend continued into 2023, and in May the growth of credit to the private sector remained at 22.5 percent, up from 16.2 percent in May-2022 (Figure 8). An analysis of sector-level data shows that personal loans, which constitute approximately 38 percent of total private loans, drove the growth of private credit, followed by loans to the trade, agriculture, and manufacturing sectors. The banking system supported the expansion of credit: deposits increased by 11 percent in 2022, and the loan-to-deposit ratio was about 80 percent. Deposits continued to grow at a robust rate of about 16 percent in H1-2023. After a modest decline of about 35 basis points over the previous 18 months, retail lending rates stabilized at about 16 percent in June 2023, encouraging further credit growth. Together, these factors boosted the domestic credit-to-GDP ratio from a recent average of 12-13 percent to 17 percent in 2022. However, while credit growth bolstered the economic recovery, it also exerted pressure on the external account amid unfavorable global conditions.

Fiscal and Debt Developments

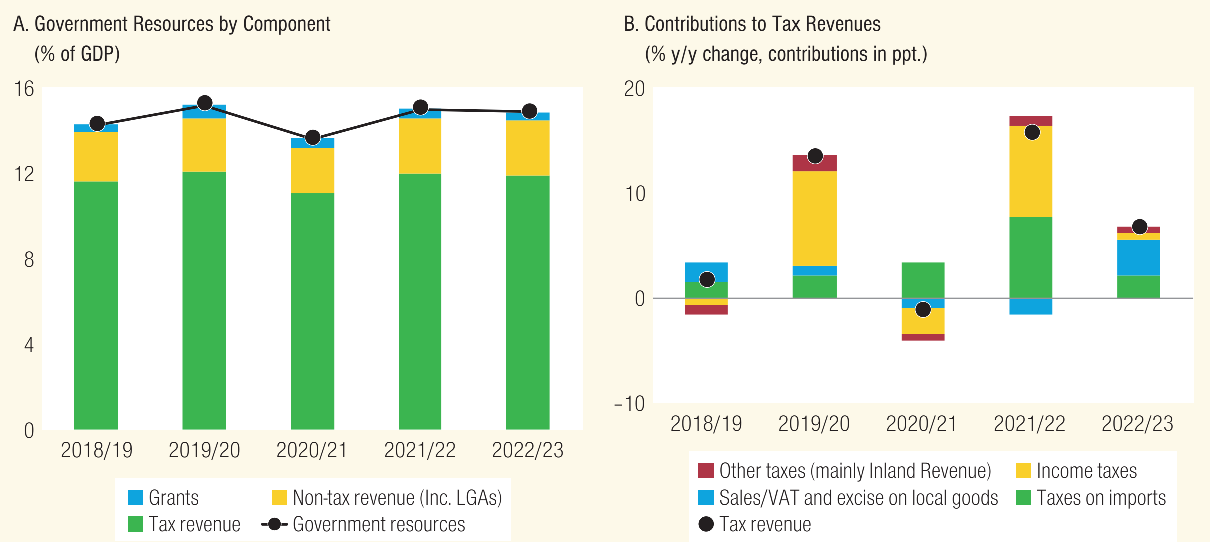
Tanzania's overall deficit, including grants,[15] widened from 3.6 percent of GDP in FY2021/22 to 4.4 percent in FY2022/23. Despite broadly stable revenue collection and the containment of overall expenditures, the use of cash and other items increased by 1.0 percent of GDP, widening the deficit.

Total government resources stood at 14.8 percent of GDP in FY2022/23, almost the same level as the prior fiscal year but 1.1 percent lower than anticipated. Representing 80 percent of total government resources (Figure 9A), tax revenue dropped slightly from 11.9 percent of GDP in FY2021/22 to 11.8 percent in FY2022/23. The government has implemented structural fiscal reforms and new tax measures over the past fiscal year,[16] but the downtick in tax-revenue collection relative to GDP suggests that those reforms have yet to yield significant results. Value-added tax (VAT) and import taxes drove revenue growth, contributing more than one-half

15 The deficit is calculated on a cash basis based on data released by BoT – Quarterly Economic Bulletin (Dec-2022). Please see https://www.bot.go.tz/Publications/Filter/2 for more information. FY GDP is World Bank staff estimates, which have been recalculated on a quarterly basis and adjusted for seasonal factors.

16 Tanzania has taken various actions to increase its revenue and fiscal space. Some of key measures include (a) expanding the tax base through electronic payments, (b) managing and reducing tax exemptions, and (c) bringing the digital economy into the tax system. Source: United Republic of Tanzania, Country Report No. 23/153, April 2023, International Monetary Fund.

FIGURE 9 • Revenues of the Central Government of Tanzania, FY



Source: Ministry of Finance and Planning, WB staff calculations.

and one-third of the overall increase in tax revenue, respectively (Figure 9B). VAT collection increased from 2.0 percent of GDP in FY2021/22 to 2.3 percent in FY2022/23, while import taxes remained broadly unchanged at about 4.6 percent of GDP. Income tax revenue fell from 4.5 to 4.2 percent of GDP over the period, partly reflecting the slowing growth of household income[17] and a decline in tax receipts from private corporations.[18] Meanwhile, nontax revenue and total grants (largely project grants[19]) remained stable at 2.6 and 0.4 percent of GDP, respectively. However, driven by lower-than-expected revenue from parastatal dividends & contributions, ministries, and regions, nontax revenue fell 0.7 percentage points short of its budgetary target.

While the government's revenue-to-GDP ratio nearly approaches a historic high, the tax-revenue-to-GDP ratio remains low by international standards and close to the average for low-income countries (LICs).[20] Measures that boost revenue collection efficiently and effectively can help Tanzania recover from the effects of the COVID-19 pandemic while advancing its goal of becoming an upper-middle-income country with well-developed human capital, an ample supply of high-quality livelihood opportunities, and sustainable, broad-based gains in living standards. Over the medium term, increased public spending will be necessary to ensure inclusive and sustainable growth, further underscoring the importance of revenue mobilization. The special focus section of this edition of the Tanzania Economic Update, "*The Efficiency and Effectiveness of Fiscal*

17 The National Panel Survey 2020–2021 – Wave 5 reports that in 2020/21 compared to 2014/15, individuals with access to one- or two-income sources decreased by 0.4 and 2.1 percentage points, respectively. Moreover, only the proportion of wage employees increased significantly by 1.4 percentage points over the period while the proportion of those whose income is sourced from other activities, such as agriculture, decreased by 1.7 percentage points. This may indicate weakened ability of individuals to mitigate economic shocks while keeping the same spending patterns. For more information, please see https://www.nbs.go.tz/nbs/takwimu/nps/wave5/NPS_Wave_5.pdf.

18 Revenue estimates report for FY2023/24 published by MoFP revealed that taxes from private financial and non-financial corporations declined by 23 percent (y/y) from Tsh108.8 billion in FY2021/22 to Tsh82.5 billion in FY2022/23.

19 While capital grants are channeled to various general government units, Tanzania National Road Agency, Road Fund Board, and Tanzania Railway Corporation account for the majority.

20 Tanzania's tax-to-GDP ratio has remained at about 11–12 percent of GDP over the last two decades, close to the average for low-income countries, according to the World Bank World Development Indicators.

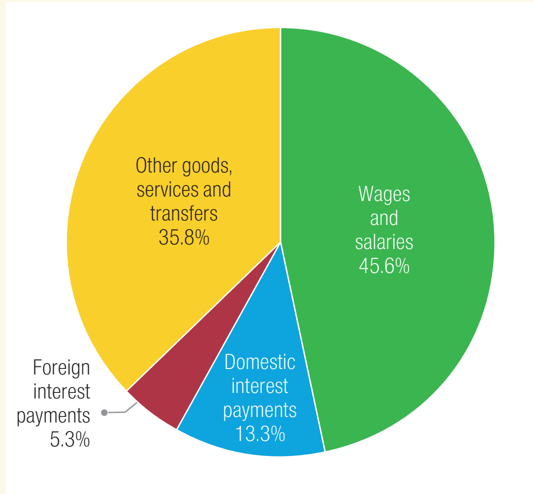
Policy in Tanzania" offers further details on revenue and spending dynamics.

Tanzania's government has achieved significant progress in containing expenditures, as total public spending[21] fell from 18.5 percent of GDP in FY2021/22 to 18.2 percent in FY2022/23, well below the budgetary target of 19.4 percent. Recurrent spending rose to 10.9 percent of GDP from about 9.5 percent over the three previous fiscal years. The increase reflected higher spending across all categories, led by other goods, services, and transfers, which represent 36 percent of recurrent spending and rose by almost a full percentage point to 3.9 percent of GDP. Wages and salaries, which represent nearly half of recurrent spending, experienced the second largest increase, rising to 5 percent of GDP as interest payments reached 1.7 percent of GDP. Domestic debt represented just one-third of the total public debt stock, but due to the highly concessional nature of Tanzania's external borrowing, domestic debt service accounted for more than two-thirds of total debt service (Figure 10). Development spending,[22] much of which remains focused on megaprojects,[23] fell from 9.0 to 7.3 percent of GDP during the period. Notwithstanding reduced capital investment recently, the Central Government's persistent and ambitious infrastructure investment plan has already resulted in a backlog of expenditure arrears (Box 3). Meanwhile, the government has recently begun to increase priority social spending,[24] which will be vital to close the human capital gap.[25] Priority social spending—which comprises recurrent and development spending on education, health, water, and rural roads, including transfers to local governments—rose from 6.4 percent of GDP in FY2021/22 to about 6.7 percent in FY2022/23.[26]

Domestic resources played a larger role in financing Tanzania's overall fiscal deficit during FY2022/23. Domestic borrowing, mainly from bank and non-bank sources, covered almost 60 percent of the fiscal deficit. Net foreign financing amounted to 1.9 percent of GDP, with one-third coming from program loans and the remaining two-thirds from development project loans. This pattern differs from that of the two previous fiscal years, when the overall fiscal balance was financed almost equally by foreign and domestic sources.

On June 15, Budget FY2023/24 was submitted to the Parliament. It envisions a consolidation effort

FIGURE 10 • Breakdown of Recurrent Expenditures, FY2022/23



Source: Ministry of Finance and Planning, WB staff calculations.

to bring the fiscal deficit (including grants) of the CG to below 3 percent of GDP (Box 4). This will be achieved through a combination of revenue enhancing and expenditure curtailing measures. Interestingly, weight of consolidation appears to be titled more towards the development spending while making the attempt to safeguard the recurrent side—which is a positive development.

Tanzania's public debt-to-GDP ratio has risen, but its risk of debt distress remains moderate.[27] The public and publicly guaranteed (PPG) debt

21 The total expenditure and development expenditure mentioned throughout the report include net lending.

22 Ibid.

23 For instance, Julius Nyerere Hydropower Project in the energy sector and the Standard Gauge Railway project in the infrastructure sector.

24 According to IMF EFF program for Tanzania, priority social spending needs to remain at about 6.7 percent of GDP.

25 According to World Bank's Human Capital Index (HCI, 2020), a child born in Tanzania in 2020 would only fulfill almost 39 percent of her full potential productivity had she enjoyed a complete education and full health, just below the SSA-average of 40 percent. For details, see https://databankfiles.worldbank.org/public/ddpext_download/hci/HCI_2pager_TZA.pdf.

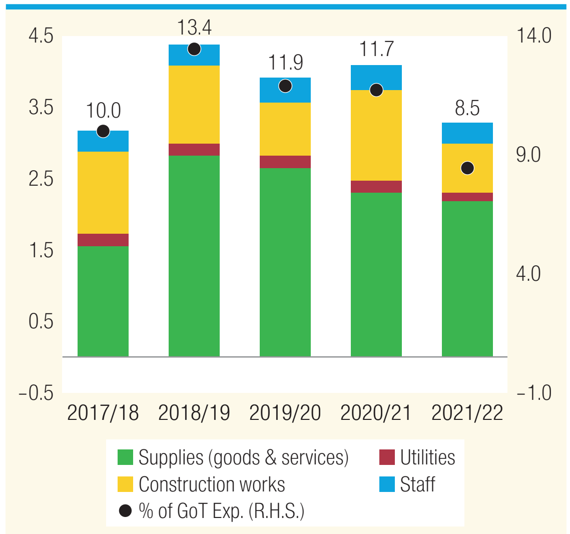
26 United Republic of Tanzania, Country Report No. 23/153, April 2023, International Monetary Fund.

27 The public sector debt includes central government debt, central government-guaranteed debt (except for guaranteed debt of SOEs and local governments) and central bank.

BOX 3: GOVERNMENT EXPENDITURE ARREARS: CURRENT STATUS AND REVISED ARREARS MANAGEMENT STRATEGY (2022)

The central government has long struggled with public financial management (PFM) issues, which have contributed to the accumulation of large expenditure arrears.[a] The World Bank's 2010, 2013, 2017 and 2022 Public Expenditure and Financial Accountability (PEFA) assessments all highlighted challenges with PFM, as have multiple IMF country reports. The stock of expenditure arrears declined marginally from Tsh4.1 trillion or 11.7 percent of total government expenditures at the end of FY2020/21 to Tsh3.2 trillion or 8.5 percent of government expenditures at the end of FY2021/22. Most arrears are owed to suppliers and contractors (Figure B3.A).

FIGURE B3.A • Trends in Central Government Expenditure Arrears (*Tsh trillions (LHS), % share (RHS)*)



Source: WB staff estimates.

Expenditure arrears are largely unverified and longstanding, and contractual arrears are prioritized for repayment. More than two-thirds of the arrears stock at end-FY2021/22 has yet to be verified, while over 55 percent of outstanding expenditure arrears were overdue for more than a year, and half of those were more than two years overdue by the end of FY2020/21. While most arrears are owed to suppliers, the government prioritized clearing contractual arears in FY2021/22. During this fiscal year, almost Tsh1.1 trillion was spent clearing contractual arrears, representing nearly half of all repayments.

The backlog of expenditure arrears reflects Tanzania's infrastructure investment ambitions and weak commitment controls. The recent simultaneous development of multiple megaprojects[b] contributed to the accumulation of arrears. Moreover, the cash-rationing government payment system, MUSE, only allows repayments for expenditure entries occurring in the same month or those below the monthly payment ceilings, whereas a more flexible system of cash planning and commitment control could help prevent the accumulation of arrears.

With support from the World Bank, Tanzania has revised its 2022 Arrears Management Strategy to establish expenditure controls and prevent the further accumulation of arrears. The government has already made efforts to speed up the tracking of arrears verification and to reduce the arrears stock as a share of government spending.[c] However, Tanzania's large arrears stock inhibits the government's ability to convey liquidity, predictability, and confidence to the private sector. The government plans to clear Tsh0.43 trillion in arrears in FY2022/23 and another Tsh0.6 trillion every year over the next three years. The government is also working to prepare properly costed budget baselines and realistic revenue projections and has amended the definition of arrears as unpaid claims over 30 days delinquent for goods and services and over 90 days delinquent for construction work.[d]

[a] Government expenditure arrears are financial obligations that the government has incurred through its operations that remain unpaid beyond the financial year of occurrence. Specifically, they are defined as outstanding claims ageing over 30 days for delivery of goods and services and ageing over 90 days for construction works in Tanzania.
[b] As Tanzania implemented her third National Five-Year Development Plan (FYDP III, 2021/22 – 2025/2026), the government has focused on improving productive infrastructures like roads, railways, ports, water, air transports, and electricity access. Source: United Republic of Tanzania, National Five-Year Development Plan, 2021/22 – 2025/26, June 2021, Ministry of Finance and Planning..
[c] Noticeably, the share of verified arrears out of total claimed arrears tripled from 10.7 percent in FY2020/21 to almost 33 percent in FY2021/22. Meanwhile, the arrears stock, as a percent of government expenditure, declined from its four-year-average (FY2017/18-FY2020/21) of 12 percent to 8.5 percent in FY2021/22.
[d] United Republic of Tanzania, Country Report No. 23/153, International Monetary Fund, April 2023.

stock increased from 41.3 percent of GDP at end-FY2020/21 to 43.8 percent at end-FY2021/22, largely due to the government's efforts to strengthen the balance sheets of state-owned enterprises (SOEs).[28] However, the public debt-to-GDP ratio remains well anchored[29] and relatively modest by the standards of neighboring countries.[30] At end-FY2021/22, almost 64 percent of public debt was held externally, while the remaining 36 percent was domestic debt (Figure 11). The latest joint IMF-World Bank Debt Sus-

[28] Government converted about Tsh 4.8 trillion (2.8 percent of GDP) on-lent debt of National Insurance Company to equity to strengthen its balance sheet. Source: United Republic of Tanzania, Country Report No. 23/153, International Monetary Fund, April 2023.

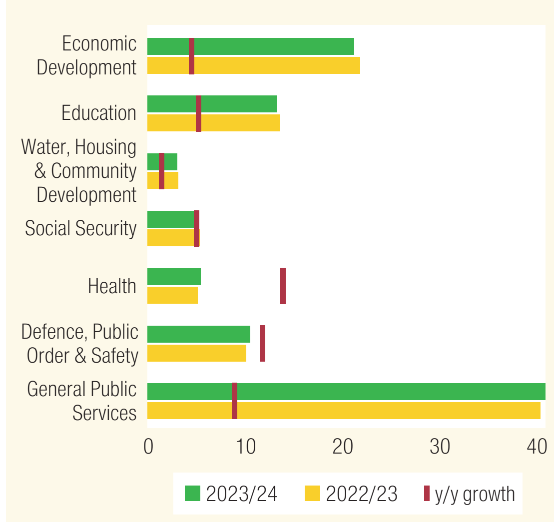
[29] While the calculated composite indicator index (a measurement to assess country's debt-carrying capacity) dropped down from 2.94 in August-2022 DSA to 2.92 in the recent DSA, it is remained within the range of the medium level (2.69 ~ 3.05).

[30] The latest IMF Global Debt Database (2022) reported that Tanzania's neighboring countries have a higher

BOX 4: PRELIMINARY BUDGET ANALYSIS FOR FY2023/24

On 15 June 2023, Hon. Dr. Mwigulu Nchemba, then Minister for Finance and Planning, presented the budget speech for FY2023/24, themed '*Accelerating Economic Recovery, Climate Change Adaption & Mitigation, and Enhancing Productive Sectors for Improved Livehood*'. This is the second budget under the sixth phase government led by President Samia Suluhu Hassan. It comes at a critical time when the government continues to implement ongoing mega projects, safeguard the government debt sustainability, manage arrears payment, and promote democracy and economic diplomacy while facing external headwinds and domestic climate change threats.

FIGURE B4.A • Sector Budget Allocations *(% share, % y/y growth)*



Source: Ministry of Finance and Planning and World Bank staff estimates.

FY2023/24 Budget has five priority focus areas that are aligned with the third and final Five-Year National Development Plan (FY2021/22–FY2025/26). These priority areas are aimed to build a competitive and industrial economy for human development. Specifically, the government intends to take solid steps in five areas: (i) realize a competitive and inclusive economy through regulating the financial sector, empowering the agriculture sector, improving key productive infrastructures, and transiting to a digital economy; (ii) deepen industrialization and service provision, including but not limited to stimulate mining sector and implement electricity distribution projects; (iii) promote investment and international trade, especially in improving business environment and fostering public-private partnerships; (iv) enhance social services in health, water, law and landing sectors; and (v) develop human capital to improve necessary skills for employment creation. These measurements are intended to sustain growth momentum and enhance the economy's resilience in line with the developing agenda.

According to FY2023/24 Budget, the government set six macroeconomic policy targets for FY2023/24,[a] particularly with a focus on fiscal consolidation through cutting unnecessary expenditures. In FY2023/24, the government is anticipated to collect domestic revenue, at 14.9 percent of GDP, the same as the previous year's budget target. However, supported by less spending on the development projects, the total expenditure is expected to be nearly one percentage points lower than the FY2022/23 budget, reaching 21.1 percent of GDP. The revenues mobilization enhancement and the expenditures curtailment would help the government achieve a target of fiscal deficit lower than 3 percent of GDP. Meanwhile, the government will continue prioritizing the concessional loans in FY2023/24, ensuring the government debt sustainability.

As noted in the speech, the distribution of the Tsh44.4 trillion total expenditure in FY2023/24 will be unevenly across sectors, with a focus on Health, Defence, Public Order & Safety, and Agriculture. The Health sector, representing 13.4 percent of the total budget, enjoyed the most significant budgetary increase of 11.3 percent. This is followed by the Defence, Public Order & Safety sector which enjoyed a 40 percent share in the budget allocation and grew by over 11 percent against last year's allocation (Figure B3.A). Although the budget allocated to the Economic Development sector exhibited a modest growth of 4 percent in FY2023/24, detailed data suggest a robust budget allocation increase in the Agriculture and Industry & Trade subsectors, with growth rate of 20.5 percent and 14.6 percent, respectively.

[a] These targets are (i) achieve a 5.2 percent real GDP growth in 2023; (ii) contain inflation with a single-digit range between 3 and 7 percent in the medium term; (iii) tax revenue is estimated to reach 12 percent of GDP; (iv) domestic revenue is estimated to reach 14.9 percent of GDP; (v) the budget deficit (incl. grants) is narrowed to below 3 percent of GDP for FY2023/24; (vi) maintain adequate foreign reserves to cover at least four months of goods and services imports.

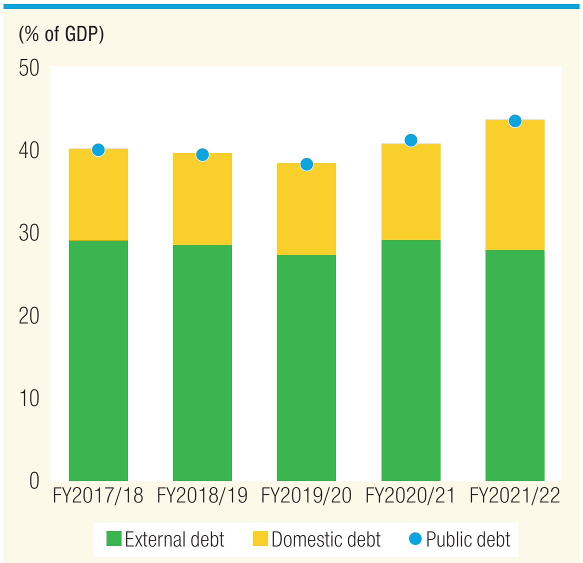
tainability Analysis (DSA)[31] assessed Tanzania's risk of overall public and external debt distress as moderate, unchanged from the previous analysis. The DSA results underscore the importance of safeguarding debt sustainability by maximizing concessional financing, increasing revenue mobilization, and strengthening public investment management by selecting only those investment projects with clear socioeconomic benefits.

The external PPG debt stock declined to 27.9 percent of GDP at end-FY2021/22, down almost 1.3 percentage points of GDP from the previous year. Multilateral loans fell from 18.1 percent of GDP to 17 percent and accounted for three-fifths of all exter-

debt-to-GDP ratio than Tanzania in 2021. For instance, Kenya's government debt is 68 percent of GDP, Uganda's is 52 percent, Rwanda's is 67 percent. Please see https://www.imf.org/external/datamapper/CG_DEBT_GDP@GDD/CHN/FRA/DEU/ITA/JPN/GBR/USA for more details.

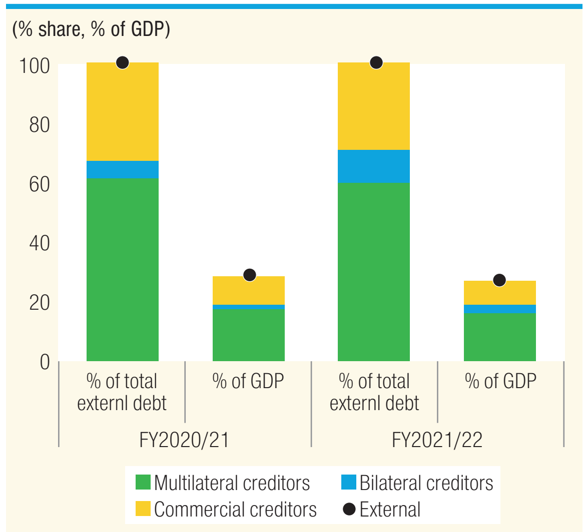
31 United Republic of Tanzania, Country Report No. 23/153, International Monetary Fund, April 2023.

FIGURE 11 • Tanzania's Public Debt



Source: DSA(April-2023), WB staff estimates.

FIGURE 12 • Concessional External Debt by Component



Source: DSA(April-2023), WB staff estimates.

TABLE 2 • Central Government Fiscal Operations, % of GDP

	Fiscal year (July to June)				
	2019/20 Actual	2020/21 Actual	2021/22 Actual	2022/23 Actual	2022/23 Budget
Total Revenue	**14.5**	**13.1**	**14.5**	**14.4**	**15.4**
Tax revenue	**12.0**	**11.0**	**11.9**	**11.8**	**12.2**
Taxes on imports	4.1	4.2	4.7	4.6	4.7
Sales/VAT and excise on local goods	2.6	2.4	2.0	2.3	2.4
Income taxes	4.5	3.8	4.5	4.2	4.3
Other taxes (mainly Inland Revenue)	0.8	0.7	0.7	0.8	0.8
Non-tax revenue (incl. LGAs)	**2.5**	**2.1**	**2.6**	**2.6**	**3.3**
Grants	**0.6**	**0.4**	**0.4**	**0.4**	**0.5**
Total expenditure and net lending	**16.6**	**16.9**	**18.5**	**18.2**	**19.4**
Recurrent expenditure	**9.8**	**9.5**	**9.5**	**10.9**	**11.2**
Wages and salaries	4.8	4.7	4.8	5.0	5.4
Interest payments	1.6	1.6	1.7	2.0	1.6
Domestic	1.0	1.2	1.2	1.5	1.0
Foreign	0.6	0.5	0.5	0.6	0.6
Other goods, services and transfers	3.4	3.2	3.0	3.9	4.2
Development expenditure and net lending	**6.8**	**7.4**	**9.0**	**7.3**	**8.3**
Overall balance after grants	**−1.5**	**−3.4**	**−3.6**	**−3.4**	**−3.5**
Adjustments to cash and other items (net)	**−0.4**	**−0.5**	**0.0**	**−1.0**	**0.0**
Overall balance (cash basis)	**−1.9**	**−3.8**	**−3.6**	**−4.4**	**−3.5**
Financing	**1.9**	**3.8**	**3.6**	**4.4**	**3.5**
Foreign financing (net)	1.6	1.7	1.9	1.9	2.1
Domestic (net)	0.3	2.1	1.7	2.5	1.4

Source: Ministry of Finance and Planning and Bank of Tanzania.
Note: Calendar year GDP for FY2018/19 onwards is based on World Bank staff estimates which is converted to quarterly GDP using seasonal factors, from which fiscal year GDP is estimated.

nal borrowing during FY2021/22. Commercial loans declined from 9.3 to 7.9 percent of GDP (28 percent of external borrowing) over the period, while bilateral loans rose from 1.9 to 3.0 percent of GDP (Figure 12). Multilateral and bilateral lending constituted almost 72 percent of external borrowing.[32] The World Bank remained Tanzania's top creditor, accounting for almost 42 percent in total external borrowing. Credit Suisse AG and Exim Bank China were the country's leading commercial creditors, each accounting for one-fourth of commercial loans.

Tanzania's domestic debt stock increased from 12.1 percent of GDP at end-FY2020/21 to 15.9 percent at end-FY2021/22.[33] Bonds and other long-tenor instruments[34] made up almost 74 percent of total domestic borrowing. The share of bonds rose from 9.2 percent of GDP to 11.7 percent over the period,[35] while share of domestic debt held as T-bills remained small at under 7 percent. Domestic arrears, which were previously classified as part of overall contingent liabilities, stood at 1.8 percent of GDP during FY2021/22. Commercial banks, pension funds, and the central bank remained the main domestic creditors, together holding almost 80 percent of the government's domestic debt.[36]

In FY2021/22, debt service on PPG debt remained unchanged from the previous year at 5.1 percent of GDP. While almost two-thirds of PPG debt is external, external debt service accounted for a smaller share of total debt service.[37] External debt service at end-FY2020/21 amounted to 2.1 percent of GDP, up slightly from the previous year, while domestic debt service remained stable at 3.0 percent of GDP.

Balance-of-Payments Position

An uncertain global economic environment continued to place significant pressure on Tanzania's external sector in 2022. In particular, rising food and energy prices and other spillovers from Russia's war in Ukraine pushed the country's current-account deficit (CAD) to its highest level since 2014. The CAD widened from US$2.37 billion (or 3.4 percent of GDP[38]) in 2021 to US$5.40 billion (or 7.1 percent of GDP) in 2022. The external trade deficit for merchandise accounted for almost the entire deterioration in the CAD during 2022 (Figure 13). While the increase in the trade deficit is partly explained by Tanzania's sustained post-pandemic recovery, a significant share was also driven by the economy's weakening terms-of-trade position.[39]

Goods exports grew modestly during 2022, supported by nontraditional items. Favorable prices helped Tanzania's goods exports grow by a cumulative 6.8 percent during 2022, up from 5.4 percent in 2021.[40] Nontraditional items like minerals and manufactured goods accounted for about 70 percent of the increase in merchandise exports. The growth of mineral exports was driven by the surge in global demand for coal, as Russia's war in Ukraine disrupted global oil and gas supplies. As a result, the value of Tanzania's coal exports shot from US$13.2 million in 2021 to US$160.4 million in 2022. Demand for gold—which accounts for

32 This reflects that the external debt portfolio is on favorable financing terms.

33 This is consistent with one of the debt management objectives: support the development of domestic debt market. Source: United Republic of Tanzania, Medium Term Debt Management Strategy, December 2022, Ministry of Finance and Planning.

34 This aligns with the government's strategy of borrowing from medium to long-term instruments to minimize the risk of refinancing and cost of financing while catering to the market's needs. Source: United Republic of Tanzania, Medium Term Debt Management Strategy, December 2022, Ministry of Finance and Planning.

35 In December 2021 (the middle of FY2021/22), the MoFP issued a non-cash bond worth Tsh 2.2 trillion (about 1.3 percent of GDP) to settle arrears to the Public Service Social Security Fund. Source: United Republic of Tanzania, Country Report No. 22/269, August 2022, International Monetary Fund.

36 Source: Monthly Economic Review, Jan 2023, Bank of Tanzania.

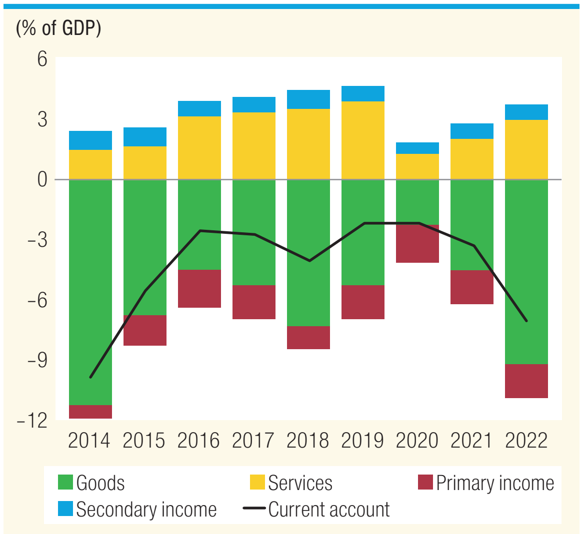
37 This reflects Tanzania's favorable debt structure—as majority of external debt is concessional.

38 The GDP figures used in this section were estimated by WB staff.

39 According to the National Bureau of Statistics, Tanzania's terms-of-trade for goods decreased by 3.1 percent in 2022, while the IMF's Commodity Terms of Trade database estimates the decline at 6.4 percent.

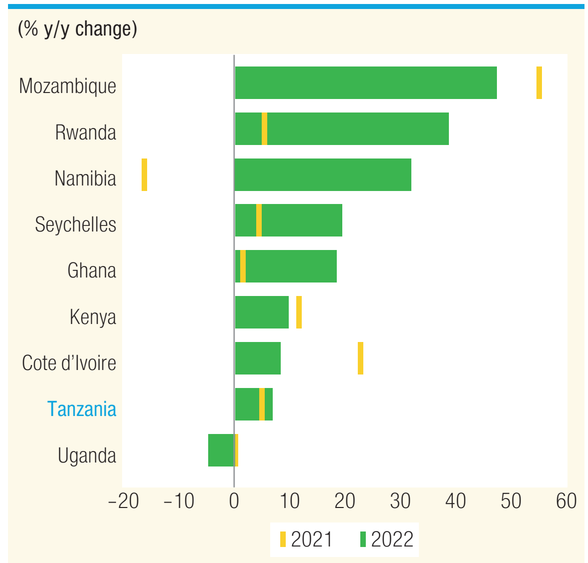
40 In 2022, according to NBS, goods export price index grew by 5.9 percent, and exports increased by 6.8 percent in value terms.

FIGURE 13 • The Current-Account Balance and its Drivers



Source: Bank of Tanzania, WB staff estimates.

FIGURE 14 • The Growth of Goods Exports



Source: Haver Analytics, WB staff estimates.

about two-fifths of the country's total goods exports—also increased significantly during the year.[41] As with minerals, favorable external conditions supported the growth of manufactured exports, which rose by 33.5 percent in 2021 and another 17 percent in 2022.[42] Meanwhile, traditional exports rebounded, growing by 22.1 percent in 2022 after contracting by a similar amount in 2021.[43] However, the contribution of traditional exports to overall export growth declined, as they represent just 10-15 percent of goods exports. Despite this strong performance, the growth rate of Tanzania's goods exports in 2022 was among the slowest in the region (Figure 14). To address this weakness, the government should attain the priority objectives identified by the FYDP (Box 5).

Services exports bolstered the external accounts during 2022. About three-fourths of the increase in services exports was due to improving travel-related inflows, followed by transport-related exports.[44] A 58 percent increase in tourist arrivals during 2022 followed a 48.6 percent increase in 2021, boosting travel receipts (Figure 15). This trend continued in the first three months of 2023, as both travel receipts and arrivals grew by over 40 percent versus the same period in the previous year. In 2022, about one-third of tourists visiting Tanzania came from regional neighbours, while two-thirds came from advanced economies. Russia was Tanzania's third-largest tourism source market in 2021, and Russian and Ukrainian tourists accounted for 10.6 percent of total arrivals. This share plunged to 1.4 percent in 2022. Nevertheless, travel receipts and tourist arrivals are both close to pre-pandemic levels. Overall, services exports continued to show strong growth momentum, rising by 42.8 percent in 2021 and almost 53 percent in 2022. The latest data indicate that this trend has continued in 2023.[45]

41 Gold exports rose from US$2.74 billion in 2021 to US$2.83 billion in 2022, an increase of 3.6 percent. As international gold prices remained broadly unchanged in 2022, the increase in gold exports mainly reflected the positive volume effect.

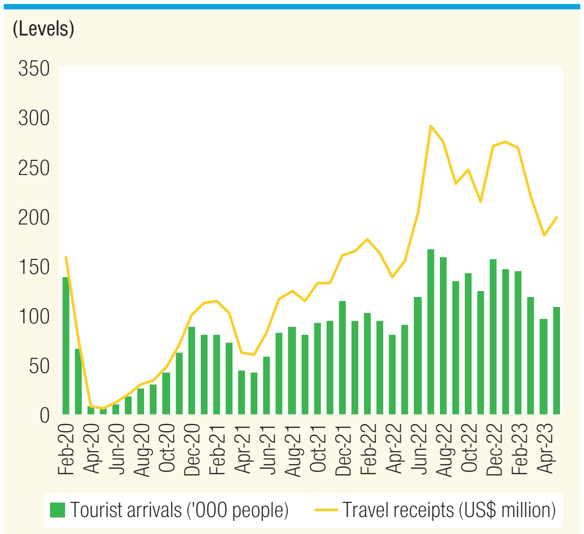
42 In 2022, growth rebounded strongly in India and the United Arab Emirates, which together receive about one-fourth of Tanzania's total goods exports. In addition, key regional export markets like Democratic Republic of Congo, Rwanda, and South Africa also exhibited sustained recoveries despite shocks.

43 Tanzania's traditional exports include commodities such as coffee, cotton, tea, cashew nuts, and tobacco.

44 Transport-related exports increased by 20 percent in 2022 and contribute about 19 percent of overall growth in exports of services from Tanzania.

45 As per monthly data, services exports grew by 27.3 percent in 5M-2023 on y/y basis. Source: Bank of Tanzania.

FIGURE 15 • Tourism Receipts and Arrivals



Source: Bank of Tanzania, NBS, WB staff estimates.

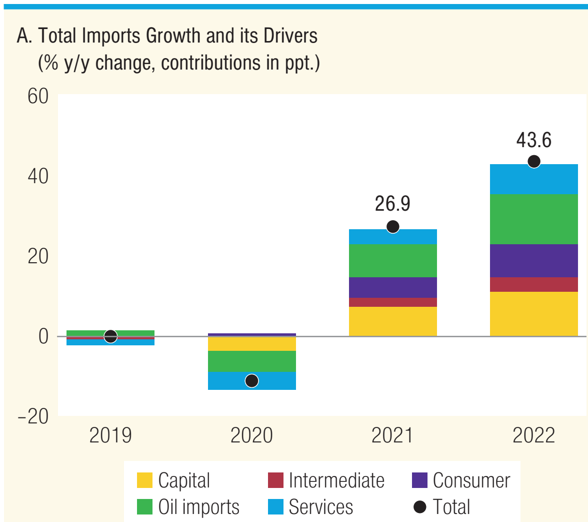
Despite the robust recovery of overall exports, a sharp increase in the import bill, especially for goods imports, widened the trade deficit. Led by strong demand for capital and intermediate goods to meet development aspirations, the growth of goods imports accelerated from 27.7 percent in 2021 to 42 percent in 2022. Reflecting the country's large infrastructure gap, all major capital-goods imports related to transportation, construction, and machinery have registered double-digit growth rates over the past two years. Similarly, due to a sustained increase in underlying demand, the growth of consumer imports has also remained robust, and consumer goods accounted for about one-fourth of the growth of goods imports in 2022.

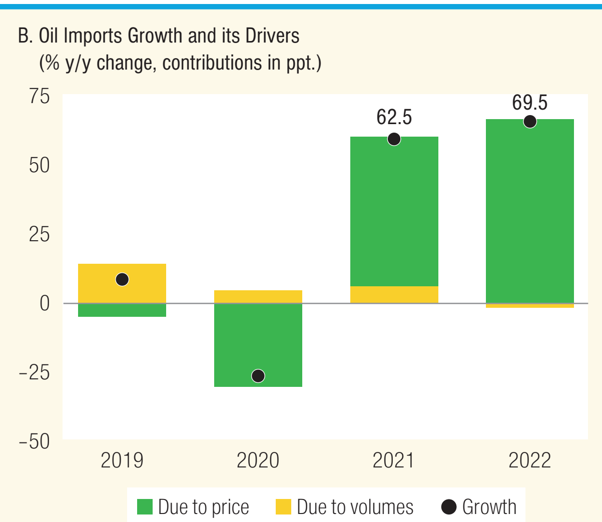
Rising global prices and elevated domestic demand have driven up the import bill. For example, the volume of oil imports fell slightly in 2022, yet the value of oil imports rose by almost 70 percent (Figure 16). By contrast, the growth of volume remained a significant factor for non-energy imports, highlighting the sustained improvement in economic activity across all sectors. Overall, goods imports were responsible for about 83 percent of total import growth in 2022. Services imports accounted for the remainder, particularly transportation services, as rising fuel prices pushed up costs.

During 5M-2023, a declining import bill narrowed the trade deficit, both for goods and services. Cumulatively, the trade deficit dropped by 5.6 percent y/y, falling from US$1.74 billion during 5M-2022 to US$1.65 billion during the same period in 2023. This trend is being driven by slowing goods imports, which contracted on a y/y basis in three out of the first five months of 2023 and grew by just 6.6 percent on a cumulative basis, down from 37.6 percent during 5M-2022.[46] Intermediate and consumer imports

[46] Goods imports declined by 19.7 percent in January 2023, 4.7 percent in February 2023, and 17.6 percent in April 2023 on a y/y basis.

FIGURE 16 • Tanzania - Imports





Source: Bank of Tanzania, NBS, WB staff estimates.

both contributed to this decline, while the import of capital goods experienced a less pronounced slowdown. Led by mineral exports, goods exports grew by a cumulative 6.2 percent in the first five months of the year. This, combined with a 43.4 percent y/y increase in travel-related services exports drove the narrowing of the trade deficit.

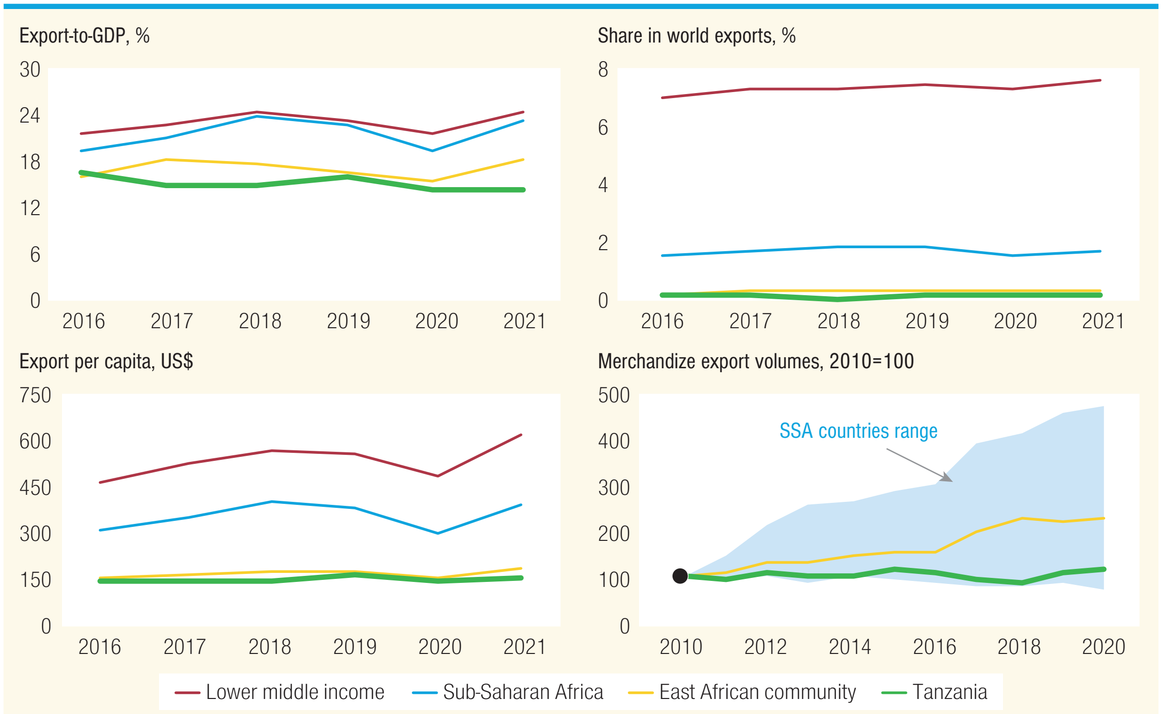
Limited financing flows and a widening CAD led to a decline in foreign-exchange reserves. In 2022, the financial account recorded a surplus of almost US$3.9 billion (5.1 percent of GDP), down from a surplus of US$4.0 billion (5.7 percent of GDP) during 2021. Both private and official flows contributed to this trend. Slowing private flows, including both portfolio and direct flows, reflected growing global risk aversion toward developing economies, as well as worsening domestic conditions for investment. The slowdown in the official flows, however, has

BOX 5: EXTERNAL COMPETITIVENESS IN TANZANIA

Tanzania's overall economic performance has seen notable improvements over the past two decades: the annual GDP growth rate averaged just over 6 percent, while goods and services exports increased by a combined 650 percent. Tanzania's Five-Year Development Plan (FYDP) for 2021/22 – 2025/26 aims to bolster economic competitiveness by improving the efficiency and productivity of the manufacturing and services sectors. As projected in the FYDP, one of the major expected outcomes of these objectives is the growth of goods and services exports from 16.1 percent of GDP in 2019/20 to 28 percent by 2025/26, increasing Tanzania's share of exports in global markets from 0.1 percent to 0.15 percent over the period.

The FYDP's export targets appear ambitious, particularly considering current domestic and global economic conditions and the medium-term outlook. However, such ambition is crucial to promote macroeconomic stability. According to World Bank data, Tanzania's export-to-GDP ratio steadily declined over the last decade, falling from a peak of 22.4 percent in 2012 to 14.3 percent in 2021, while the country's share in global export markets remained stagnant. While the slowdown in export growth is due in part to the global trade deceleration—a challenge faced by many countries since the 2008 global financial crisis, Tanzania's recent export performance significantly lags those both of its regional neighbors and global peers (Figure B5.A).

FIGURE B5.A • A Tanzania's Export Performance



Source: WDI, WB staff estimates.

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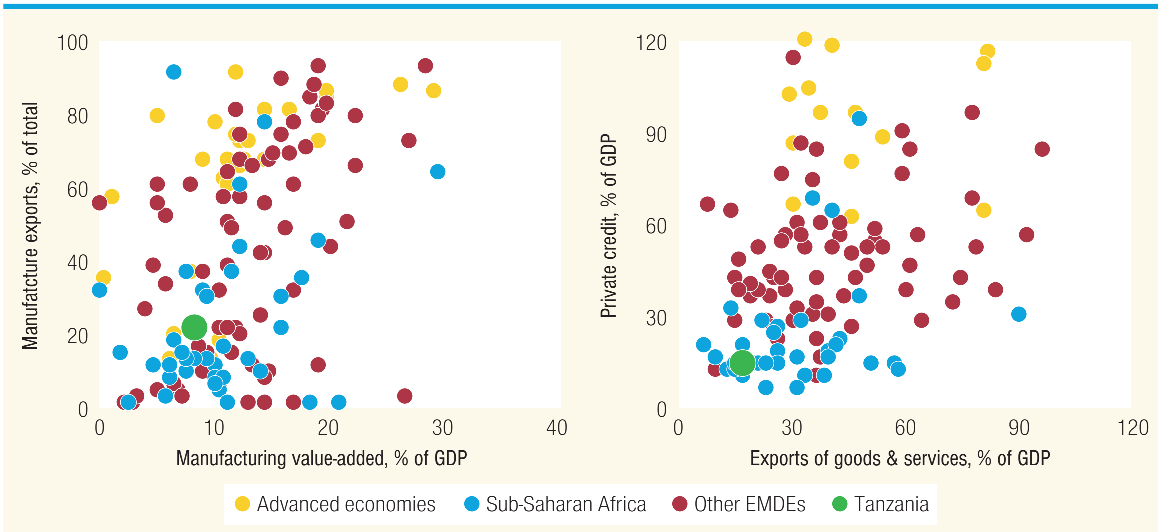
BOX 5: EXTERNAL COMPETITIVENESS IN TANZANIA *(continued)*

The trends presented in Figure B5.A highlight the underlying weaknesses in Tanzania's export structure, especially with regard to merchandize exports. These weaknesses mostly stem from Tanzania's narrow manufacturing base relative to those of other major regional economies. Another important factor is the lower penetration of credit in the economy (Figure B5.B). Moreover, the share of credit to the manufacturing sector stands at just 11 percent of total lending. These shortcomings have been reflected in a significant decline in total factor productivity over the last decade (Figure B5.C).

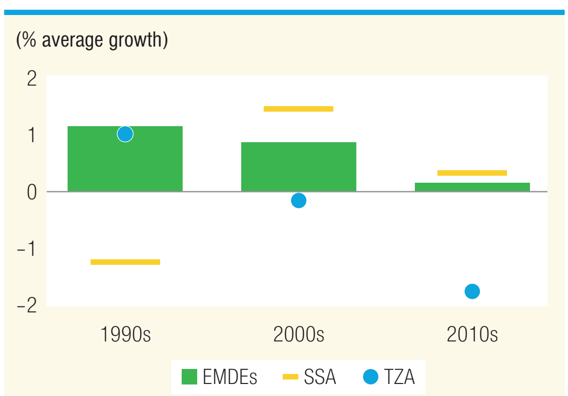
To address these issues, the FYDP identified several priority objectives, including improved access to markets, the establishment of trade-logistics centers, reforms to lower nontariff barriers, reduced logistics costs through improved transport infrastructure, and the development of a national brand for domestically produced products. The FYDP also provided a comprehensive blueprint for promoting services exports, including tourism. To achieve these goals and improve the economy's export competitiveness and productivity, however, the authorities will need to swiftly implement the agreed-upon reform agenda with support from development partners.

FIGURE B5.B • Manufacturing, Credit and Exports



Source: WDI, WB staff estimates.

FIGURE B5.C • Total Factor Productivity



Source: Conference Board.

larger implications for import-dependent economies such as Tanzania. Net government flows dropped by 9 percent between 2021 and 2022, falling from 4.0 percent of GDP to 3.4 percent. Due to the narrowing financial-account surplus and widening CAD, gross official foreign-exchange reserves fell by US$1.2 billion in 2022, reaching about US$5.2 billion at the end of the year and continuing to decline during the first five months of 2023. As a result, reserve coverage fell from a peak of 7.0 months of imports in September 2021 to just 4.8 months at end-June 2023. The decline in reserves was due in part to the direct management of the foreign-exchange market by regional economies, as the depreciation of local currency against the US dollar has been moderate to high over the past year (Box 6).

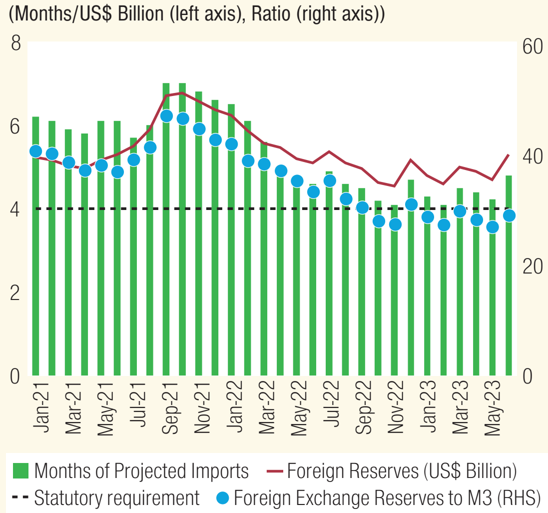
BOX 6: TANZANIA'S DECLINING OFFICIAL FOREIGN-EXCHANGE RESERVES

Tanzania's official foreign-exchange reserves (OFER)[a] have fallen by more than 20 percent over the past two years, though remain adequate for managing the balance of payments. OFER fell from a peak of US$6.8 billion at end-September 2021 to US$5.3 billion in June 2023, with import cover[b] declining from 7.0 months to 4.8 months, remaining above the EAC convergence criteria of at least 4 months. Similarly, the ratio of official reserves to broad money[c] fell over the period but stayed above 27 percent at its lowest, exceeding the international standard of at least 20 percent (Figure B6.A). These two benchmarks indicate that Tanzania's OFER remains adequate. Like in Tanzania, reserve drawdowns were also observed in most East African countries between 2022 and 2023. Kenya's OFER fell to US$7.0 billion (3.9 months of imports) in March 2023, their lowest level since 2015. Uganda's reserves also dropped, from US$4.2 billion (4.4 months of imports) in May 2022 to US$3.5 billion (3.8 months of imports) in May 2023. Official reserve levels in other countries in the region such as Rwanda, Mozambique, and Mauritius also declined to varying degrees over the period (Figure B6.B).

Rising costs of imports, interest rate hikes in the US and seasonality of export earnings were key drivers of foreign exchange pressures. Global inflationary pressures caused by pandemic-related supply-chain disruptions and the spillover of Russia's invasion of Ukraine have raised the costs of strategic imports such as fuel and food. Price pressures also prompted the US Federal Reserve to raise interest rates 11 times since March of last year. Rate hikes in other advanced economies followed, drawing portfolio capital away from emerging markets and developing economies, which saw their currencies depreciate against the US dollar. In addition, the seasonality of Tanzania's traditional crop exports and tourism receipts exacerbated the abovementioned foreign exchange demand pressures.

FIGURE B6.A • Official Foreign-exchange Reserves, Tanzania

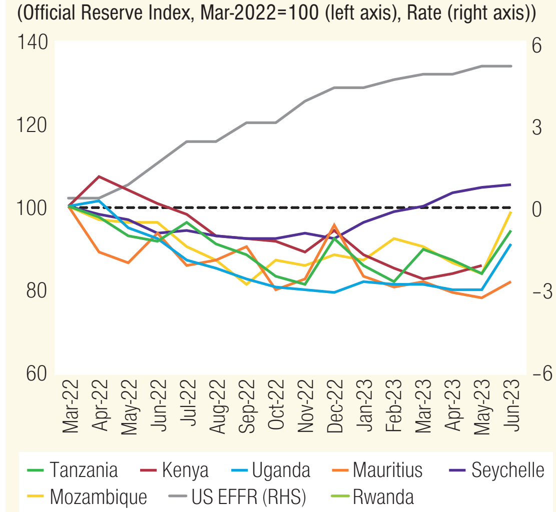
(Months/US$ Billion (left axis), Ratio (right axis))



Source: Bank of Tanzania, WB staff estimates.

FIGURE B6.B • Regional Peers Trends and US Rate Hikes

(Official Reserve Index, Mar-2022=100 (left axis), Rate (right axis))



Source: Central Banks, US Fed, WB staff estimates.

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BOX 6: TANZANIA'S DECLINING OFFICIAL FOREIGN-EXCHANGE RESERVES *(continued)*

Falling reserves have negatively impacted Tanzania, including through fuel shortages and the emergence of a parallel foreign exchange market. The Bank of Tanzania used reserves in 2022 and early 2023 to help meet building foreign exchange pressures, while keeping the official nominal exchange rate stable. Continued pressures and slowing use of reserves caused a shortage of dollars available to meet importer needs at the official rate, and commercial banks accumulated over US$700 million worth of outstanding Letters of Credit. This caused delays in oil imports, and pump prices rose in Dar es Salaam by 17 percent. Insufficient access to foreign currency among firms and households, combined with the limited flexibility of Tanzania's official exchange rate, also gave rise to a parallel foreign-exchange market charging a premium of 8 to 10 percent compared to the official rate. The distortion of a parallel market causes significant uncertainty to business and can reduce formal economic activity through reduced importation. It can also deter foreign investment and discourage lending to the government, as investors may be unable to repatriate profits or purchase imports at the parallel-market rate.

In May 2023, the Bank of Tanzania (BoT) announced short term measures to help address the decline in official reserves and foreign exchange. The BoT increased sales of foreign exchange on the Interbank Foreign Exchange Market, taken steps to address excess liquidity in financial markets, facilitated the resolution of Letters of Credit, and increased the value of transactions conducted outside the Interbank Foreign Exchange Market. Moreover, the BoT has mopped up excess liquidity in the financial market and allowed more flexibility of the exchange rate in recent months, with the Tanzanian shilling depreciating by one percent between January and June 2023. Continued flexibility will be important going forward, to eliminate the distortive parallel foreign exchange market. The Government can also look for ways to lessen or better time its demand for foreign exchange against available inflows, for example by adjusting the implementation of large capital imports for development projects.

More fundamentally, longer term measures are needed to boost forex inflows–such as exports, foreign direct investment (FDI) and remittances–to better manage transitory forex demand pressures. Slowing structural reforms and expanding reliance on public investment in the past decade have reduced private gross fixed capital formation by 2 percentage points of GDP and decreased FDI inflows to 1.3 percent of GDP in 2021 from 5.6 percent in 2010. Exports as a share of GDP has also sharply declined from 20.9 percent in 2012 to 14.3 in 2021. These trends highlight the urgency of Government implementing structural reforms to strengthen the competitiveness of the economy, improve the business and investment environment, and reduce the cost of regulatory compliance. This includes follow-through on key initiatives such as eliminating payment arrears to the private sector, revamping the legal frameworks for investment and public-private partnerships, and improving the resilience of the labor force to shocks.

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[a] Official foreign-exchange reserves generally refer to external financial assets used by the central bank for multiple purposes, such as financing the balance of payments, intervening in foreign-exchange markets to stabilize exchange rate, and servicing external debt. These assets usually include foreign-currency reserves (e.g., securities and deposits) and non-foreign-currency reserves (e.g., IMF reserve positions, Special Drawing Rights, gold, etc.).

[b] Different countries use different methods to calculate import cover. For example, Kenya calculates the ratio between OFER (end of period) and the average value of imports over the past 36 months, while Tanzania uses the ratio between OFER and the average projected value of imports over the following financial year.

[c] According to Schanz (2019), Tanzania's banking sectors has a large share of foreign-currency liabilities at around 36 percent, which makes the ratio of OFER to broad money another important benchmark to measure the reserves adequacy for Tanzania. Source: Schanz, J. F. (2019). Foreign exchange reserves in Africa: benefits, costs and political economy considerations. BIS Paper, (105).

2

MACROECONOMIC OUTLOOK AND RISKS

Global Conditions

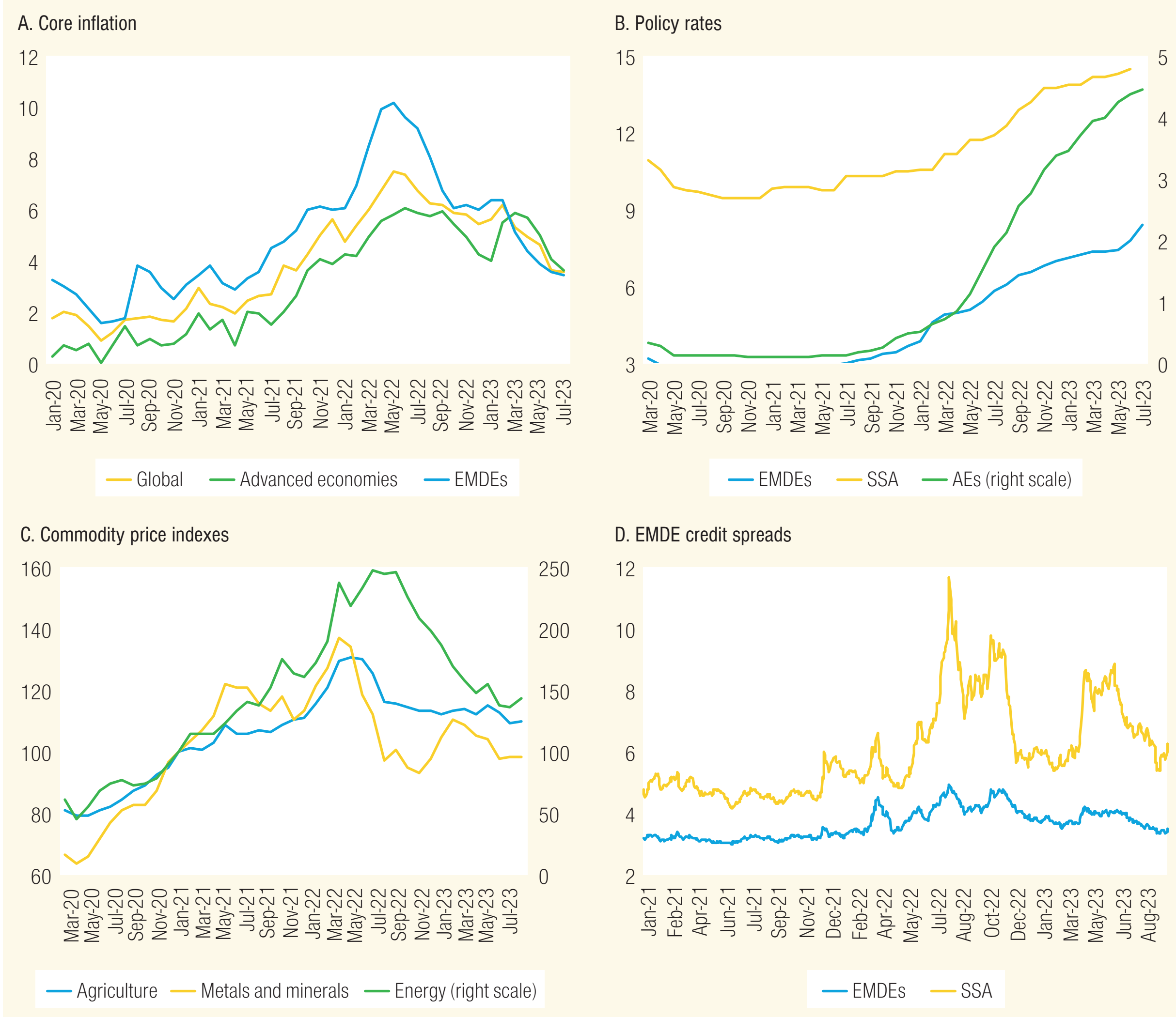
Global growth is expected to slow sharply this year as ongoing monetary tightening and more restrictive credit conditions weigh on economic activity. Despite a recent deceleration in global headline inflation due to easing supply disruptions and moderating commodity prices, inflationary pressures remain elevated across much of the world. In most inflation-targeting economies, inflation rates remain above the policy target (Figure 17A). Monetary tightening has been swift and unprecedented, especially in advanced economies, leading to a sharp increase in borrowing costs, tighter credit conditions, and episodes of financial stress in banking and interest-rate-sensitive sectors such as commercial real estate. Global economic activity is stronger than had been expected earlier in the year but is still projected to weaken substantially in 2023, with a particularly sharp slowdown in advanced economies, reflecting the delayed negative impact of higher interest rates (Figure 17B). Global growth is projected to fall to 2.1 percent this year before recovering modestly to 2.4 percent in 2024.[47]

Growth in emerging markets and developing economies (EMDEs) is expected to soften significantly this year amid slowing external demand, tighter global financial conditions, and weaker spillover from renewed growth in China. The aggregate growth rate for EMDEs, excluding China, is projected to fall from 4.1 percent in 2022 to 2.9 percent this year, as weaker external demand amplifies the negative impact of elevated inflation and tighter monetary policies. The recovery of the service sectors is expected to drive a substantial acceleration in the growth of the Chinese economy, albeit with limited spillovers on global demand, trade, and commodity prices (Figure 17C). Meanwhile, tighter financing conditions, slower growth, and high debt levels are expected to undermine debt dynamics across EMDEs, especially low-income countries, and further narrow their already constrained fiscal space, increasing the risk of debt distress.

Growth in SSA is expected to moderate, reflecting worsening country-specific challenges and mounting external headwinds. Aggregate

[47] World Bank. 2023. *Global Economic Prospects. June 2023*. Washington, DC. World Bank.

FIGURE 17 • Global Indicators



Source: Bank for International Settlements; Haver Analytics; JP Morgan; International Monetary Fund; World Bank.
Notes: AEs =Advanced economies ; EMDEs = Emerging Markets and Developing Economies ; SSA = Sub-Saharan Africa.
A. Figure shows the median 3-month-on-3-month annualized percentage change of core inflation. Sample includes 31 advanced economies and 45 EMDEs. Last observation is July 2023.
B. Unweighted averages. Sample includes 16 advanced economies, 21 EMDEs (Argentina was excluded as its high inflation distorts the average), and 8 SSA economies Last observation is July 2023.
C. Pink Sheet data for energy, metals, and agricultural prices indexed to January 2021=100. Last observation is July 2023.
D. Percentage points. Figure shows JP Morgan Emerging Markets Bond Index (EMBI); SSA indicates median for 9 economies. Last observation is August 16, 2023.

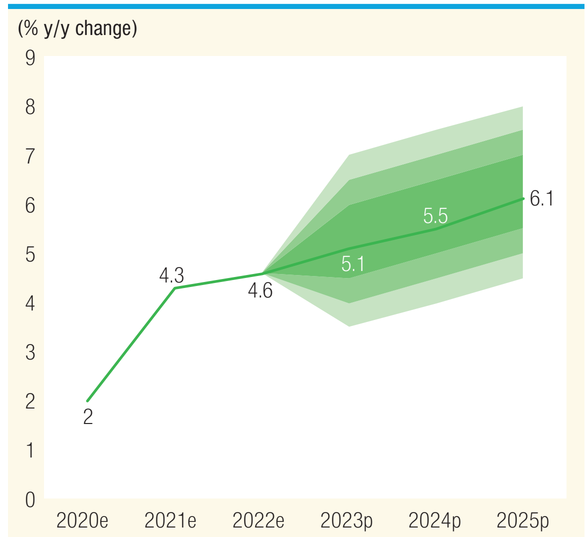
regional growth is projected to bottom out at 3.7 percent this year, with only a moderate improvement to 3.9 percent anticipated for 2024. The ongoing energy crisis in South Africa and persistent challenges in Nigeria's oil sector are expected to continue to hinder overall growth in SSA. While accelerating economic activity in China could boost exports in some countries, particularly metal exporters, limited access to external borrowing will weigh on the recovery as borrowing costs and financing needs remain elevated (Figure 17D). High living costs across the region are projected to continue to weaken private consumption, while limited fiscal space and tight monetary policies are likely to constrain investment growth. In addition to external and domestic headwinds, many SSA countries also face increased fragility due to insecurity and political instability, as well as persistent poverty. Many SSA economies, already coping with the negative consequences of climate change, lack the fiscal resources necessary to strengthen climate resilience.

Outlook and Risks for Tanzania

While Tanzania's economy is projected to grow by 5.1 percent in 2023, this projection has been adjusted downward to reflect the impact of worsening global economic conditions and insufficient rainfall in agricultural areas. In 2022, the post-pandemic economic reopening, coupled with sustained tourism inflows, boosted domestic demand, helping to offset a modest increase in inflation and a slowdown in external demand. Meanwhile, public investment in megaprojects contributed to capital formation. Growth is likely to edge up further to 5.5 percent in 2024 as the business climate improves and domestic reforms take hold. However, medium-term growth is expected to average about 5.8 percent, as the impact of pent-up demand subsides while inflation remains elevated and higher interest rates temper domestic demand. The annual GDP growth rate is not expected to return to its potential until 2025, when the cyclical recovery will close the output gap. This projection assumes that the government's reform agenda will be successfully implemented. Without mitigation measures, the country's long-term growth potential could weaken, with GDP growth ranging from 4.5 to 5.5 percent (or 1.6 to 2.6 percent per capita) in 2023 under alternative scenarios (Figure 18). A deteriorating external environment and the delayed implementation of domestic reforms are the major risks to the macroeconomic outlook.

The expansion of agriculture and services activities is expected to drive growth and poverty reduction over the medium term. Agricultural output growth is expected to accelerate from 3 percent to about 5 percent by 2025, while the growth of services is expected to rise from 5 percent to 7 percent. The agricultural sector, which employs nearly 70 percent of the rural workforce, is expected to benefit from increased government spending on irrigation infrastructure and extension services, boosting agriculture productivity and incomes of the people. In FY2022/23, the government almost doubled agricultural spending from about 0.4 percent of GDP in previous years to about 0.7 percent. Meanwhile, the rapid expansion of retail and repair services is expected to boost incomes among urban informal workers. The continued expansion of tourism could also increase incomes and support poverty reduction in urban areas.

FIGURE 18 • Real GDP Growth Forecasts under Alternative Scenarios



Source: WB staff estmates.
Note: These estimates are based on growth scenarios and risk profiles that use different assumptions for global uncertainty and domestic policy implementation. The lighter bands indicate less likely outcomes, while darker bands indicate the most likely outcomes, and the central black line is the baseline scenario.

Price pressures are expected to moderate over the medium term. The headline inflation rate is expected to fall to 4.2 percent in 2023, far below the official target of 5 percent. Elevated global food and fuel prices, exacerbated by Russia's war in Ukraine, will continue to drive inflationary pressures. The global shift to less-accommodative monetary policies has led to tighter global financial conditions, rising capital outflows, and currency depreciation among EMDEs. These external developments have affected Tanzania largely through a deterioration in the terms of trade and rising inflationary pressures. The country's monetary authorities will adhere to their mandate of ensuring price stability and are expected to anchor expectations and keep inflation within the target range. Going forward, inflation is expected to taper gradually as global commodity prices moderate, planned investments in agriculture are completed, and an interest-rate-based monetary framework is implemented.[48]

The fiscal deficit is projected to narrow in the near term as the economic recovery bolsters domestic revenues and the pace of

[48] This framework is expected to be established as part of the IMF-ECF program.

public spending slows. The central government's overall fiscal deficit is projected to narrow slightly to 3.4 percent of GDP in FY2023/24. While the fertilizer subsidy program, additional hiring in the education and health sectors, and recent increases in the wages and salaries of civil servants[49] are expected to keep recurrent expenditures elevated, rebounding economic activity and enhanced revenue mobilization are expected to improve the fiscal outlook over the medium term. The completion of large hydropower projects will help moderate capital spending and aid the consolidation effort, and the central government's overall deficit is projected to narrow by 1 percentage point of GDP by end-2025. Growth and fiscal consolidation are expected to reduce the public debt stock from 43.8 percent of GDP in 2022 to 41.9 percent in the near term and about 38 percent in the medium term. However, outstanding VAT refunds and domestic expenditure arrears[50] were estimated at about 3-4 percent of GDP at end-2022, and implementing the recently approved Arrears Management Strategy will remain critical to strengthen fiscal management.

The CAD is expected to narrow over the medium term and should be financed largely by concessional external borrowing and FDI. The robust recovery of tourism, coupled with slowing import growth and easing global commodity prices, could help narrow the CAD by almost 2 percentage points of GDP by 2025. After approving a key investment law, the government is now preparing its implementing regulations, which should help attract more FDI over the medium term.

Significant downside risks cloud the growth outlook. Key domestic risks include the slow or incomplete implementation of structural reforms, particularly those relating to private-sector development and women's economic empowerment, as well as the impact of climate change on the agriculture and tourism sectors. The medium-term outlook hinges on the implementation of the reform agenda. On the external front, synchronous monetary policy tightening by major central banks, combined with global fiscal tightening, has triggered a sharper-than-expected downturn in growth and increased the risk of a global recession. Meanwhile, mounting financial stress could exacerbate existing fiscal and financial vulnerabilities. Adverse shocks could weaken business and consumer confidence and temper private investment and consumption, which are key drivers of growth. As global economic activity slows, external demand will continue to weaken, with especially negative implications for the manufacturing sector. A continued commitment to priority reforms will be critical to strengthen the economic recovery, preserve macroeconomic stability, and support sustainable and inclusive growth.

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49 This includes a 23.3 percent increase in the number of public servants anticipated in the FY2022/23 budget.

50 The authorities have made progress in reducing VAT refund arrears, which stood at Tsh 681 billion (0.4 percent of GDP) at end-December 2022, of which unpaid verified refund claims were only Tsh22 billion. Policies to address this longstanding domestic arrears problem are being supported by both the World Bank and the IMF-ECF program.

TABLE 3 • Medium-Term Outlook, 2021-2025
(Annual % change unless otherwise indicated)

	2021 Est.	2022 Est.	2023 Fcst.	2024 Fcst.	2025 Fcst.
Real GDP Growth (at constant market prices)	**4.3**	**4.6**	**5.1**	**5.5**	**6.1**
Private Consumption	2.3	4.8	2.2	3.3	3.3
Government Consumption	9.0	8.4	10.7	6.2	11.3
Gross Fixed Capital Investment	7.8	9.3	5.3	5.4	5.3
Exports, Goods and Services	5.2	10.2	13.8	10.4	10.2
Imports, Goods and Services	9.6	23.7	6.8	4.2	3.6
Inflation (consumer price index)	3.7	4.3	4.2	4.1	3.9
Current Account Balance (% of GDP)	−3.2	−5.6	−5.1	−4.4	−3.5
Net Foreign Direct Investment (% of GDP)	1.6	1.8	2.1	2.6	2.9
Fiscal Balance (% of GDP in FY)	−3.8	−3.5	−4.0	−3.4	−2.9
Gross Nominal Debt (% of GDP in FY)[a]	41.3	43.8	40.9	39.2	37.8

Source: World Bank Staff Estimates.
Note: Est. stands for Estimates and Fcst. stands for Forecasts. All variables are based on calendar year unless otherwise specified. Fiscal Year (FY) runs from 1st July to 30th June
[a] As is the same in the published WB-IMF Joint Debt Sustainability Analysis in April 2023. For details, see United Republic of Tanzania, Country Report No. 23/153, April 2023, International Monetary Fund.

3

SPECIAL FOCUS: THE EFFICIENCY AND EFFECTIVENESS OF FISCAL POLICY IN TANZANIA

Introduction

Public spending in Tanzania has increased, led by development expenditures, but remains low by the standards of comparable countries. At about 17 percent of GDP, total public spending is below the average for SSA (18 percent), LICs (21 percent), and lower-middle-income countries (LMICs) (28 percent). Closing compliance gaps can help Tanzania increase revenue collection and establish a fairer, more efficient tax system while increasing public expenditures, including priority social spending. The distributional impact of its revenue and expenditure policies indicates that Tanzania's fiscal system substantially reduces income inequality, while public spending on social services more than offsets a moderate increase in poverty. The analysis of the efficiency and effectiveness of Tanzania's fiscal policy presented below is based on the BOOST[51] database and the Commitment to Equity (CEQ)[52] methodology.

Benchmarking Public Expenditures

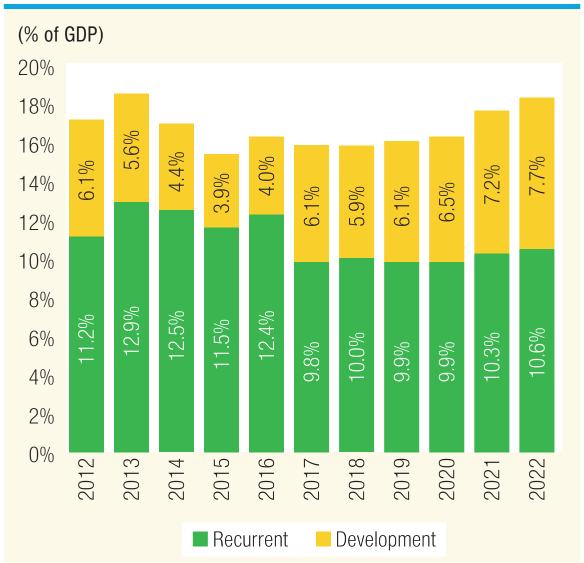
Historical Overall Expenditure Performance

Given the limited scope of Tanzanian monetary policy, the government relies heavily on fiscal policy to achieve its growth and stabilization objectives. However, this does not imply that an expansionary fiscal stance is necessary to accelerate growth. While fiscal stimulus will likely increase

[51] The BOOST database project initiated by the World Bank in early 2010 aims to increase the transparency and efficiency of public spending across the world by improving access to government expenditure data and linking expenditures to relevant outcomes.

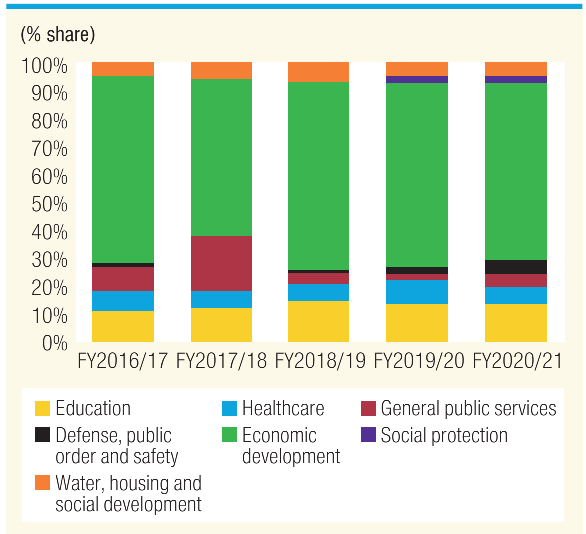
[52] The CEQ methodology provides a comprehensive assessment of how taxes and social spending affect income inequality and poverty. These assessments are comparable across countries and over time.

FIGURE 19 • Trends in Government Spending



Source: MoFP and WB staff calculations.

FIGURE 20 • Composition of Development Expenditure by Sector



Source: MoFP and WB staff calculations.

aggregate demand and boost economic activity in the short term, investments that address binding supply constraints will be vital to raise potential output and support economic growth over the medium term. In recent years, political uncertainty has increased public expenditure volatility, negatively affecting Tanzania's economic performance. In addition to greater expenditure predictability, regulatory reforms and improvements in PFM can enhance the impact of fiscal policy on economic activity. Effective sectoral policies, both in the productive and social sectors, are a critical complement to sound macro-fiscal policies. Finally, rationalizing recurrent spending, prioritizing public investments, strengthening public investment management, and enhancing tax collection will also be crucial to accelerate and sustain economic growth.

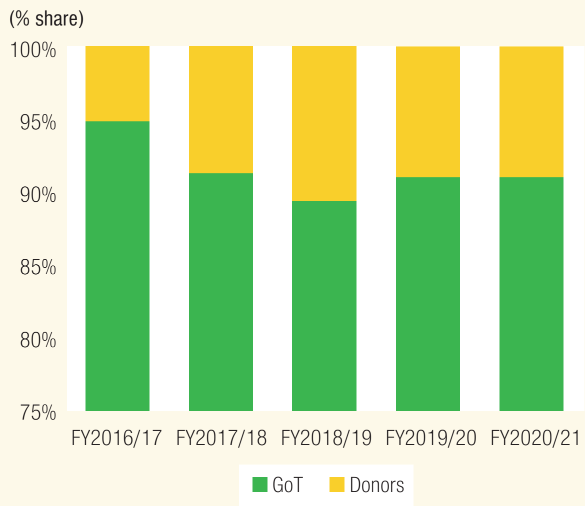
Public spending has broadly stabilized as a share of GDP since FY2012/13, and the growth of development expenditures has outpaced the growth of recurrent spending since FY2016/17. Government spending increased significantly from 12.6 percent of GDP in FY2000/01 to about 19 percent in FY2005/06 as the authorities ramped up priority expenditures to achieve the Millennium Development Goals. Buoyant revenues and strong donor assistance facilitated Tanzania's fiscal expansion, which continued into the early 2010s. Expenditures broadly stabilized as a share of GDP from FY2012/13 onward. The shift toward development expenditures reflected the priorities outlined in the government's second Five-Year Development Plan,[53] which aims to accelerate the economy's structural transformation by addressing the infrastructure gap and building human capital.

Between FY2016/17 and FY2020/21, recurrent spending averaged about 10 percent of GDP. Meanwhile, development expenditures averaged 6.5 percent of GDP, up from 4.8 percent during FY2011/12–FY2015/16 (Figure 19). Between FY2016/17 and FY2020/21, more than 60 percent of development expenditures were directed to the real sector. These expenditures mainly consisted of infrastructure investments in the Standard Gauge Railway, the Rufiji hydroelectric power plant, and other transportation and electrification projects. (Figure 20).

General government revenue remains the primary source of financing both for recurrent and development spending. The share of foreign financing in total government spending has increased over time, but donor support remains highly fragmented. Between FY2016/17

[53] https://mof.go.tz/docs/news/FYDP%20III%20English.pdf.

FIGURE 21 • Sources of Financing for Public Spending and Top 10 Sources of Finance for Development Spending, FY2020/21



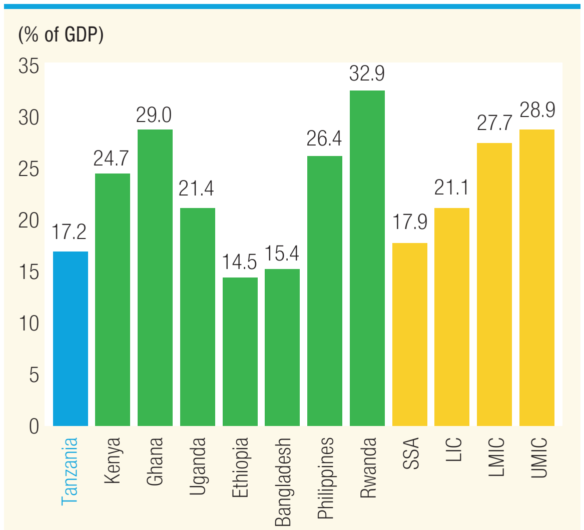
Source of Financing/Donor	% of Total
Government of Tanzania	79.0%
World Bank	10.1%
African Development Bank	3.2%
Basket Fund	1.4%
DFID	0.8%
KOICA	0.4%
South Korea	0.4%
JICA	0.4%
Global Fund	0.4%
SIDA	0.4%
French Development Agency	0.3%

Source: WB BOOST dataset.

and FY2020/21, donor financing accounted for an average of about 20 percent of total development spending or 9 percent of total government spending. However, over 30 development partners disbursed funds in FY2020/21, many with engagements spanning several sectors, which required government ministries and agencies to engage with multiple stakeholders. (Figure 21).

The size of Tanzania's general government is relatively small by the standards of structural peers and comparable income-group averages. Total government spending was estimated at about 17.2 percent of GDP in 2020, below the SSA average of 17.9 percent (Figure 22). Among structural peers, Tanzania has the third lowest level of public spending as a share of GDP after Ethiopia (14.5 percent) and Bangladesh (15.4 percent).

FIGURE 22 • Total Public Spending in Tanzania and Comparator Countries, 2020 or Latest Available Year



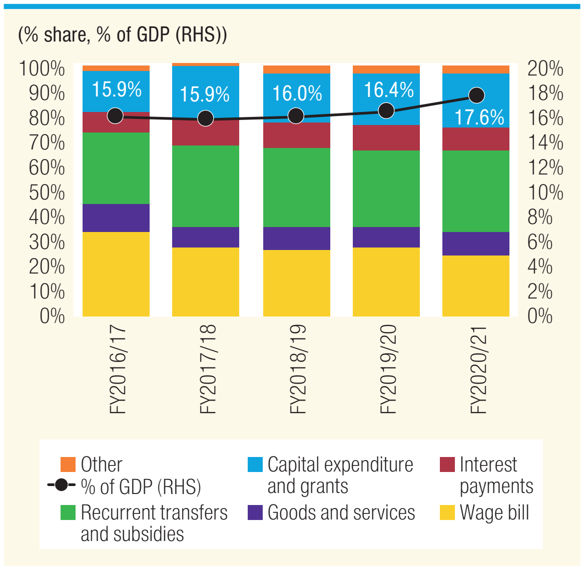
Source: IMF Fiscal Monitor (April 2022), WB-WDI.

Expenditures by Economic Classification

The composition of public spending has remained relatively stable over time, with the wage bill accounting for a large share of expenditures. Recurrent transfers and subsidies are the largest contributor to total spending, followed by the wage bill. Between FY2016/17 and FY2020/21, recurrent transfers and subsidies accounted for an average of about 32 percent of total spending, while the wage bill represented an average of 25 percent, and capital expenditures and grants made up another 20 percent (Figure 23).

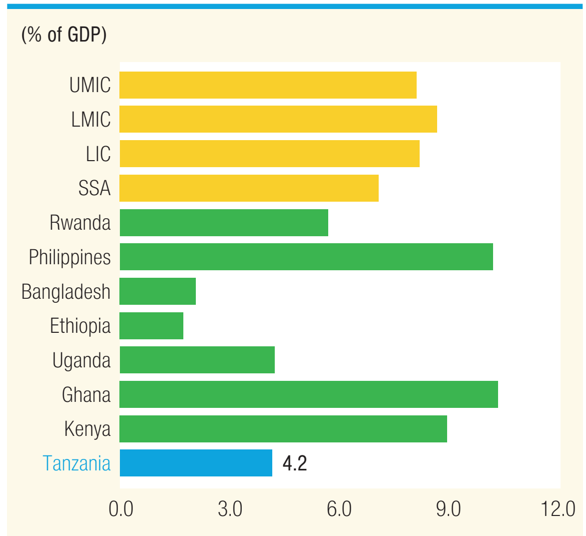
Wages and salaries account for most of the government's personnel costs, though social security contributions are nontrivial. At 4.2 percent of GDP in 2020, spending on the

FIGURE 23 • Composition of Government Spending



Source: WB BOOST data and WB staff calculations.

FIGURE 24 • The Wage Bill in Tanzania and Comparator countries, 2020 or Latest Available Data



Source: WB BOOST data, WB staff calculations, WB-WDI.

public-sector wage bill was significantly below the SSA average (7.1 percent), and Tanzania was tied with Uganda for the third lowest wage-bill-to-GDP ratio among structural peers[54] after Ethiopia (1.7 percent) and Bangladesh (2.1 percent) (Figure 24). However, Tanzania's wage bill represents a large share of total government spending, ranking fourth highest among structural peers after the Philippines (38.5 percent), Kenya (36.2 percent), and Ghana (35.6 percent).

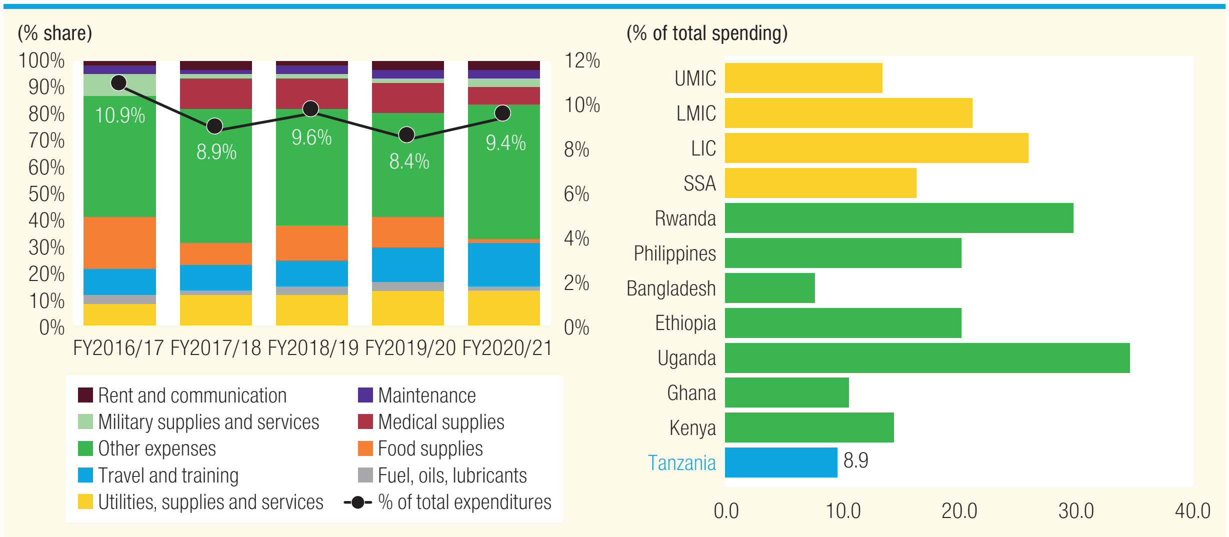
After a slight contraction in FY2016/17, spending on goods and services stabilized at 9 percent of total spending, but the transparency of spending has deteriorated. The goods and services category is broad, but spending is largely concentrated in eight items: domestic and foreign travel and training (16 percent); utilities, supplies, and services (13 percent); medical supplies (7 percent); maintenance (4 percent); fuels, oil, and lubricants (3 percent); military supplies and services (3 percent); rent and communication (3 percent); and food supplies (1 percent) (Figure 25). However, half of all goods and services expenditures in FY2020/21 were classified under "other operational expenses," which may signal an erosion of fiscal transparency within this category.

Capital expenditures and capital grants have remained relatively stable, while subsidies and current transfers are the largest expenditure components. Capital grants are channeled to various central government units, but three budget entities—the Tanzania National Road Agency, the Road Fund Board, and the Tanzania Railway Corporation—accounted for about 70 percent of the total capital transfers in FY2020/21. Meanwhile, on-budget capital expenditures mainly comprised investments in defense, economic development, and healthcare (Figure 26).

Current transfers to SOEs and local government authorities (LGAs) accounted for about one-third of total spending over the analyzed period. According to the official budget data, most capital transfers in FY2020/21 went to SOEs, primarily to finance energy-related projects and support the operations of the Tanzania Electric Supply Company Limited (Annex 4). Similarly, the largest shares of recurrent transfers were dedicated to education (44 percent) and healthcare (12 percent).

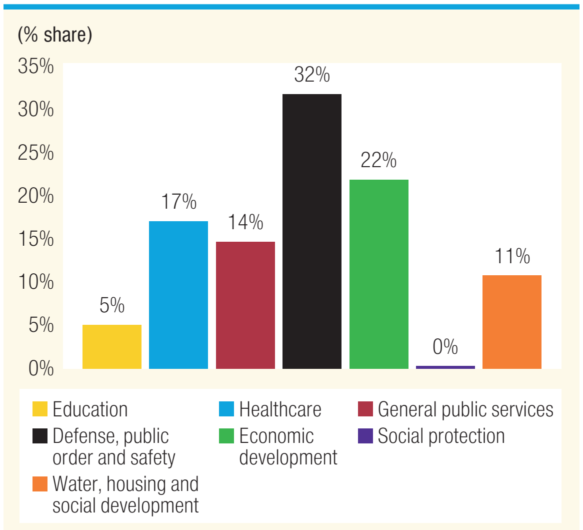
54 Structural peers are countries with economies similar in size to Tanzania's.

FIGURE 25 • Public Spending on Goods Services in Tanzania and Comparator Countries, 2020 or Latest Available Years



Source: WB BOOST data, WB staff calculations, *WB-WDI*.

FIGURE 26 • Composition of Capital Expenditures by Sector, 2021



Source: WB BOOST data, WB staff calculations, *WB-WDI*.

Budget Credibility

Budget execution rates are low, particularly for development expenditures (Figure 27). The gap between the approved and executed budgets offers insight into the quality of the budget process and the government's implementation capacity.[55] Over the past four years, the execution rate for development expenditures averaged 67 percent, with large fluctuations both between and within years. The significant under-budgeting observed in FY2017/18 and FY2018/19 likely indicates weaknesses in strategic planning, budget preparation, and/or expenditure execution. For example, planned activities may have a limited connection to proposed budgets, or policymakers may be unable to adjust initial budget requests to reflect approved allocations. Deficiencies in the budget process likely undermine the efficiency and effectiveness of development projects. This problem has also been pointed out in the latest Controller and Auditor General (CAG) report (Box 7).

While the execution rate for domestically financed development spending has improved, execution rates for donor-financed projects remain low. The execution rate for domestically financed projects rose from 60 percent in FY2017/18 to 85 percent in FY2020/21, while aggregate

55 While budget execution is often used to measure absorptive capacity, it may reflect a combination of challenges in planning, budgeting, and execution, as well as political uncertainty.

FIGURE 27 • Approved and Actual Expenditures by Budget Type, FY2017/18-FY2020/21

Source: WB BOOST data, WB staff calculations.

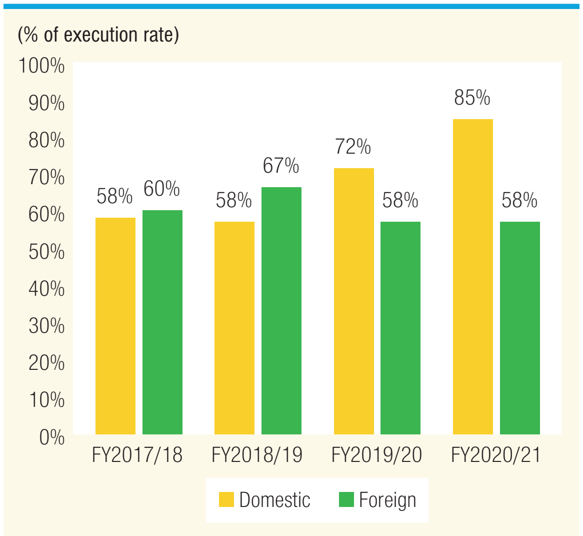
execution rates for donor-financed projects averaged just 58 percent (Figure 28) due to delays in contracting non-concessional loans and the slower-than-expected mobilization of concessional loans.

Expenditures by Sector

Economic development is Tanzania's largest expenditure category by far, while health and education sectors remain relatively underfunded (Figure 29). General government spending on economic development reached 4.6 percent of GDP in FY2020/21, driven by investments in the transportation and energy sectors. Economic development includes expenditures on general economic, commercial, labor affairs, agriculture; energy, mining, manufacturing, and construction; transportation, communication; and other industries.

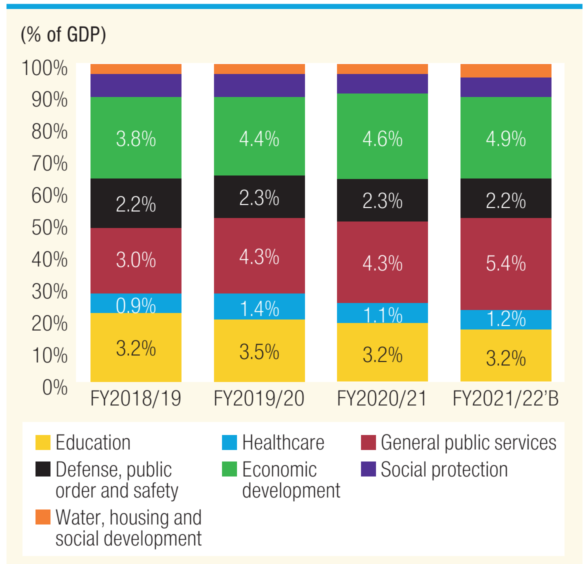
Meanwhile, spending on general public services rose to 4.3 percent of GDP, reflecting mounting interest payments. After a combined increase of 1 percentage point between FY2018/19 and FY2019/20, public spending on education, healthcare, social protection, and other social services declined again in FY 2020/21. Relative to GDP, public health and education spending in Tanzania is below the averages for SSA, LICs, and LMICs (Figure 30). At 3.3 percent of GDP, Tanzania's level of education spending is the third lowest among structural peers after Bangladesh (1.3 percent of GDP) and Uganda (2.6 percent of GDP).

FIGURE 28 • Budget Execution Rates for Development Projects by Financing Source



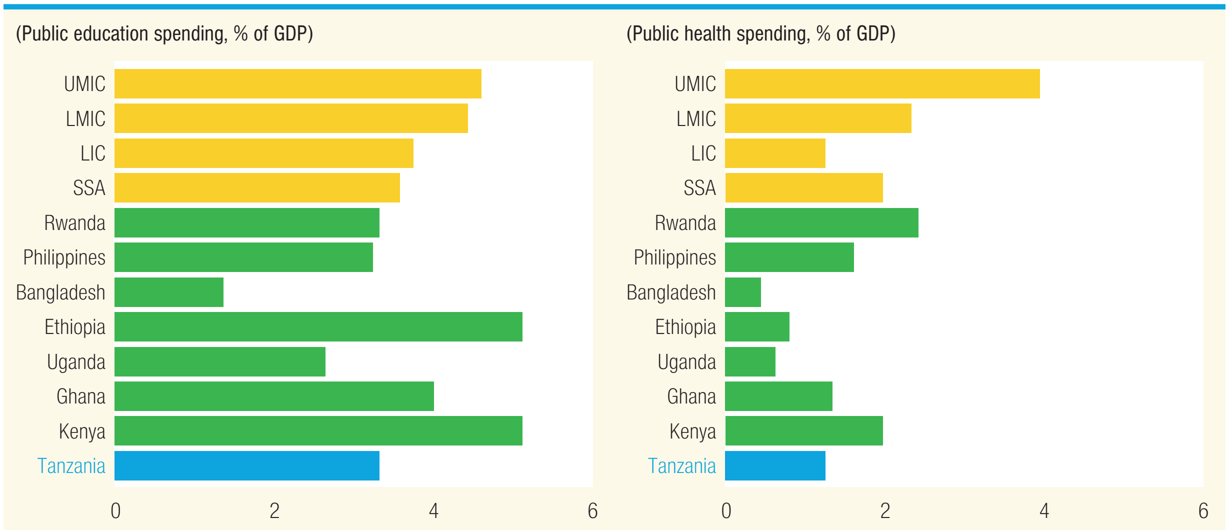
Source: WB BOOST data, WB staff calculations.

FIGURE 29 • Functional Composition of General Government Spending



Source: WB BOOST data, WB staff calculations.

FIGURE 30 • Social Spending in Tanzania and Comparator Countries



Source: WB BOOST data, WB staff calculations.

The Efficiency of Public Spending

The efficiency of public spending can be analyzed both from an allocative and a technical perspective. The findings can assist the government in improving public health and educational outcomes without the need for additional resources. The following analysis focuses on the technical efficiency of government spending on education and healthcare in Tanzania and compares it to the rest of world. "Technical efficiency" implies that public spending delivers the greatest marginal benefit for a given level of resources. For example, increasing value for money in public procurement, strengthening bidding processes, mandating cost-benefit analyses, or tightening controls on fraud and corruption could increase the technical efficiency of public spending. A data-envelopment analysis (DEA) of the relative efficiency of various national healthcare and educational systems can situate Tanzania's experience in the international context. An output-oriented DEA model can simulate maximal improvements in key sectoral outcomes (e.g., life expectancy at birth and infant mortality) without altering per capita health spending. The scatter matrix of the input and output variables shows that, across countries, higher levels of per capita healthcare spending are associated with longer life expectancy at birth and lower infant mortality rates (Annexes 5 and 6).

All Tanzania has significant scope to achieve efficiency gains both in education and health spending. The country's efficiency score of 89 percent implies that technical inefficiencies reduce health system outcomes by 11 percent relative to their potential level (Annexes 7 and 8). In other words, if the health system operated at maximum efficiency, Tanzania could improve key health outcomes by 11 percent without the need for additional resources. The scope to improve the overall efficiency of spending is much greater. Tanzania's efficiency score is 20 percent, implying that 80 percent of overall technical inefficiency can be attributed to the mismanagement of resources. Because efficiency estimates are expressed relative to a given level of spending, it is possible for a country to be fully efficient while remaining below the outcome levels of countries with greater health and/or education expenditures.

Benchmarking Tax Revenues

The Historical Performance of Tanzania's Tax System

Tanzania made steady progress in expanding tax collection between 2000 and 2015, but these gains have not been sustained. From collecting less than

BOX 7: TANZANIA'S PFM CHALLENGES

The 2022 PEFA report identified the lack of a reliable and credible annual budget as the most important challenge facing Tanzania's PFM system. Deficiencies in the core aspects of the PFM, such as budget credibility, cash management, and commitment controls, have continued to undermine budget execution as well as the monitoring and management of domestic payment arrears. Despite recent improvements, the execution rate for the development budget has remained around 70 percent, and in December 2022 the stock of payment arrears was between 3 and 4 percent of GDP. The monitoring of arrears and accounts payable is weakened by the cash-rationing system, as MUSE restricts payments when expenditures exceed the available cash in a given month.

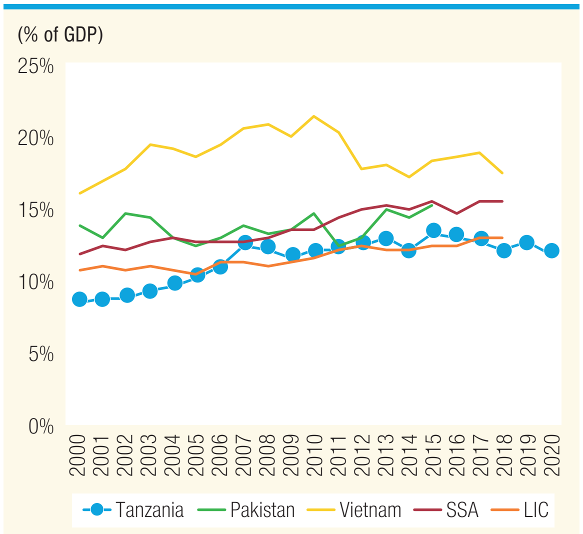
Moreover, the CAG report for FY2021/22 revealed significant gaps in the effectiveness of Tanzania PFM system. The CAG report found major irregularities in government spending, including a sharp increase in unsupported expenditures and trivial expenses. These irregularities are largely driven by weak governance and accountability systems across all levels of government. Moreover, significant weaknesses continue to be observed in public procurement, including unlawful preferences in uncompetitive bidding processes, the unfair evaluation and removal of bidders, the unlawful cancellation of contracts, and unplanned procurements.

While the cash-rationing system has helped maintain aggregate fiscal discipline, it has also undermined the strategic allocation of resources and weakened service delivery. The introduction of MUSE yielded substantial improvements in the PFM system, including introducing more modern and flexible methods of cash planning and commitment control, which can help strengthen the predictability of the budget while controlling the fiscal deficit. These improvements complement recent reforms designed to ensure that salary payments and regular recurrent expenditures are fully financed each month. Further progress could be made in smoothing development expenditures and non-regular recurrent expenditures, which remain subject to monthly cash controls. Subnational procurement systems are also in need of improvements, including increased digitalization and the use of competitive bidding systems.

With support from its development partners, the government is implementing the sixth phase of the Public Financial Management Reform Program (PFMRP VI) during FY2022/23-FY2026/27, which should help to address remaining weaknesses in the PFM system. Improving budget credibility, cash management, and procurement is critical to ensure that the Tanzania PFM system maintains aggregate fiscal discipline while allocating resources in line with strategic priorities and promoting efficient service delivery. Previous phases of the PFMRP have yielded important gains in regulatory reform, human-resources capacity, and the adoption of IT systems, the introduction of the electronic payment gateway and MUSE. The challenge for the PFMRP VI will be to comprehensively address the remaining weaknesses in PFM while maintaining the high standards achieved in other aspects of the PFM system.

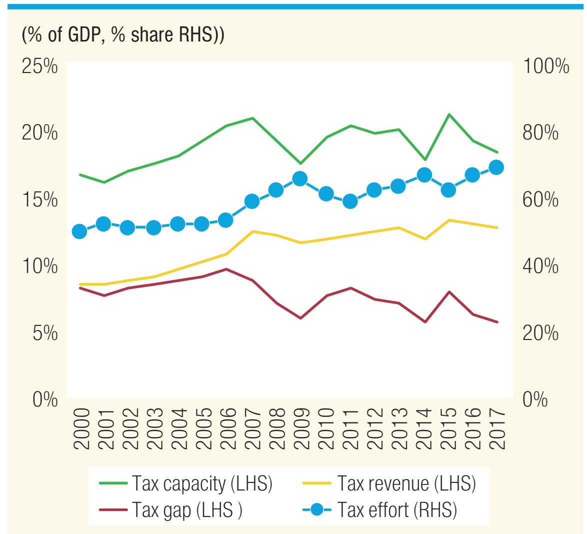
Source: Tanzania PEFA 2022 report and CAG 2021/22 report.

FIGURE 31 • Tax Revenue



Source: WB analysis, data from TRA 2022 and ICTD 2020.

FIGURE 32 • Tax Collection vs. Tax Capacity



Source: WB analysis, data from TRA 2022, ICTD 2020 and WDI 2020.

10 percent of GDP in tax revenue between FY2000/01 and FY2004/05, Tanzania improved its tax-to-GDP ratio to 13.3 percent in FY2015/16 (Figure 31). Increasing revenue collection helped Tanzania formally achieve LMIC status in 2020,[56] though the tax-to-GDP ratio remains close to the LIC average. Between 2000 and 2020, Tanzania's tax-to-GDP ratio was below the level of structural comparators such as Pakistan and Nepal, as well as aspirational peers such as Vietnam, and the SSA average. Nevertheless, Tanzania did experience a clear increase over the period.

Rising tax effort has boosted Tanzania's tax-to-GDP ratio, and significant progress has been made in closing the tax gap. Tanzania's tax effort has steadily increased since 2000 (Figure 32),[57] with the tax gap narrowing from an average of about 8 percent of GDP from 2000 to a low of 5.6 percent in 2017. Between 2000 and 2017, the growth of personal income tax (PIT) and corporate income tax (CIT) drove the increase in total tax revenue, while the contributions from VAT and excise taxes declined. Together, these four instruments account for about 80 percent of total tax revenue.[58] As a result, Tanzania has increased its total tax revenue while shifting to a greater reliance on direct taxes over indirect taxes.

Tanzania's tax system is progressive, but the tax net is very limited. The PIT, which is based on a graduated rate structure, is very progressive, and revenue is collected exclusively from formal workers, who tend to be better off than their informal counterparts. Tanzania's VAT is also progressive, unlike the VATs of many comparable countries. This is due in part to its narrow base, as many low-turnover businesses need not register for VAT. The VAT turnover threshold was approximately 47 times GDP per capita in 2020, far higher than the thresholds in other large middle-income countries with significant informal sectors.[59] However, a

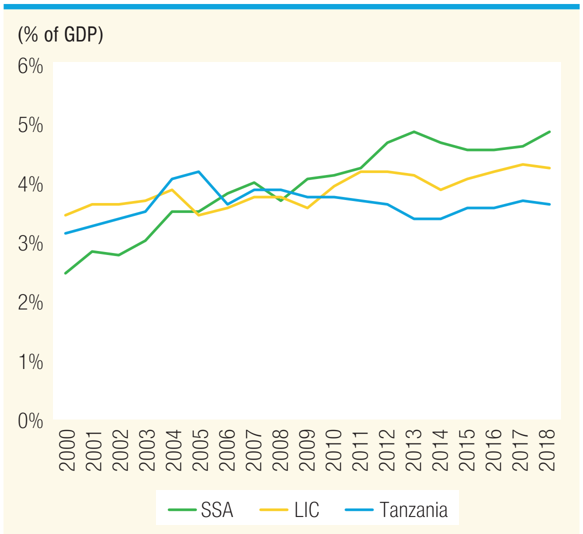
56 See World Bank (3rd March, 2021) Press Release – Maintaining Tanzania's Lower Middle Income Status Post Covid-19 Will Depend on Strengthening Resilience. Available at: https://www.worldbank.org/en/news/press-release/2021/03/03/maintaining-tanzanias-lower-middle-income-status-post-covid-19-will-depend-on-strengthening-resilience#:~:text=DAR%20ES%20SALAAM%2C%20March%203,%2Dmiddle%2Dincome%20country%20status.

57 Tax effort is expressed as the share of tax revenue collected divided by the stochastically predicted amount (tax capacity) that could be collected given a country's GDP per capita, GDP per capita squared, and trade as a percentage of GDP.

58 The TRA's National Statistics Dataset offers a granular review of tax revenue collected both in mainland Tanzania and Zanzibar from 1996/97 to 2020/21 across 11 tax instruments.

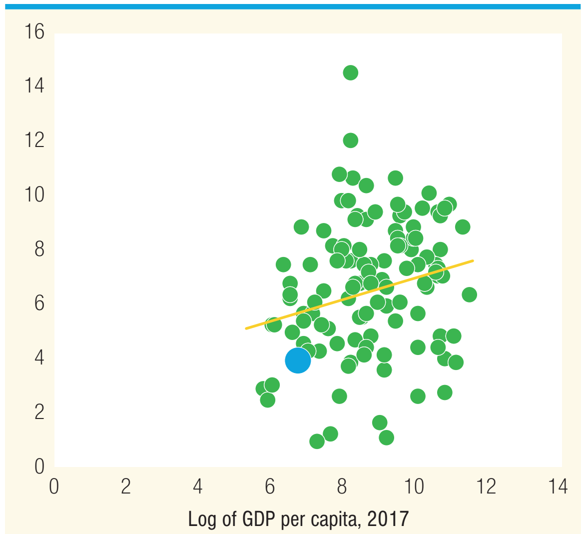
59 For example, the VAT threshold is approximately 10 times average GDP per capita in Thailand and 20 times average GDP per capita in the Philippines.

FIGURE 33 • Historical VAT Performance



Source: WB analysis, data from TRA 2022, ICTD 2020, and WDI 2020.

FIGURE 34 • Income Level and VAT Revenue



Source: WB analysis, data from ICTD 2020 and KPMG 2020.

holistic poverty and equity assessment of fiscal policy would be necessary to estimate the net impact of all taxes and transfers. Other fiscal policy instruments, including conditional cash transfers and public primary education, are far more progressive than VAT.

Tax collection fell at the start of the COVID-19 pandemic. The government largely refrained from imposing strict mobility restrictions, but slowing economic activity still reduced tax revenue. In addition, the government granted tax relief, which contributed to revenue contracting more sharply than GDP. As a result, the tax-to-GDP ratio fell by nearly 0.75 percentage points. A cross-country analysis shows that the recovery of tax revenue is likely to lag the economic recovery, as tax noncompliance tends to worsen during economic crises, and tax morale may be difficult to reestablish.[60]

Indirect Taxes: Key Trends and Assessment of Performance

VAT revenue underperforms in Tanzania relative to comparators, and there is room for improvement. VAT revenue peaked in FY2005/06 at 4.2 percent of GDP (Figure 33). Since 2006, it has accounted for 3.4–3.9 percent of GDP, or an average of approximately 30 percent of TRA Mainland's tax revenue (Figure 33). Trendline analysis indicates that it should expect to generate more than 5 percent of GDP (Figure 34).

Tanzania's 2017 C-efficiency ratio[61] was about 27 percent, well below the SSA average of 37 percent and the LIC average of 39 percent, indicating substantial room for improvement (Figure 35). Poor collection performance and a relatively high VAT rate drive down Tanzania's C-efficiency ratio,[62] while the relatively small share of final consumption in GDP fails to offset this effect.

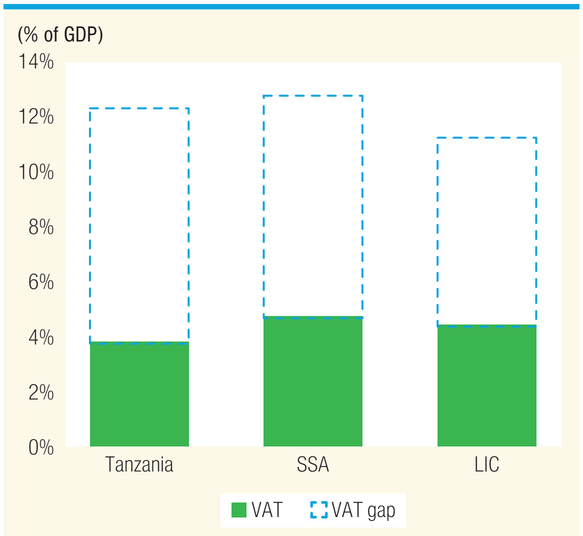
Low VAT revenue collection stems from policy and compliance gaps. Between 2013 and 2017, VAT revenue increased by about 3 percent, much slower than the VAT revenue growth observed in comparable countries between 2013 and 2018. Tanzania has a long list of exemptions in the tax code (food, machinery, education, etc.) and some items are

60 For further analysis and recommendations for addressing noncompliance during economic crisis, see: Brondolo, J. (2009), "Collecting Taxes During an Economic Crisis: Challenges and Policy Options," IMF Staff Position Note.

61 C-efficiency is a popular metric used to evaluate the efficiency of the VAT. It is calculated by dividing VAT revenue as a share of GDP by the product of the statutory rate and household final consumption as a share of GDP. For a full discussion of how the C-efficiency indicator can be used to measure VAT effectiveness, see Keen, M. (2013). The Anatomy of the VAT, IMF Working Paper No. 13/111.

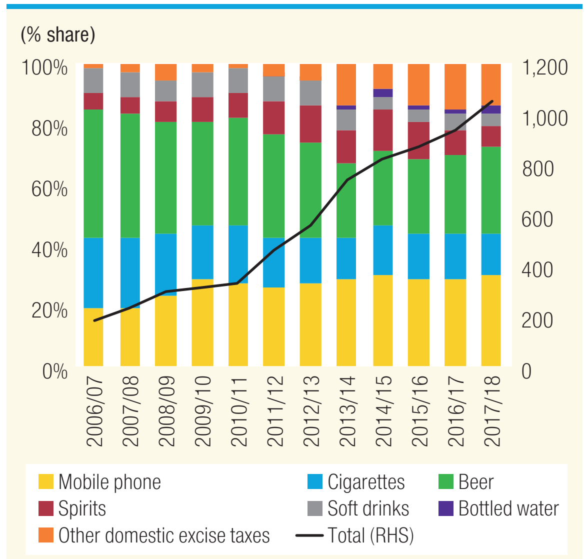
62 C-efficiency ratio measures the efficiency of tax collection.

FIGURE 35 • VAT C-Efficiency, 2017



Note: only countries with data are included, so for SSA (n=16) and for LIC (n=10).
Source: WB analysis, data from TRA 2022, ICTD 2020, and WDI 2020.

FIGURE 36 • The Excise Tax Mix



Source: WB analysis, data from Tanzania Tax Statistics Report 2017/18.

improperly exempted, reducing a substantial amount of GDP.[63] VAT exemptions result in direct revenue foregone when they apply to final consumption, but have more ambiguous impacts when they apply to earlier stages of the value-chain. A long list of VAT exemptions also complicates administration of the VAT, which is associated with higher noncompliance[64] and higher costs of administering the VAT. The country's high VAT threshold narrows the VAT base, increasing progressivity but reducing revenue. Small and medium firms below the threshold pay some embedded VAT on the inputs they purchase from firms above the threshold. However, the effective VAT rate that applies to these smaller firms is typically lower than if they were formally part of the VAT system and so were mandated to charge VAT on their final sales and to credit the VAT on their inputs. Moreover, just as with a long list of exemptions, a high VAT threshold compromises the application of the VAT as it means many transactions are excluded from it, complicating the task of managing VAT compliance. Finally, widespread informality (54 percent of the economy) further diminishes VAT collection.[65] Informality both results in lower VAT potential, due to its impact on firm productivity and growth, and lower VAT collection, due to its association with higher non-compliance.

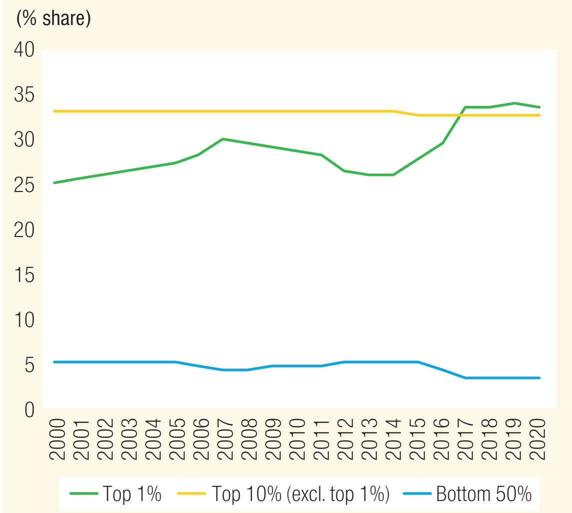
The Tanzanian government imposes excise duties on a variety of items, including alcoholic beverages, tobacco products, natural gas and petroleum products, to advance environmental and public health objectives. The wide array of excise types and tariff structures presents a tradeoff between the targeting of policy goals and the complexity of the tax system. The share of excise tax revenue in total tax revenue fell between 2000 and 2020, and its composition shifted, with the contribution of mobile phones rising while that of tobacco declined. Between 2006 and 2017, total excise revenue grew by an average of 18.3 percent each year, with mobile phones contributing 33.5 percent, beer 27.7 percent,

63 In the 2017-2018 fiscal year, 15 agricultural products were exempted from VAT and reduced tax revenue by over Tsh21 billion or 0.02 percent of GDP. World Bank (2020) Tanzania Public Expenditure Review FY20: Policy Options for Improving Revenue Mobilization.

64 Complexity tends to result in higher rate of noncompliance due either to unintentional mistakes arising from taxpayers' misinterpreting the regulations or to the willful exploitation of complexity to evade taxation.

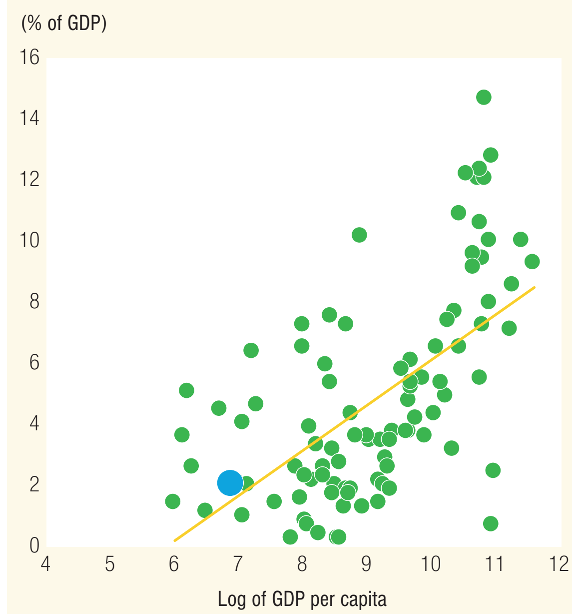
65 See the MIMIC estimation method in Elgin, C., Kose, M. A., Ohnsorge, F., & Yu, S. (2021) Understanding Informality, CAMA Working Paper, 76/2021, September 2021, Centre for Applied Macroeconomic Analysis (CAMA), University of Crawford. Available at: https://cama.crawford.anu.edu.au/sites/default/files/publication/cama_crawford_anu_edu_au/2021-09/76_2021_elgin_kose_ohnsorge_yu.pdf.

FIGURE 37 • Share of Wealth Owned by Households in the Bottom 50%, the Top 10% Excluding the Top 1%, and the Top 1% of the Income Distribution



Source: WB analysis, data from WID 2022.

FIGURE 38 • PIT Revenue and Income Level, 2018



Source:WB analysis, data from TRA 2022, ICTD 2020, and WDI 2020.

and tobacco 12.9 percent (Figure 36). Lower contributions from tobacco excise taxes reflect the failure of specific duties on tobacco products to keep up with growth and inflation. The resulting increased affordability of cigarettes represents a missed opportunity to raise revenue while advancing public health objectives.[66]

Direct Taxes: Key Trends and Performance

Income and wealth inequality are widening. In 2018, Tanzania's Gini coefficient[67] was 40.5, placing it in the bottom quartile of countries that year. Moreover, income inequality had increased significantly since 2000, when the Gini coefficient was 37.3. Wealth inequality is also substantial and increasing, as households in the bottom 50 percent have seen their share of total wealth fall from over 5 percent in 2000 to roughly 4 percent in 2020, while the share of total wealth owned by households in the top 1 percent rose from 25 percent to 34 percent (Figure 37). More effective taxation of income and wealth could enhance fiscal equity.

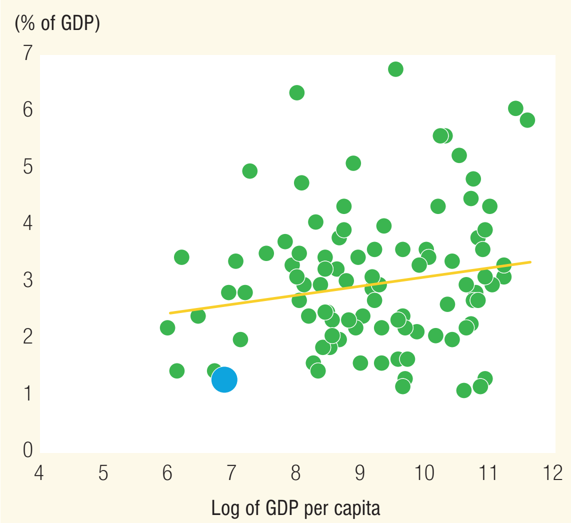
Tanzania collects the total amount of income tax that would be expected given its level of GDP per capita, but PIT revenue is much higher, and CIT revenue is much lower, than in most comparable countries. Income taxes increased their share in Tanzania's total tax revenue from 25 percent in FY2000/01 to over 35 percent in FY2020/21. PIT and CIT are the largest categories of direct taxes, together amounting to roughly 4 percent of GDP. This share is consistent with Tanzania's income level (Figure 38, 39). However, Tanzania's CIT and PIT are less productive[68] than those of its regional and income-group comparators, resulting in lower revenue collection (Figure 40).

66 Tobacco use is one of the most common risk factors for non-communicable diseases (NCDs). The WHO estimated that NCDs accounted for 27 percent of all deaths in Tanzania in 2010.

67 Gini coefficient is a measure of income inequality, and the coefficient is a number between 0 and 1, where 0 corresponds with perfect equality (where everyone has the same income) and 1 correspond with perfect inequality (where one person has all the income and everyone else has zero income).

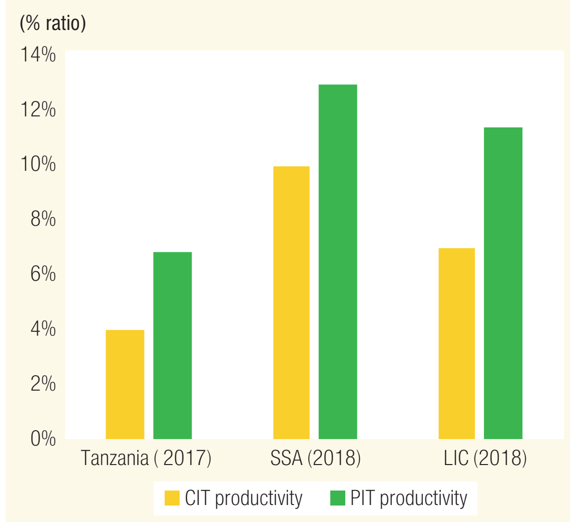
68 Productivity here is defined as collection from a particular tax instrument as a share of GDP divided by the top statutory rate for that tax instrument. For PIT, for example, this would be PIT revenue as a share of GDP divided by the top marginal bracket rate of PIT.

FIGURE 39 • CIT Revenue and Income Level, 2018



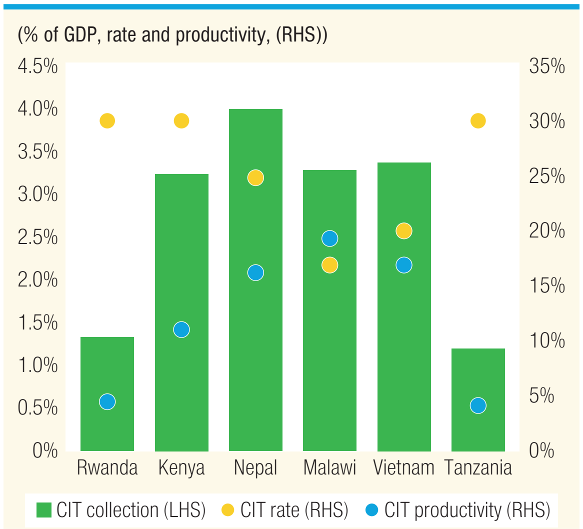
Source: WB analysis, data from ICTD 2020 and KPMG 2020.

FIGURE 40 • CIT and PIT Productivity



Source: WB analysis, data from ICTD 2020 and KPMG 2020.

FIGURE 41 • CIT Collection, Rate and Productivity in Selected Countries, 2018



Source: WB analysis, TRA 2022, ICTD 2020 and Tax Foundation 2021.

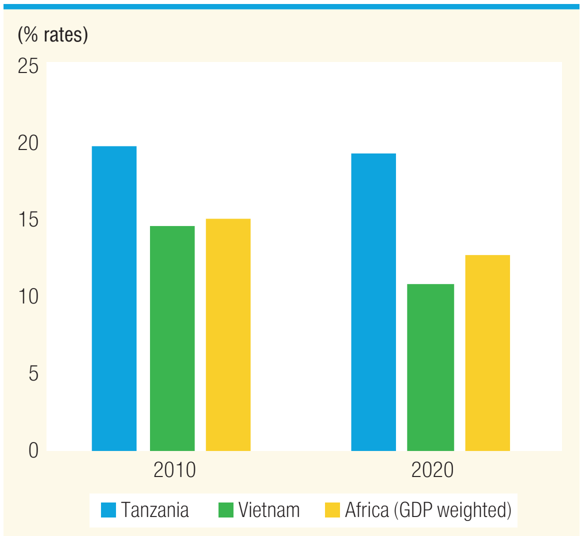
Tanzania's low CIT productivity by regional and peer-country standards may reflect policy and/or compliance gaps. Among five comparator countries, only Rwanda has a comparable level of CIT productivity at 4.4 percent (Figure 41). Tanzania's low CIT productivity is likely driven by compliance gaps, in tax registration, filing, reporting, and payment. An additional policy gap is caused by CIT incentives, including reduced rates and tax holidays or exemptions.[69] These incentives tend to disproportionately advantage some firms, multinational corporations, and high-income households, thereby worsening income inequality and distorting competition among firms.

Business taxation has provided stability for investors, but steps need to be taken to reform international taxation rules to reduce risks from tax avoidance. Tanzania's overall Marginal Effective Tax Rates (METR)[70] fell slightly from 19.8 percent in 2010 to 19.2 percent in 2020, a decline of just 0.6 percentage points (Figure 42), but the broadly stable METR offers a degree of tax certainty to prospective investors. In addition, the difference between the METRs for services and manufacturing is only 1.1 percentage point, far smaller than in peer countries, indicating no substantial bias toward either sector.

69 See: https://taxsummaries.pwc.com/tanzania/corporate/tax-credits-and-incentives.

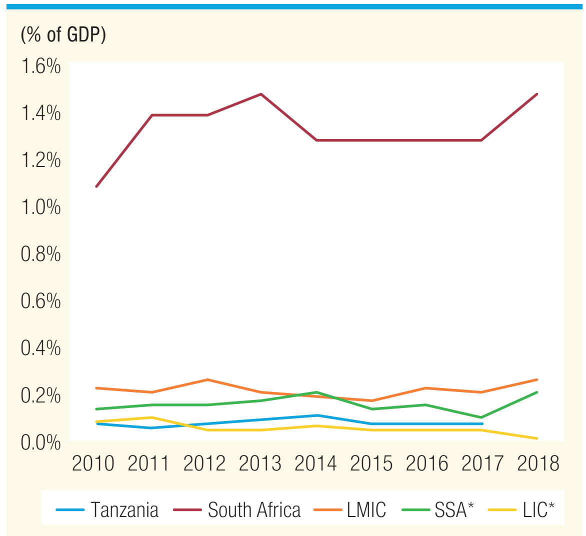
70 See Fullerton, D. (1999) "Marginal Effective Tax Rate." in The Encyclopedia of Taxation and Tax Policy. The METR on capital income is calculated by taking the expected pretax rate of return minus the expected after-tax rate of return on a new marginal investment, divided by the pretax rate of return.

FIGURE 42 • Marginal Effective Tax Rates



Source: WB analysis, data from UNU-WIDER 2020.
Note: These samples are greatly influenced by the sample of countries reporting and should be regarded as indicative rather than absolute.

FIGURE 43 • Property Taxes Revenue, 2010-2018



Source: WB analysis, data from UNU-WIDER 2020.
Note: These samples are greatly influenced by the sample of countries reporting and should be regarded as indicative rather than absolute.

However, Tanzania's international taxation regime is limited, which creates opportunities for tax avoidance that jeopardize tax fairness and result in revenue losses. Tanzania has not signed the Inclusive Framework on Base Erosion and Profit Shifting,[71] which was designed in part to close loopholes in thousands of tax treaties worldwide that have inadvertently facilitated profit shifting by multinationals and other forms of tax avoidance. Research has shown that large, medium, and small firms all engage in tax avoidance in Tanzania.[72] A systematic review of Tanzania's international tax policy in the context of the cross-country experience could inform measures to reduce tax avoidance, increase revenue, and improve overall fairness of business taxes.[73]

The government could significantly increase revenue collection from property taxes and direct taxes. Between 2010 and 2018, revenue from property taxes averaged about 0.1 percent of GDP per year, close to the LIC average and just slightly below the SSA average (Figure 43). Property taxes can be an effective subnational tax instrument due to the fixed location of the taxable property. In addition, the low productivity of PIT and especially CIT undermines the government's revenue position. PIT and CIT productivity gaps disproportionately favor wealthy households and well-connected firms, exacerbating wealth and income inequality.

Revenue Administrator

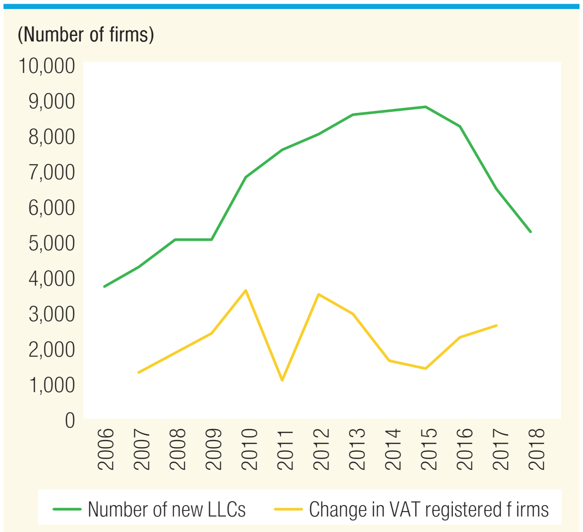
The government has expanded taxpayer registration, but gaps remain. The VAT was introduced in July 1998, but despite its importance as a revenue source, the number of VAT-registered taxpayers and businesses remains low. Certain firms are exempted from VAT registration, including those with turnover below the threshold (currently Tsh200 million in a

71 For a full list of signatories, see: https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf

72 See: https://www.dw.com/en/africas-problem-with-tax-avoidance/a-48401574.

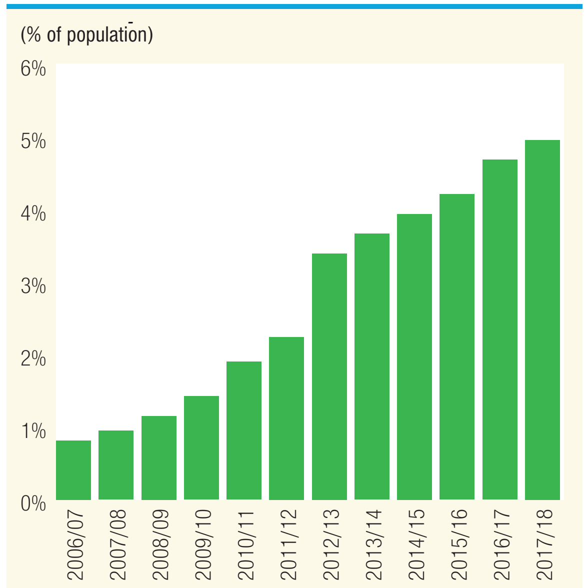
73 Outdated international tax treaties created loopholes in the taxation of multinationals, which allowed them to shift profits offshore to minimize their tax liability. See in Crivelli, E., De Mooj, R. & Keen, M. (2015) Base Erosion, Profit Shifting and Developing Countries, IMF Working Paper 15/118; Dharmapala, D. (2014) What do we know about base erosion and profit shifting? A review of the empirical literature, Coase-Sandor Institute for Law & Economics Working Paper No. 702, 2014; Aizenman, J. & Jinjarak, Y. (2009). Globalisation and Developing Countries – a Shrinking Tax Base?, The Journal of Development Studies, 45:5, 653-671, DOI: 10.1080/00220380802582338; and Griffith, R., Miller, H., & O'Connell, M. (2014) Ownership of intellectual property and corporate taxation, Journal of Public Economics, Vol. 112, April 2014, pg. 12-23.

FIGURE 44 • Limited Liability Corporations and VAT-Registered Firms



Source: WB analysis, data from Tanzania National Bureau of Statistics 2019 and WB Entrepreneurship 2022.

FIGURE 45 • Registered Taxpayers, FY



Source: WB analysis, data from Tanzania National Bureau of Statistics 2019.

12-month period) and those that deal exclusively in VAT-exempt products.[74] In FY2014/15, the Statistical Business Register Survey found that almost half of 154,000 surveyed firms were registered for VAT,[75] though registration rates varied by region.[76] Between 2006 and 2018, an average of just under 6,700 limited liability corporations were formed each year, while the number of VAT-registered companies increased by an average of 2,200 (Figure 44).

The adoption of digital technologies has yielded some success in increasing taxpayer registration. The Electronic Fiscal Device (EFD) was introduced in 2010, though it was not effectively implemented in mainland Tanzania until January 2011.[77] The largest increase in tax revenue in recent years coincided with the expansion of the EFD to include non-VAT-registered businesses (e.g., small-scale traders) in 2013 (Figure 45), but despite the EFD's advantages, the cost of using it is high and must be borne by firms, which promotes informality and other forms of noncompliance, leading to lower-than-expected VAT collection.[78] Nevertheless, increased digitalization and other reforms can help reduce the administrative burden of tax compliance. The authorities have attempted to reduce the burden of paying taxes by simplifying processes and gradually introducing automation. Digital solutions can also yield other potential benefits, such as facilitating more efficient, less expensive communications with taxpayers at scale.[79]

74 As reported in Msangi, S. Y. (2015) Evaluation and Analysis of Value Added Tax (VAT) Compliance: A Case Study of Small and Medium Enterprises in Tanzania [Doctoral Dissertation, Faculty of Business and Law, School of Management, University of Southampton]. Available at: https://eprints.soton.ac.uk/404882/1/Final%2520PhD%2520thesis%2520-%2520Salma%2520Msangi.pdf.

75 National Bureau of Statistics, Ministry of Finance and Planning (2016) Statistical Business Register Report, 2014/15 Tanzania Mainland, The United Republic of Tanzania, Dar es Salaam. Available at: https://www.nbs.go.tz/nbs/takwimu/Br/2014_15_SBR.pdf.

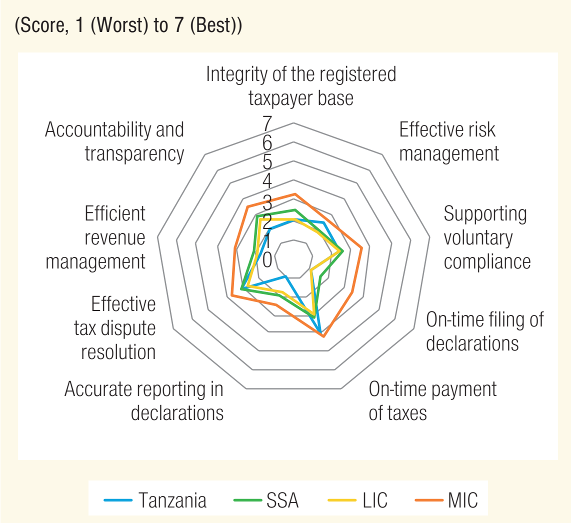
76 See the full discussion in Msangi (2015).

77 For more information, see Fjeldstad, O.H. et al (2018) The Customer is King: Evidence on VAT Compliance in Tanzania, ICTD Working Paper 83, Institute of Development Studies. Available at: https://opendocs.ids.ac.uk/opendocs/bitstream/handle/20.500.12413/14093/ICTD_WP83.pdf?sequence=1&isAllowed=y.

78 For a review of interview responses from SME taxpayers and TRA officials, please see Appendix 2 in Msangi (2015).

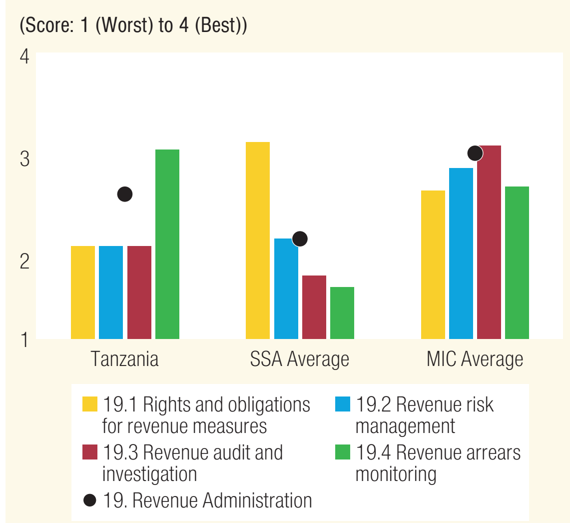
79 See, e.g., Kira, A. R. (2017) An evaluation of governments' initiatives in enhancing small taxpayers' voluntary tax compliance in developing countries, International Journal of Academic Research in Accounting, Finance and Management Sciences, Vol 7(1), pg. 253-267.

FIGURE 46 • TADAT Scores, Tanzania and Comparators, 2018



Source: WB analysis, TADAT (2018).

FIGURE 47 • PEFA Indicator 19: Revenue Administration, 2020



Source: WB analysis, data from PEFA (2020).

Weaknesses in revenue administration distort tax policy and encourage informality. A 2014 reform effort simplified the VAT system and increased the turnover threshold from Tsh40 million to Tsh100 million. The reform narrowed the VAT base to shrink the VAT register, which had proven difficult for the TRA to manage, undermining compliance monitoring and enforcement. Despite the higher VAT threshold, ongoing challenges with VAT refunds highlight unresolved weaknesses in revenue administration. Strengthening VAT administration will support private-sector liquidity and boost revenue collection by closing compliance gaps, while also enabling the TRA to broaden VAT collection and support business formalization by lowering the VAT threshold.

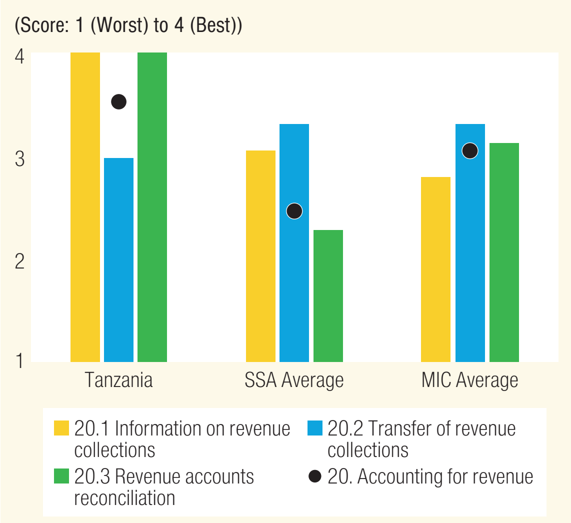
Strengthening compliance management is critical to enhance revenue administration. Tanzania scores poorly on the Tax Administration Diagnostic Assessment Tool (TADAT), with the weakest areas being 'On-time Filing of Declarations', 'Accurate Reporting in Declarations', 'Efficient Revenue Management', and 'Accountability and Transparency' (Figure 46). The accuracy and timeliness of tax-filing declarations could be substantially improved, as Tanzania currently lags many LICs in both areas. The weak integrity of the registered taxpayer base further narrows the distribution of the tax burden while undermining efforts to analyze taxpayer information.

If the TRA is not able to effectively leverage third-party data to cross-check the declarations of existing tax filers, compliance gaps will likely remain substantial, and addressing them may require a set of complementary reforms. The ongoing increase in e-filing will likely help Tanzania lower the cost of tax compliance and improve compliance-risk management, but enabling reforms—including an effective registration system, third-party data verification, and a comprehensive compliance-risk management strategy supported by major investments in technology—are still pending.[80]

The TRA's capacity for risk management and audit investigation hinges on the integrity of the taxpayer base. In the 2022 PEFA assessment, Tanzania performed relatively well on measures of revenue accounting but poorly on revenue administration, including in the critical areas of risk management and auditing (Figure 47).

80 Tanzania's positive experience with using digital solutions to strengthen property tax administration shows that successful reforms in this area at the national level are possible. See: McCluskey, W. & Huang, C.Y., (2019) The Role of ICT in Property Tax Administration: Lessons from Tanzania, CMI Brief 6, Chr. Michelsen Institute (CMI). Available at: https://www.cmi.no/publications/6880-the-role-of-ict-in-property-tax-administration-lessons-from-tanzania

FIGURE 48 • PEFA Indicator 20: Accounting for Revenue, 2020



Source: WB analysis, data from PEFA (2020).

These findings indicate that the TRA has limited ability to identify firms that are less likely to be complying with registration, filing, reporting, or payment requirements and to prioritize audits accordingly. The TRA's risk-management and auditing capabilities can be enhanced in several ways, including through hiring and training more specialized staff. The success of these reforms will require fundamental improvements in the integrity of the taxpayer base.

The Distributional Impact of Fiscal Policy

The Distributional Effects of Taxation and Public Spending

This section presents the results of a fiscal-incidence analysis for mainland Tanzania based on the CEQ methodology. The CEQ focuses on three questions: (i) which types of households pay taxes, (ii) who receives direct and indirect transfers, including utility subsidies and access to publicly funded services such as education and healthcare, and (iii) how fiscal policy affects household incomes, poverty, and inequality. Collectively, this analysis looks at what is paid and what is received without assessing how individuals and households change behavior in response to taxes and public spending. It similarly does not capture and consider any indirect impacts that occur throughout an economy due to fiscal policy. Despite these limitations, the effects calculated with this method are considered a reasonable approximation of the short-run welfare impact.

The analysis uses data from the FY2017/18 Household Budget Survey, as well as administrative records on taxes and social spending. It assesses the extent to which fiscal policy redistributes income in Tanzania, as well as the government's scope to accelerate poverty reduction through changes in taxation and social spending while still respecting the limits of fiscal prudence. Overall, most taxes appear to be progressive, but the combined effect of taxes and transfers slightly increases poverty. It should however be acknowledged that redistribution is not the only function of fiscal policy. On top of realizing social goals, fiscal policy seeks to create conditions ideal for growth and a stable macroeconomic environment.

The policy design, institutional framework, and administrative processes that underpin Tanzania's fiscal system are broadly similar to those of many other developing countries. The main components of government revenues are direct and indirect taxes, supplemented by domestic and external loans and grants. In FY2017/18, central government revenue (excluding grants) totaled Tsh17.4 trillion, or 13.5 percent of GDP, just below the regional average (Annex 6). The combined revenue of the central and local governments (including grants) totaled Tsh18.9 trillion, or 15.0 percent of GDP.[81] Revenue from indirect taxes amounts to 7.5 percent of GDP, versus 4.2 percent for direct taxes. Despite Tanzania's relatively small formal sector, the government collects significant revenue from taxes on formal employment and entrepreneurship through the PIT, which includes PAYE and the Presumptive Tax levied on earned income.[82] VAT is levied at a statutory rate of 18 percent on goods and services and accounts for about

[81] The average for 16 regional countries with a recent CEQ analysis is 18.6 percent.

[82] Presumptive tax is typically an income tax based on the accounting records of small businesses.

46 percent of total indirect tax revenue, while excise taxes[83] and import duties contribute an additional 23 and 18 percent, respectively. Indirect taxes may have important effects on poverty and inequality as they are taxes on consumption and lower-income households spend a greater share of their income on consumption than higher-income households do. Overall, the total direct and indirect taxes (included in this analysis) represent approximately 73 percent of total government tax revenues in FY2017/18, while total social expenditure covered represents more than 35 percent of total expenditure.[84]

Government spending totaled Tsh20.5 trillion in FY2017/18, equivalent to 16 percent of GDP. This level is low by international standards but in line with the average for other developing countries in the region. A large share of government spending is devoted to providing public services such as healthcare, education, and national defense, as well as covering the recurrent costs associated with the electricity supply, road maintenance, debt service, etc. About one-third of total government spending is devoted to health, education, and social protection (Annex 7). While recurrent spending substantially exceeds capital investment, expenditures have shifted toward the latter in recent years. However, rising levels of spending on major development projects entail a tradeoff with expanded service delivery.

The Tanzanian government uses two official national poverty lines. The basic-needs line, based on the HBS 2017/18, was set at Tsh49,320 per adult equivalent per month, or about Tsh1,620 (US$0.70) per adult equivalent per day, which equals US$1.35 per capita per day in 2011 purchasing power parity (PPP) terms. The food-poverty line is set at Tsh33,748 per adult equivalent per month, or about US$0.92 per capita per day in PPP terms. The poverty gap is estimated as the consumption shortfall from the basic-needs poverty line as a share of the same poverty line. In the CEQ analysis, values for these poverty indicators are estimated using six different definitions of income (Table 4).[85]

The CEQ methodology assesses the distributional impact of taxes, transfers, and subsidies across income groups in Tanzania in 2020 based on household-level data and administrative records on taxes and social spending. The CEQ methodology reveals household incomes before and after fiscal interventions and shows how taxes, social contributions, subsidies, and public spending are allocated across households. As a result, it is possible to compare income-based measures of wellbeing before and after taxes and public transfers. The CEQ includes several discrete income concepts, and various fiscal instruments (i.e., taxes and transfers) are added or subtracted to move from one concept to another (Figure 46). Whenever possible, taxes and transfers are allocated to households using information obtained through the HBS. When such data are not available, imputation, simulation, or alternative surveys may be used.

The CEQ assessment shows that all three poverty indicators worsen when direct and indirect taxes are taken into account, but larger changes are observed at the higher poverty line. The poverty headcount index increases by 1.1 percentage points and 0.1 percentage point with the national basic-needs poverty line and food-poverty line, respectively. Furthermore, the combination of direct transfers and direct taxes and contributions has only a modest impact on poverty using the national poverty lines.

83 Excise taxes are applied on a specific or ad valorem basis to a list of specific products (e.g., alcoholic beverages, cigarettes, gasoline, etc.) and services (electronic communication services, financial services).

84 On the tax side, the analysis did not include the CIT or PIT due to the limitations of the data and methodology. On the expenditure side, not all details about the coverage and total expenditure in cash transfers and indirect (in-kind) transfers are available from the household survey data, and the estimates used here are mainly based on social protection expenditures (e.g., cash transfers) and public expenditures on health and education.

85 The CEQ methodology described in Lustig (2018) was used to assess the distributional impact of taxes, transfers, and subsidies across income groups in Tanzania in 2020 based on household-level data and administrative records on taxes and social spending. Figure 49 presents the main CEQ income concepts and what fiscal instruments (i.e., taxes and transfers) need to be added or subtracted to move from one concept to another.

TABLE 4 • Poverty Indicators Across CEQ Income Concepts

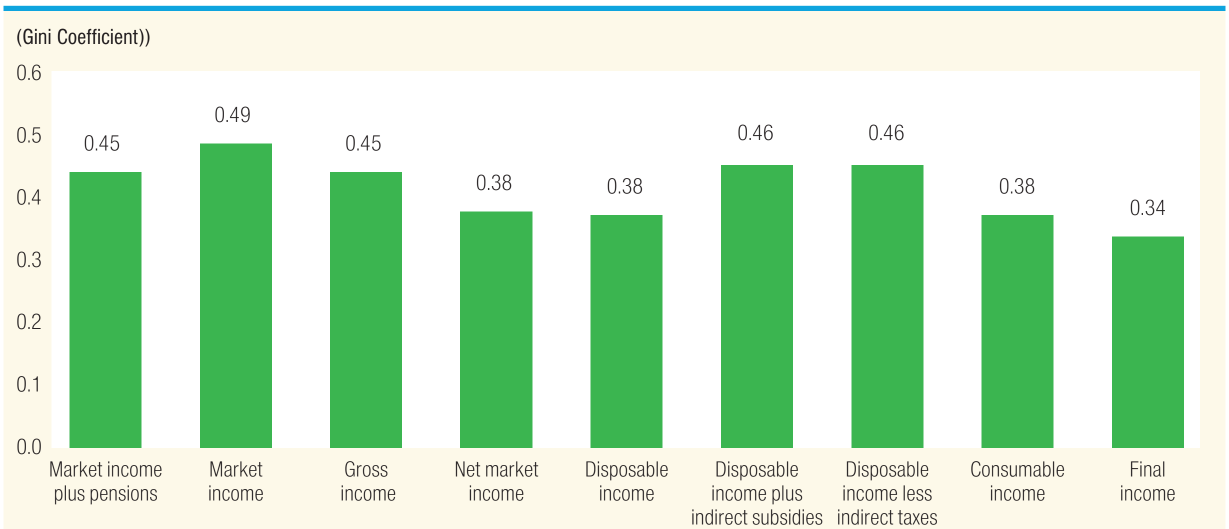
Item	Amount in FY2017/18 (Tsh Millions)	Share of Tax Revenue (%)	Share of GDP (%)	Included in Analysis (Yes/No)
Total Central Government Revenue (including LGAs) & Grants	18,875,535		14.6	
Central government revenue (excluding grants)	17,403,388		13.5	
Tax revenue	15,120,902	100	11.7	
Direct taxes, *of which*:	5,431,192	36	4.2	
Personal income tax (Presumptive Tax)	213,418	1	0.2	No
Corporate income tax	1,238,076	8	1	No
Payroll tax (PAYE)	2,344,699	16	1.8	Yes
Property taxes (Rental Tax)	63,764	0	0.1	No
Skills & Development Levy	282,840	2	0.2	Yes
Indirect Taxes, of which:	9,689,710	64	7.5	
VAT	4,476,646	30	3.5	Yes
Excise Taxes	2,200,214	15	1.7	Yes
Import Duties	1,735,643	11	1.3	Yes
Nontax revenue	99,630	1	0.1	No
Grants	813,483	5	0.6	No

Overall, fiscal policy reduces inequality. The Gini coefficient falls from 0.45 for market income plus pensions to 0.34 for final income (Figure 49). Unlike the impact on poverty, this effect is consistent across income concepts.

The Progressivity and Marginal Contribution of Each Tax and Transfer

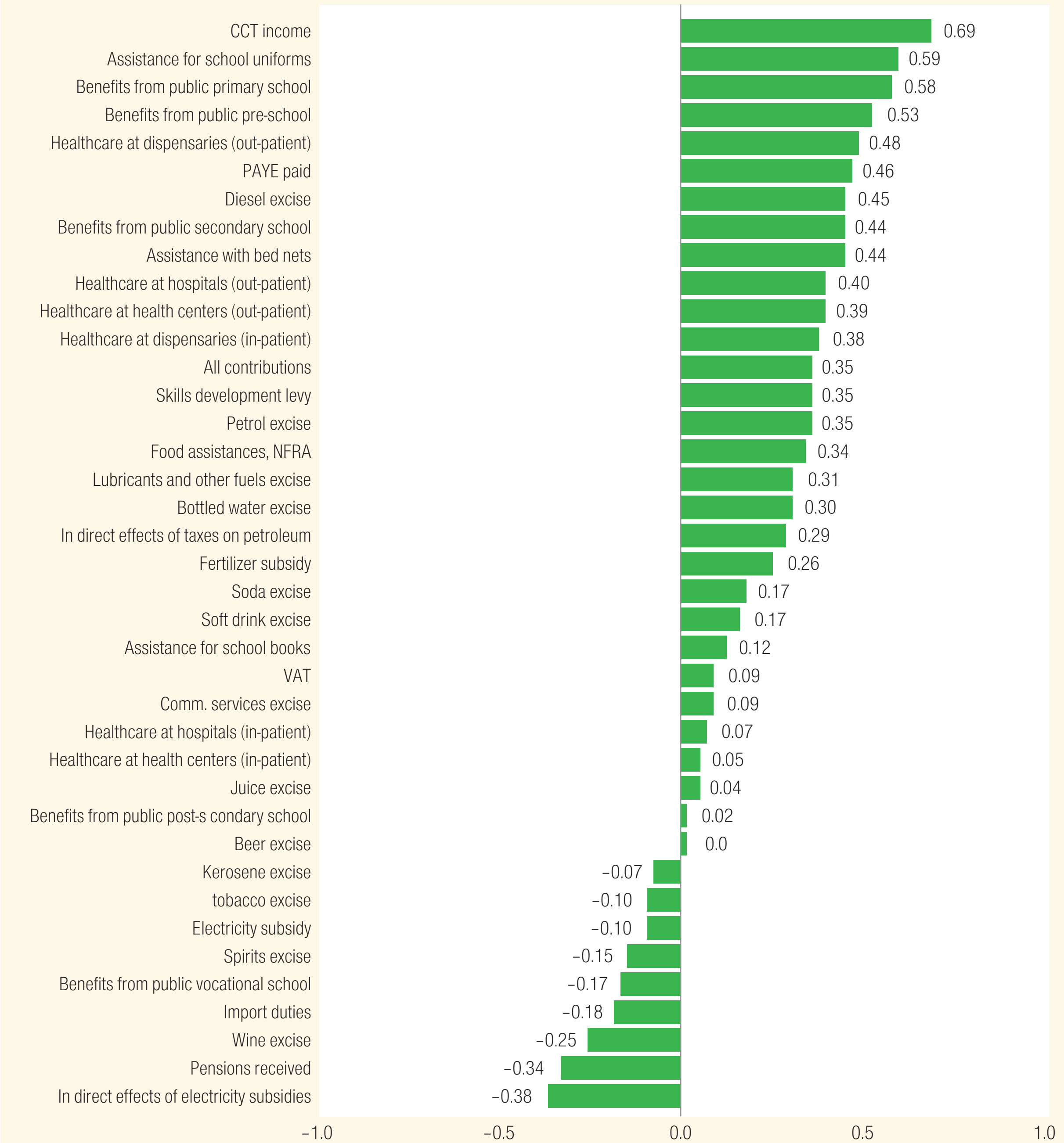
An analysis of the distributional effects of each fiscal instrument reveals that conditional cash

FIGURE 49 • Inequality Indicators across CEQ Income Concepts



Source: NBS HBS 2017/18 and WB staff estimates.

FIGURE 50 • Kakwani Index for Individual Taxes and Expenditures Relative to Market Income Plus



Source: NBS HBS 2017/18 and WB staff estimates.

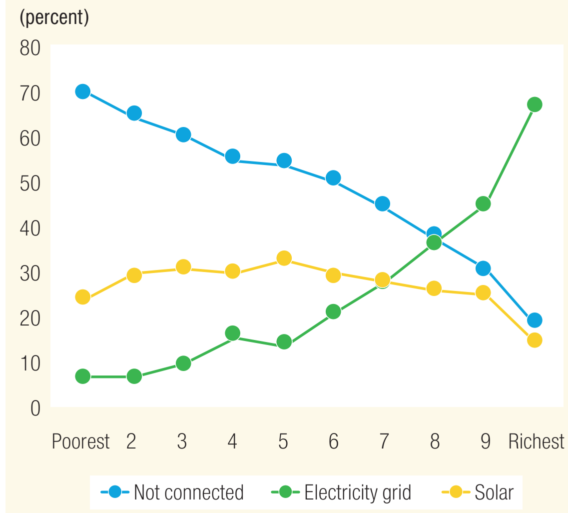
transfers (CCTs) are the most progressive; taxes appear to be progressive; while electricity subsidies are deeply regressive. The Kakwani index[86] reveals the relative progressivity of different fiscal instruments (Figure 50). The high progressivity of CCTs is expected, as the program explicitly targets

[86] The Kakwani index is a measure of the progressivity of a given social intervention. It is equal to the difference in the Gini index for incomes before and after the intervention. Theoretically, the Kakwani index can vary between −1 to 1, with larger index values indicating more progressive social interventions.

poor households. Other expenditures that disproportionally benefit poor households include assistance for school uniforms and in-kind benefits such as public primary school, public preschool, and health-care provided at outpatient dispensaries. In addition, spending on public vocational schools appears to be regressive, while spending on all other forms of post-secondary public education is slightly progressive. At 0.09, the Kakwani index for VAT is also progressive.

Taxes on formal workers, such as PAYE and the Skills & Development Levy, are very progressive, as formal workers tend to have higher incomes than their informal counterparts. Several excise taxes are regressive, including those on wine, spirits, tobacco, and kerosene, but these taxes have specific objectives other than fiscal equity. Electricity subsidies are steeply regressive because only households in the upper end of income distribution are connected to the electricity grid (Figure 51).[87]

FIGURE 51 • Main Sources of Household Power by Welfare Decile in Mainland Tanzania



Source: NBS HBS 2017/18.

The Findings of the CEQ Analysis in Historical and International Context

The key finding from the CEQ analysis is that most taxes appear to be progressive. While the combined effect of taxes and transfers also reduce inequality, they slightly increase poverty because the indirect taxes that account for a large share of revenue are taxes on consumption, and lower-income households spend a larger share of their income on consumption. The size of the effect of fiscal policy on poverty is smaller than that observed in FY2011/12, which may indicate that fiscal policy is becoming more pro-poor over time.

The progressivity of Tanzanian fiscal policy has remained broadly unchanged since the previous CEQ analysis. Most of the Kakwani index scores for taxes and expenditure programs are close to those calculated by Younger et al. (2016) based on data from the 2011/12 HBS. Moreover, a comparison with 18 previous CEQ analyses reveals that the combined effect of taxes and transfers in Tanzania reduces inequality to a greater extent than in most comparable countries. The sample group includes South Africa, Ghana, Kenya, and the average of 17 CEQs previously completed for LMICs. Despite the country's relatively low levels of pre-fiscal inequality, Tanzania's fiscal policy is one of the most progressive among comparators (Figure 53).[88]

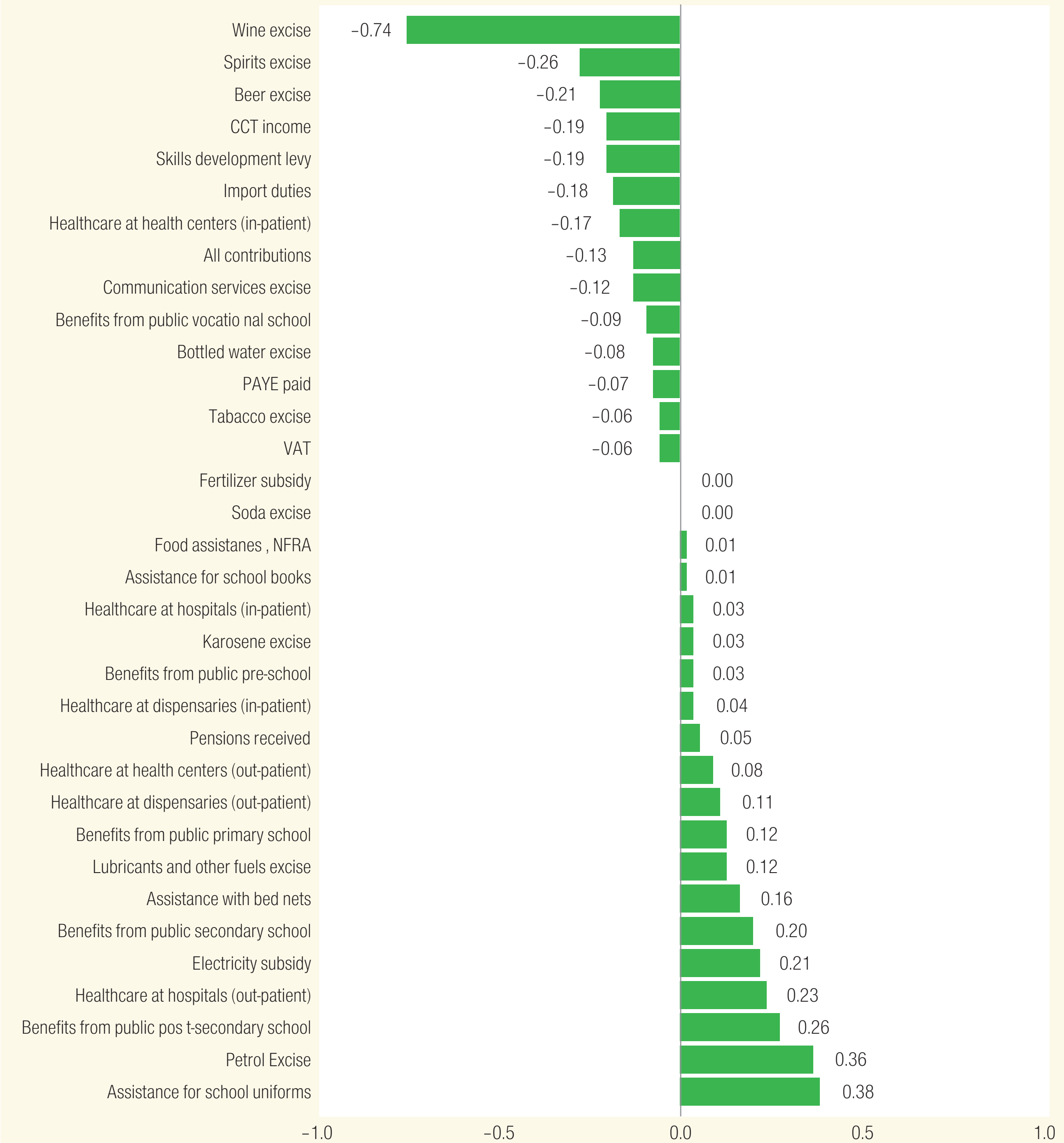
Tanzania' redistributive fiscal policies increase the poverty rate at the international poverty line by about 2 percentage points. This occurs because the regressive effect of indirect taxes is not fully offset by pro-poor cash transfers and subsidies. Unlike the reduction in inequality, the increase in poverty in Tanzania is one of the most significant among comparator countries, exceeded only by Kenya (Figure 54). It should be noted that almost half of the population in Tanzania lives under this poverty line, and this measure is less relevant in the national context.[89]

87 This finding was also highlighted in the previous CEQ assessment for Tanzania (Younger et al.,2016), which presented a policy simulation showing that eliminating electricity subsidies would provide opportunities to strengthen the government's budgetary position while reducing poverty and inequality.

88 Comparability between these studies can differ because of the share of the fiscal system included in the analysis and differences in methodology, so these results need to be taken only as suggestive.

89 The size of the effect in 2017/18 was smaller than that observed in 2011/12 (Younger et al. 2016), which may indicate that fiscal policy is becoming more pro-poor over time.

FIGURE 52 • Difference in the Progressivity of Fiscal Interventions between FY2011/12 and FY2017/18

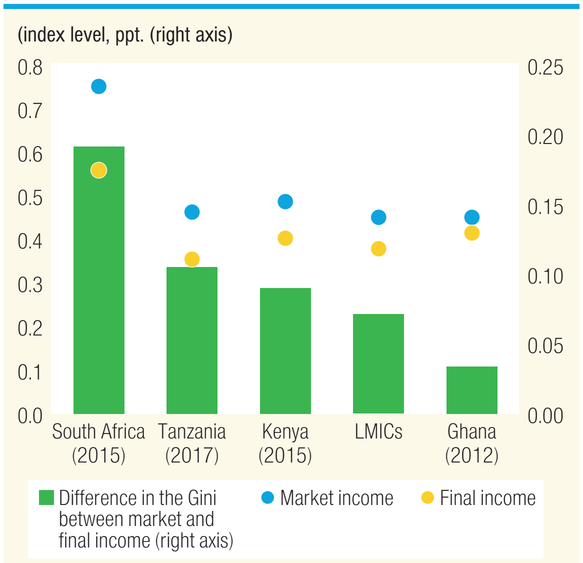


Source: NBS HBS 2017/18 and WB staff estimates.

The CEQ simulation[90] shows that broadening the VAT base could slightly increase the poverty rate while reducing inequality. The marginal increase in the poverty rate is expected, as the scenario simulates an expansion of tax liability without considering how the resulting revenue would be spent. However, the simulated increase in the poverty rate is very small at less than 1 percentage point (Table 5). Meanwhile, the (minor) reduction in the Gini coefficient

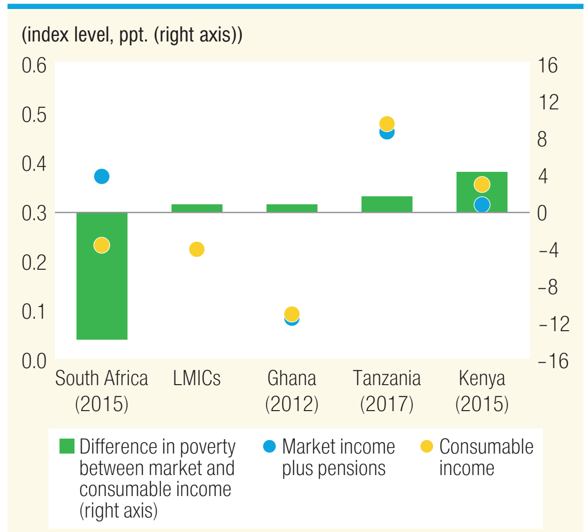
90 A fiscal simulation tool currently being prepared by the authors of this chapter could allow for additional policy simulations, such as the removal of electricity subsidies or an increase in social transfers.

FIGURE 53 • The Redistribution Impact of Fiscal Policy, Tanzania and Comparators



Source: NBS HBS 2017/18, CEQ Data Center on Fiscal Redistribution, 2021, and WB staff estimates.

FIGURE 54 • Poverty Headcount at Market Income and Consumable Income, Tanzania and Comparators



Source: NBS HBS 2017/18, CEQ Data Center on Fiscal Redistribution, 2021, and WB staff estimates.

suggests that broadening the VAT base would increase the progressivity of tax policy.[91] Further analysis could simulate how the increase in VAT revenue could be used to offset the impact on poverty and further improve fiscal equity. Based on the findings of this analysis, channeling a share of the revenue through the existing CCT program would likely advance both objectives, as the program is among the most progressive and pro-poor elements of Tanzania's fiscal policy.

Implementing a standard VAT rate for water and petroleum products would be progressive in terms of its impact on the income distribution, even if it slightly increases poverty. The resulting revenue could be used to finance poverty-reducing expenditures. Based on the CEQ analysis, dedicating a portion of the increase in VAT revenue to augment the funding of the CCT program would likely have a highly positive impact both on poverty and inequality.

[91] The simulation accounts for the indirect effects of VAT only in the case of petroleum.

TABLE 5 • Simulated Results of Broadening the VAT

	Poverty line (Tsh per month)		
	49,320*		33,748**
	Headcount index	Poverty gap	Headcount index
Market Income plus Pensions	**26.3**	**6.3**	**8.4**
+ direct transfers (cash, and near-cash such as school uniform and book subsidies)	25.3	5.9	7.5
– direct taxes and contributions (such as personal income tax)	26.3	6.1	7.9
+ indirect subsidies – indirect taxes –>			
Consumable Income	**27.4**	**6.4**	**8.5**

ANNEX 1
CORE MACROECONOMIC DATA SOURCES FOR THE REPORT

Sector	Series	Latest Data Point	Source	Measurement Year
Tanzania Mainland				
Real	GDP at constant 2015 prices by activity and by demand, MFO Spring Survey 2023, monthly tourist arrivals at Tanzania Mainland by Nationality, monthly electricity and quarterly cement production data.	GDP data: Q1 2023 and 2022 High frequency data: June 2023 for tourist arrivals and Q1 2023 for other data	National Bureau of Statistics, Bank of Tanzania, Haver, Integrated Labor Force Survey, Welfare Monitoring Survey, World Bank staff estimates.	Calendar Year
Inflation	Inflation (headline, food, non–food, core, energy), credit to selected economic activities.	June 2023	National Bureau of Statistics, Bank of Tanzania, World Bank staff estimates.	Calendar Year
Monetary	M3, reserve money, broad money and private sector credit	June 2023	Bank of Tanzania	Calendar Year
Fiscal	Revenues, expenditures, grants, financing, expenditure arrears	FY2022/23	Ministry of Finance and Planning, Bank of Tanzania	Fiscal Year
Debt	PPG total, external and domestic	FY2021/22	Bank of Tanzania, United Republic of Tanzania, Country Report No. 23/153, April 2023, International Monetary Fund.	Fiscal Year
External	BoP, exports and imports of goods and services.	BoP: Q4 2022 Trade data: 5M-2023	Bank of Tanzania and National Bureau of Statistics.	Calendar Year
Outlook	Global PMI Index, Global Sentix Index, Commodity Price Indexes,	July 2023	World Bank staff estimates, Bloomberg, Haver, Goldman Sachs Financial condition indices, JP Morgan Global Purchasing Manger's Indexes, World Bank Data	Calendar Year

(continued on next page)

(continued)

Sector	Series	Latest Data Point	Source	Measurement Year
Zanzibar				
Real	GDP at constant 2015 prices by activity, tourist arrivals	GDP data: Q4 2022 Tourist data: June 2023	Bank of Tanzania and Office of the Chief Government Statistician (OCGS) – Zanzibar	Calendar Year
Inflation	Inflation (headline, food, non–food)	June 2023	Bank of Tanzania	Calendar Year
Current account	Merchandise trade data	June 2023	Bank of Tanzania	Calendar Year
Fiscal	Revenues, expenditures, grants, financing	H1-FY2022/23	Bank of Tanzania and OCGS – Zanzibar	Fiscal Year

ANNEX 2
ZANZIBAR RECENT ECONOMIC SYNOPSIS

Zanzibar Recent Economic Development

Overview

Zanzibar is a **semi-autonomous** province that united with Tanzania Mainland to form the United Republic of Tanzania (URT)

Its population was estimated at around **1.9 million** (or **3.1 percent** of URT's total population) in 2021 and its real GDP was **2.4 percent** of URT's in 2022

Zanzibar is an island economy driven by the **services sector** and **heavily dependent on imports**. The services industry takes the lion's share, representing 52 percent of the total GDP, followed by agriculture and industry each contributing around 20 percent. **Tourists** in Zanzibar make up over 1/4 of URT's total tourist visitors

Zanzibar's economy continues to grow albeit moderately

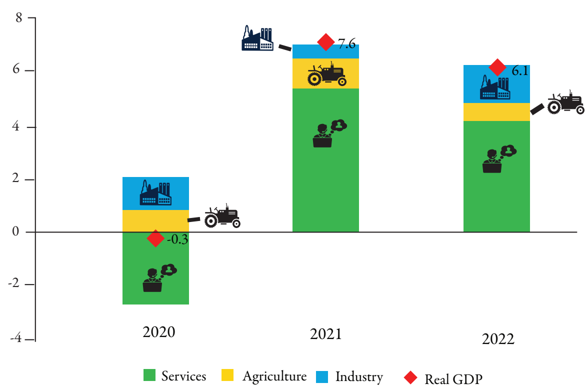
Economic growth

6.1% 2022

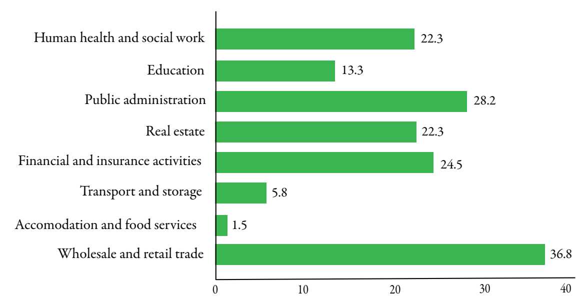
7.6% 2021

The **services sector** has **exceeded** pre-pandemic performance by over **13 percent**

Real GDP Growth (% change, y/y)



Growth of Key Services Subsectors vis-à-vis 2019 (% change, y/y)



Almost 2/3 of the GDP growth was driven by the **services sector** followed by industry at 23 percent in 2022

Most of the key subsectors have **bounced back** to their pre-pandemic levels

Tourism remains the primary driver for growth and jobs

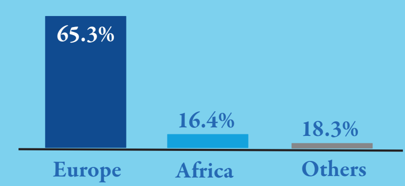
0.5 million

In 2022 Zanzibar attracted **0.5 million** tourist arrivals (1.9% higher than 2021)

47%

In H1-2023, the number of tourist arrivals soared by over **47 percent** (y/y) from H1-2022

Tourist Arrivals by Continents, H1-2023



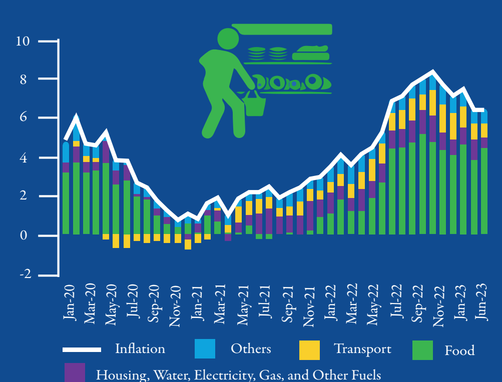
Headline inflation has picked up significantly

5.1%

Headline inflation stood at **5.1 percent** in 2022 compared to **1.7 percent** in 2021

During H1-2023, headline inflation rose to **7.3 percent** vis-à-vis 3.5 percent in H1-2022

Zanzibar Headline Inflation Trend (% change, y/y)



Food inflation was **10.7 percent** during H1-2023 but 2.7 percent during the corresponding period one year ago

This reflects the escalating prices of...

Maize +66% (y/y)

Beans +54% (y/y)

Rice +52% (y/y)

61%

Food and Non-alcoholic Bevarages remained the leading driving force of the inflation, contributing almost **61 percent** to the overall increase **followed by...**

Transport +15%

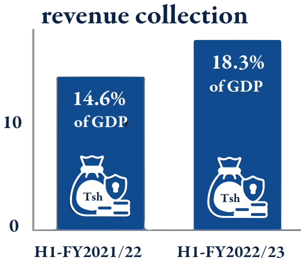
Water, housing & electricity +13%

Overall balance remains modest

Overall balance remained the same

2.8% of GDP H1-FY2022/23 = 2.8% of GDP H1-FY2021/22

Improved tax revenue collection

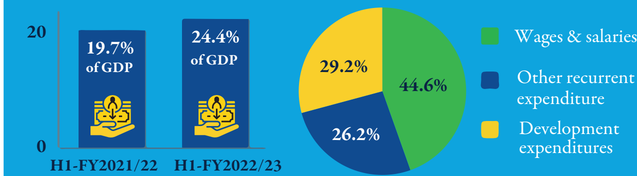


Non tax revenue as a percentage of GDP decline by

0.5%

FEES

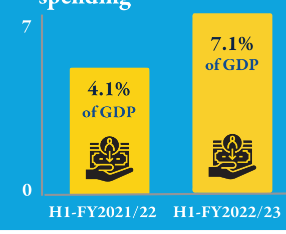
Total spending picked up



Tsh

This is driven by **higher wages and salaries payments** by **2.2** percent of GDP...

...and rising **development spending**

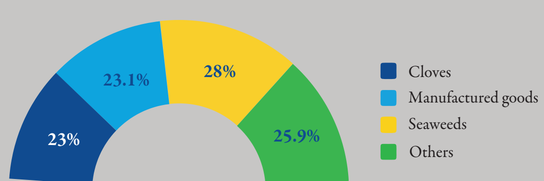


Merchandise trade deficit widened because of rising imports

Trade balance of goods registered a deficit of **US$226.5 million** in **H1-2023** compared to US$184.8 million in H1-2022

40.5% During H1-2023, exports decreased by **40.5 percent**

Major Export for H1-2023



This growth in exports due to decreases in...

-50.7% y/y — Manufactured goods

-70.4% y/y — Cloves

The **volume effects** dominated the price effects for **cloves** while the **reverse** is true for **seaweeds**

Growth in imports substantially outpaced the growth in exports

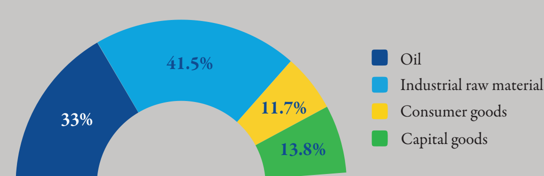
37.1% H1-2022

6.2% H1-2023

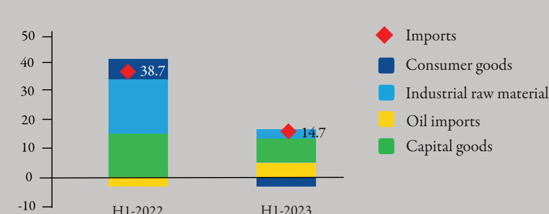
3 largest import partners

UAE	China	India
46%	11%	8%

Major imports for H1-2023



Goods Imports Growth (% change, y/y)



The imports growth is driven by **oil and capital goods** imports

Source: Bank of Tanzania, OCGS and World Bank staff estimates

ANNEX 3

SUMMARY OF SPECIAL FOCUSES FROM THE LATEST TANZANIA ECONOMIC UPDATES

Fall 2022 TEU-18: “Clean Water, Bright Future: The Transformative Impact of Investing in WASH”

The provision of near-universal access to water, sanitation and hygiene (WASH) services can drastically improve multiple facets of Tanzania’s population. Although there has been progress towards increasing access to WASH services, achieving the Sustainable Development Goals of the UN will require greater prioritization. The Water Sector Development Program (WSDP) has made significant progress; however, the current WSDP-3 stands to have the largest impact towards providing near-universal access to WASH services yet. Achieving the goals of WSDP-3 would mitigate the high volume of yearly deaths due to inadequate WASH services, would significantly reduce economic loss, and would bring substantial increases in job creation and workforce productivity. With a majority of the population without adequate WASH services, the provision of near-universal access will be crucial for the development of Tanzania.

Spring 2022 TEU-17: “Accelerating Growth by Expanding Women’s Economic Opportunities and Ensuring Equitable Access to Assets”

Over the last two decades, a growing share of Tanzanian women have entered salaried employment, and an increase in the female labor-force participation rate (LFPR) has accelerated Tanzania’s transition to lower-middle-income country. However, women still face multiple challenges, including persistent gender gaps in wage rates and agricultural productivity. Despite recent progress, women are less likely to own a home, exercise secure land rights, hold a bank account, or have access to finance. These gender disparities prevent women from maximizing their contribution to Tanzania’s economic development.

Fall 2021 TEU-16: “The Recovery Resilience, and Transformation of Tanzania’s Tourism Sector”

Tanzania’s abundant nature and rich cultural resources are a considerable economic opportunity. The tourism sector can support the government's broader development objectives by: (i) creating jobs, both directly and through backward linkages to other sectors; (ii) generating foreign-exchange earnings; (iii) providing revenue to support the preservation and maintenance of natural and cultural heritage; and (iv) expanding the tax base to finance development expenditures and poverty-reduction efforts. However, the COVID-19 crisis severely impacted Tanzania's tourism sector as the disruption of global travel and tourism activity resulted in job losses and business closures. This prompted policymakers, investors, firms, and development practitioners to reconsider tourism's underlying sustainability and value proposition.

Spring 2021 TEU-15: "Raising the Bar: Achieving Tanzania's Development Vision"

Following two decades of sustained growth, Tanzania reached an important milestone in July 2020, when it formally graduated from low-income country (LIC) to lower-middle-income country (LMIC) status. While reaching LMIC status is a laudable achievement, Tanzania's larger development agenda remains unfinished. The Tanzania Development Vision (TDV) 2025 envisages Tanzania as a middle- income country with well-developed human capital, an ample supply of high-quality livelihood opportunities, and broad-based gains in living standards. Achieving this will require an annual GDP growth rate of 8 percent, the creation of 8 million jobs, and sustained improvements in social indicators. While Tanzania aspires to middle-income status, in the near term it will need to maintain its LMIC status in a context of deep and lasting external shocks. This special focus further frames three pillars reflect both the lessons of the international experience and Tanzania's unique circumstances and form the basis for an actionable policy agenda to achieve the goals of the TDV 2025.

Fall 2020 TEU-14: "The Potential of the Digital Economy"

The digital economy is growing quickly globally, and it can support the delivery of stronger policy responses and help contain the spread of the virus. However, expanding the digital economy depends both on the interaction of digital platforms and on legislation. Both governments and firms should contribute to driving trust and transparency online. This Special Focus gives a number of recommendations as well as interventions that the Government of Tanzania could consider if the digital economy is to rapidly expand, and to respond effectively to the COVID-19 pandemic.

ANNEX 4
COMPOSITION OF GOVERNMENT SUBSIDIES BY PROJECT, TSH, FY2021/22

Composition of Government Subsidies by Project, Tsh, FY 2022/21	Approved	Actual
0000	130,552,120,855	106,567,572,274
3115 – Petroleum Sub-Sector Development Project	25,804,662,000	701,742,356
3121 – Makambako-Sonega 220 kv, 300 km		5,000,000,000
3147 – Transfer to Tanzania Electric Supply Company Limited	25,326,600,000	5,450,206,345
3155 – LNG Development Project		2,200,000,000
3157 – Iringa-Singida-Shinyanga (BPIT)	12,587,640,000	7,587,640,000
3162 – Construction of Natural Gas Pipeline – Mtwara – Dar es Salaam	1,100,000,000	
3164 – 150MW Natural GAS Fired Plant Kinyerezi	138,000,000,000	6,231,640,072
3165 – Ruhudji Hydropower Project	6,500,000,000	500,000,000
3166 – North-West Grid Extension Project	50,105,471,000	21,077,489,848
3167 – Rumakali Hydropower Project	6,500,000,000	5,000,000,000
3168 – Kikonge hydropower Project	1,038,480,000	1,038,480,000
3169 – Rusumo Falls Hydroelectric	13,846,404,000	13,846,404,000
3172 – Rufiji Hydropower Project	1,440,000,000,000	1,006,645,129,875
3175 – Singida-Arusha-Namanga Transmission Line Project	30,210,336,000	7,553,668,691
3176 – East African Crude Oil Pipeline Project		261,660,000,000
3179 – Rufiji-Chalinze-Kinyerezi-Dodoma 400kV Trans. Line	12,031,292,000	8,626,428,925
4279 – Expansion of TBC Coverage	5,000,000,000	5,200,106,311

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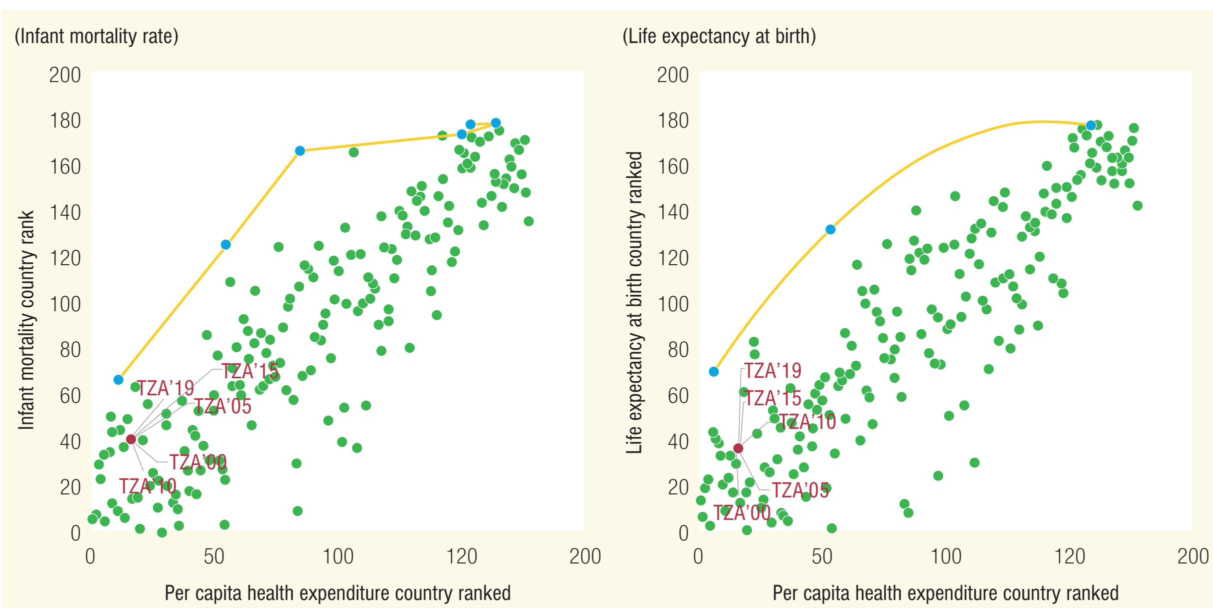
(continued)

Composition of Government Subsidies by Project, Tsh, FY 2022/21	Approved	Actual
4486 – Agricultural Sector Development Programme (ASDP)	150,000,000	
5421 – Health Sector Basket Fund	2,400,000	
5426 – Bugando Medical Sector	1,000,000,000	914,188,739
5427 – Kilamanjaro Christian Medical Centre	1,000,000,000	1,000,000,000
Grand Total	**1,900,755,405,855**	**1,466,800,697,436**

Source: BOOST data.

ANNEX 5

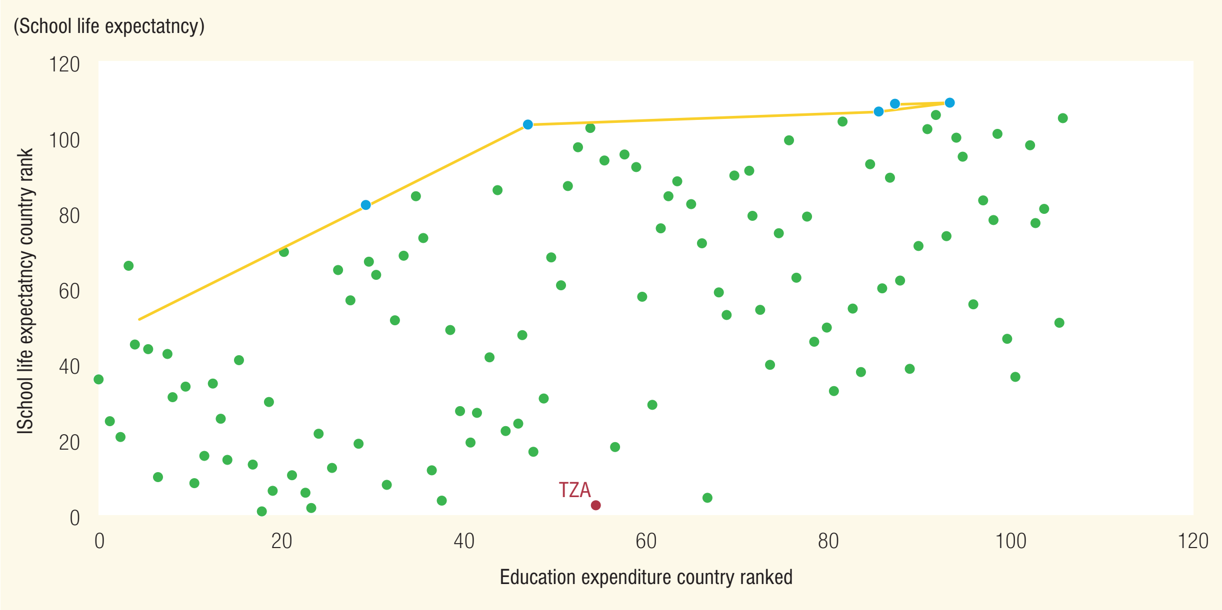
THE DEA EFFICIENCY FRONTIERS SHOW A DIRECT, POSITIVE RELATIONSHIP BETWEEN PER CAPITA HEALTH SPENDING AND KEY HEALTH INDICATORS



Note: X axis represents country ranking on per capita health expenditure (0 = lowest country spending on healthcare), Y axis represents country ranking on life expectancy at birth and infant mortality (inverse values), respectively (0 = lowest/highest life expectancy/child mortality country ranking). The solid red line going through efficient countries depicts the efficient frontier that represents achieved efficiency.

ANNEX 6

THE DEA EFFICIENCY FRONTIERS SHOW A SIMILARLY POSITIVE RELATIONSHIP BETWEEN PER CAPITA EDUCATION SPENDING AND EDUCATION OUTCOMES



Note: X axis represents country's ranking on education expenditure (0 = lowest country spending on education), Y axis represents country ranking on average year of schooling in secondary education (0 = lowest country ranking on schooling). The solid red line going through efficient countries depicts the efficient frontier that represents achieved efficiency.

ANNEX 7
THE DEA REVEALS THAT TANZANIA'S HEALTH EXPENDITURES ARE LESS EFFICIENT THAN THOSE OF MANY COMPARABLE COUNTRIES… AND ITS' EDUCATION EXPENDITURES ARE AMONG THE LEAST EFFICIENT

(DEA Efficiency Scores in Healthcare, Tanzania and Comparators)		
LSO	0.71	***Least Efficient***
SLE	0.73	
SWZ	0.74	
CIV	0.74	
TCD	0.75	
NGA	0.75	
GNQ	0.79	
CMR	0.79	
GNB	0.80	
ZAF	0.81	
NAM	0.81	
ZWE	0.81	
GIN	0.82	
SDN	0.82	
AFG	0.82	
MLI	0.82	
...	...	
TKM	0.89	
TZA	0.89	
PNG	0.89	
...	...	
JOR	0.97	
COL	0.97	
KGZ	0.97	
TUN	0.98	
VEN	0.98	
POL	0.98	
...	...	
CRI	1.00	
BGD	1.00	
JPN	1.00	
ETH	1.00	
MOZ	1.00	
FIN	1.00	***Most Efficient***

Source: DEA efficiency scores based on WDI and WHQ data.

(DEA Efficiency Scores for Education, Tanzania and Comparators)		
TZA	0.2	***Least Efficient***
TCD	0.2	
NER	0.2	
MOZ	0.2	
...	...	
LSO	0.4	
BDI	0.5	
PRY	0.6	
MYS	0.6	
PRT	0.8	
...	...	
KAZ	0.9	
HUN	0.9	
ALB	0.9	
STP	1.0	
WSM	1.0	
MDA	1.0	
LTU	1.0	
BEL	1.0	***Most Efficient***

Source: DEA efficiency scores based on WDI and WHQ data.

ANNEX 8
GOVERNMENT REVENUES

Item	Amount in FY2017/18 (Tsh millions)	Share of Tax Revenue (%)	Share of GDP (%)	Included in Analysis (Yes/No)
Total Central Government Revenue (Including LGAs) and Grants	18,875,535		14.6	
Central Government Revenue (Excluding Grants)	17,403,388		13.5	
Tax Revenue	15,120,902	100	11.7	
Direct Taxes, *of which*:	5,431,192	36	4.2	
Personal Income Tax (Presumptive Tax)	213,418	1	0.2	No
Corporate Income Tax	1,238,076	8	1	No
Payroll Tax (PAYE)	2,344,699	16	1.8	Yes
Property Taxes (Rental Tax)	63,764	0	0.1	No
Skills and Development Levy	282,840	2	0.2	Yes
Indirect Taxes, *of which*:	9,689,710	64	7.5	
VAT	4,476,646	30	3.5	Yes
Excise Taxes	2,200,214	15	1.7	Yes
Import Duties	1,735,643	11	1.3	Yes
Nontax Revenue	99,630	1	0.1	No
Grants	813,483	5	0.6	No

Source: Authors' elaboration based on official data from Tanzania Revenue Authority

ANNEX 9

PUBLIC SPENDING, FY2017/18

	Amount FY 2017/18 (Millions)	Share of Spending	Share of GDP	Included in Analysis (Yes/No)
Total Public Spending	20,468,072.0	100.0%	15.8%	
Primary Government Spending				
Defense Spending	1,236,118.9	6.0%	1.0%	No
Social Spending:				
Social protection (collective government services)	185,020.0	0.9%	0.1%	
Social inclusion (individual government services)	582.6	0.0%	0.0%	
Education, of which:	1,664,157.9	8.1%	1.3%	Yes
Primary	174,603.5	0.9%	0.1%	Yes
Secondary	163,112.0	0.8%	0.1%	Yes
Post-secondary non-tertiary	453.6	0.0%	0.0%	Yes
Tertiary	1,549.2	0.0%	0.0%	Yes
Health spending, of which:	5,577,384.0	27.2%	4.3%	Yes
Government expenditure on health	1,731,800.0	8.5%	1.3%	Yes
Health insurance	451,836.0	2.2%	0.3%	Yes
Out-of-pocket payments	1,553,603.0	7.6%	1.2%	Yes
Housing & urban development, *of which*:	424,946.6	2.1%	0.3%	No
Housing	17,152.2	0.1%	0.0%	No

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	Amount FY 2017/18 (Millions)	Share of Spending	Share of GDP	Included in Analysis (Yes/No)
Community Development	35,591.1	0.2%	0.0%	No
Water supply	371,530.1	1.8%	0.3%	No
Street lights	673.2	0.0%	0.0%	No
Non-Social Spending				
Environmental Protection, *of which*:	30,945.0	0.2%	0.0%	No
Protection of biodiversity and landscape	24,845.0	0.1%	0.0%	No
Other environmental protection	4,002.0	0.0%	0.0%	No
Energy, *of which*:				
Electricity	1,942,402.0	9.5%	1.5%	No
Non-Electric Energy	9,148.0	0.0%	0.0%	No
Petroleum and natural gas	23,350.0	0.1%	0.0%	No
Agricultural development	285,210.0	1.4%	0.2%	No
Rural roads	771,000.0	3.8%	0.6%	No

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