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February 7, 1986

To: Members of the Executive Board

From: The Secretary

Subject: Tanzania - Staff Report for the 1985 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with Tanzania, which has been tentatively scheduled for discussion on Friday, March 7, 1986. A proposed decision appears on page 23.

Mr. Basu (ext. 6511) or Mr. Abdi (ext. 6517) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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INTERNATIONAL MONETARY FUND

TANZANIA

Staff Report for 1985 Article IV Consultation

Prepared by the African Department and
the Exchange and Trade Relations Department

Approved by A.D. Ouattara and W.A. Beveridge

February 7, 1986

I. Introduction

The 1985 Article IV consultation discussions with Tanzania were held in Dar es Salaam during the period December 3-14, 1985. The Tanzanian representatives included the Minister of Finance and Economic Planning, Mr. C.D. Msuya; the Governor of the Bank of Tanzania, Mr. C.M. Nyirabu; the Principal Secretary of the Ministry of Finance and Economic Planning, Mr. G. Rutihinda; and other senior officials of ministries and agencies concerned with economic and financial matters. The staff representatives were Mr. R.J. Bhatia (head-AFR), Mr. A. Abdi (AFR), Mr. E. Kreis (FAD), Mr. K. Thugge (EP-AFR), Mr. E. Zervoudakis (ETR), and Miss A. Hatcher (secretary-BCS). The Alternate Executive Director for Tanzania, Mr. Abdallah, attended the policy discussions. A World Bank mission held concurrent discussions with the Tanzanian authorities through December 10, 1985. The Fund and Bank staff held extensive discussions both at headquarters and in Dar es Salaam in an attempt to arrive at a consistent diagnosis of the economic situation and the identification of appropriate adjustment policies. A subsequent staff visit took place during January 7-17, 1986 to discuss with the authorities a possible adjustment scenario.

Tanzania continues to avail itself of the transitional arrangements of Article XIV, Section 2. Summaries of Tanzania's relations with the Fund and the Bank are presented in Attachments I and II, respectively.

II. Recent Economic Developments

Tanzania's economic and financial situation has deteriorated rapidly since the mid-1970s, and particularly since 1982, as reflected in a low or negative growth in real GDP, high inflation, and large imbalances in the fiscal and external accounts. Adverse external developments, including recurrent droughts and a substantial worsening of the terms of trade, partly accounted for this deterioration. Inadequate domestic policies, however, also contributed to weakening of the economy and in many aspects were the principal factors that led to the low domestic production, the emergence of acute shortages of imports, the exhaustion of official reserves, and a buildup of external payments arrears.

Based on preliminary national income accounts data, which at best are indicative of trends, real gross domestic product (GDP) increased by only about 2 percent over the four years ended 1984 (Table 1). Acute price distortions and shortages of imported inputs contributed to a 56 percent decline in industrial output, and constrained the growth of the service sector. Agricultural output, which accounts for about 46 percent of GDP increased by only 1-2 percent annually. With few exceptions, the volume of marketed food crops and traditional agricultural exports declined, and the volume of marketed production of most crops was significantly below the peaks realized in the 1970s. This decline in the volume of marketed agricultural production is attributed primarily to an erosion of price incentives. Officially set producer prices for export crops declined in real terms by 23-50 percent over the decade ended with the 1984/85 crop season. In recent years, both export and domestic food crops were also adversely affected by shortages of essential inputs, transportation difficulties, and inefficient marketing arrangements.

The domestic inflation rate, as measured by the official national consumer price index (NCPI), accelerated sharply to an annual average of about 30 percent in 1980-84, from about 12 percent in 1976-79. Although occasionally, when the commodities are not available at controlled prices, parallel market prices are reflected in the NCPI calculations, extensive price controls and large consumer subsidies moderated the rate of domestic price increases recorded by these official indices. The list of price-controlled commodities has, however, been significantly reduced over the past four years, and the consumer price subsidies were eliminated in June 1984; nevertheless, still price controls remain extensive and cover several hundreds of items.

Production and price data are not yet available for 1985. Staff estimates based on partial data, however, indicate that real GDP grew by about 2 percent, primarily on account of higher production of domestic food crops. Due to a worsening foreign exchange situation and reduced availability of essential inputs, production in most other sectors is estimated to have declined. Marketing of export crops has also been affected adversely by the shortages of fuel oil and other transportation problems. The recorded rate of inflation is estimated to have moderated somewhat to about 27 percent in 1985, from a peak of 36 percent in the preceding year, in part due to lower increases in food prices, which account for 47 percent and 64 percent of the old and new NCPI weights, respectively.

In recent years, financial operations of the Central Government and the rest of the public sector have recorded large deficits, which contributed to, and also reflected, the deterioration in Tanzania's economic and financial situation. The Central Government's overall deficit in fiscal years 1981/82-1983/84 (July-June) averaged about

Table 1. Tanzania: Selected Economic and Financial Indicators, 1981-85

	1981	1982	1983	1984 Prel.	1985 Est.
	(Changes in percent)				
GDP and prices					
Real GDP	-1.1	1.3	-0.4	2.5	2.5
Consumer prices	25.6	28.9	27.0	36.2	26.5
Government budget 2/					
Revenue, excluding grants	15.5	17.0	18.4	34.7	0.3
Total expenditure	33.5	-4.0	13.3	23.0	7.2
Money and credit					
Total credit	23.9	19.5	15.8	21.9	17.2
Of which: government (net)	(28.3)	(25.3)	(17.5)	(21.9)	(12.6)
Money plus quasi-money	27.1	20.4	13.2	22.4	19.0
Velocity (GDP relative to M)	2.80	2.76	2.67	2.51	2.52
Interest rates (12-month deposits)	5.00	5.50	5.50	5.50	7.50
External sector (on the basis of U.S. dollars)					
Exports, f.o.b.	11.5	-26.6	-8.3	-2.5	-11.6
Imports, c.i.f.	-4.8	-5.7	-25.3	2.5	15.8
Export volume	23.2	-23.0	-10.2	-4.3	-2.2
Import volume	-13.6	-9.9	-20.8	4.3	18.4
Terms of trade	-17.9	-10.6	8.2	3.8	-7.6
Nominal effective exchange rate (depreciation -) 3/	12.7	-4.2	-15.6	-19.2	3.2
Real effective exchange rate (depreciation -)	26.7	20.6	2.2	4.0	15.0
	(In percent of GDP) 1/				
Overall government budget deficit (cash basis)	-14.1	-11.1	-10.0	-8.1	-8.7
Balance of payments current account deficit	-10.7	-13.5	-9.2	-10.1	-10.5
	(In percent of merchandise exports)				
External current account deficit					
Excluding grants	93.3	155.8	115.0	122.1	167.6
Including grants	74.2	133.2	92.7	96.0	135.6
Scheduled external debt service 4/					
Including IMF	16.7	19.4	35.3	66.4	53.5
Excluding IMF	11.7	16.0	28.9	60.9	49.7
Actual external debt service					
Including IMF	15.0	14.7	22.0	21.0	...
Excluding IMF	10.0	11.3	15.6	15.5	...
	(In millions of U.S. dollars)				
External current account balance, excluding grants (deficit -)	-525.6	-643.7	-435.7	-450.6	-546.3
Overall balance (deficit -)	-1.8	-93.6	-0.2	-158.7	-278.5
External payments arrears	296.2	401.5	540.0	695.0	980.0
Commercial	(...)	(...)	(247.0)	249.0)	320.0)
Debt service	(...)	(...)	(293.0)	(446.0)	(660.0)
Medium- and long-term debt (including related arrears)	2,200.0	2,450.0	3,119.4	5/ 3,001.2	5/ 3,181.2
	(In weeks of imports)				
Gross official reserves	2.3	1.9	4.0	2.4	2.2

Sources: Based on data provided by the Tanzanian authorities; and staff estimates.

1/ Based on revised official GDP series and staff estimates for 1985.
2/ On a fiscal year basis, beginning on July 1 of each year. Preliminary estimates are given for 1984/85.
3/ Import-weighted; changes in end-of-period indexes based on December 1978 = 100. Minus indicates depreciation.
4/ In percent of exports of goods and services, and private transfers.
5/ Based on creditors' survey data compiled with assistance from a Swedish commercial bank and may not be comparable with data for earlier years.

T Sh 7.3 billion, equivalent to 11.7 percent of GDP (Table 2), and reflected both lower revenues (mainly reflecting an overvalued exchange rate and price controls) and a rapid growth in current expenditure, primarily for subsidies and transfers. These deficits were financed to a large extent by domestic bank credit, which averaged about two thirds of the overall deficit and about one fourth of the money stock at the beginning of each fiscal year during the three-year period. In order to reduce the deficit, a number of fiscal measures were introduced with the presentation of the 1984/85 budget. They included selective increases in consumption and sales taxes, which were estimated to yield T Sh 1.0 billion, the elimination of food and agricultural input subsidies from the budget, the reorganization of some central government ministries, and the abolition of budgetary transfers to major agricultural parastatals. Revenue-collection administration was also strengthened. As a result, central government operations in the fiscal year 1984/85 recorded a deficit of T Sh 6.8 billion, about 8.1 percent of GDP, compared with 10 percent in 1983/84 and 12.6 percent budgeted for 1984/85.

The improvement in the budget outturn for 1984/85 is attributable to a sharp increase in tax revenue, 27 percent above the budgeted amount (36 percent above the outturn in the previous year), with customs duties almost doubling and consumption taxes rising by 38 percent. The increase in tax revenue over the budgeted estimate is explained to a large extent by the nominal depreciation of the exchange rate of the Tanzania shilling in June 1984 and by the expansion of "own-exchange" imports, which resulted in a sizable increase of dutiable imports. Recurrent expenditure also rose sharply (by 15 percent compared to the budgeted amount and by 26 percent compared to the previous year's actuals), as transfers to the local government and defense expenditure rose substantially above the original budget allocations. This increase in current expenditure was, however, to a large extent compensated for by underspending on capital projects. These trends resulted in a lower deficit and bank borrowing of T Sh 3.0 billion, or about 40 percent below the original budget estimates.

The 1985/86 approved budget estimates the overall deficit to be of the order of T Sh 8.7 billion (equivalent to about 8.7 percent of estimated GDP.) As the use of net foreign loans and grants is projected to rise only moderately, the domestic borrowing requirements are budgeted to increase substantially, and over 60 percent of the deficit is expected to be financed by bank credit. Total revenue is estimated to remain unchanged, from the preliminary outturn of 1984/85, despite new discretionary tax measures which are estimated to yield T Sh 1.2 billion (1.3 percent of GDP). These measures include increases in fees charged for services provided by the Government; a reduction in transfers of earmarked revenue; increases in sales and excise taxes; a new payroll tax; and other net changes in tax rates and fees. Total expenditure is budgeted to increase by 7 percent, which is almost entirely accounted for by a projected 27 percent increase in capital outlays.

Table 2. Tanzania: Summary of Fiscal Operations, 1980/81-1985/86

(In millions of Tanzania shillings)

	1980/81 Actual	1981/82 Actual	1982/83 Prov. actual	1983/84 Prov.	1984/85 Rev. bud. est. 1/	1984/85 Prel. outturn	1985/86 Rev. bud. est. 2/	1985/86 Staff est. 3/
Total revenue	8,742	10,101	11,819	13,995	14,809	18,855	18,920	20,160
Tax revenue	8,139	9,078	11,252	13,407	13,144	18,231	17,343	19,300
Nontax revenue	603	1,025	567	588	1,665	624	1,577	860
Total expenditure and net spending	14,370	19,182	18,442	20,886	25,520	25,699	27,561	27,403
Recurrent expenditure	9,656	13,980	14,062	16,174	17,668	20,376	20,762	21,782
Development expenditure	4,688	5,196	4,359	4,733	7,532	5,306	6,784	5,606
Net lending	26	6	21	-21	50	15	15	15
Overall deficit (checks-issued basis)	-5,628	-9,081	-6,623	-6,891	-10,441	-6,844	-8,641	-7,243
Adjustment to cash and other items (net)	-612	1,213	-412	-154	--	84	--	--
Overall deficit (checks-cashed basis)	-6,240	-7,868	-7,035	-7,045	-10,441	-6,760	-8,641	-7,243
Foreign financing (net)	2,702	2,860	2,563	1,464	4,964	2,500	3,202	1,676
Foreign grants	1,870	1,656	1,593	1,234	3,540	1,892	2,884	1,685
Net foreign loans	832	1,204	970	230	1,424	608	318	-9
Gross borrowing	907	1,287	1,151	661	2,200	1,244	1,542	1,215
Repayment	-75	-83	-181	-431	-776	-636	-1,224	-1,224
Domestic financing (net)	3,538	5,008	4,472	5,581	5,477	4,260	5,439	5,567
Nonbank borrowing	620	780	469	507	725	1,231	239	536
Bank borrowing	2,918	4,228	4,003	5,074	4,752	3,029	5,200	5,031
Memorandum items:								
Overall cash deficit as percentage of total expenditure	43.4	41.0	38.1	33.7	41.4	26.3	31.4	26.4
Overall cash deficit as percentage of estimated GDP 4/	13.3	14.1	11.1	10.0	12.6	8.1	8.7	7.3

Sources: Ministry of Finance; and staff estimates.

1/ The revised estimates include the original budget, supplementary expenditure bills, new tax measures, and adjustments for the devaluation announced in early June 1984.

2/ Include the original budget plus the measures announced in the National Assembly by the Minister of Financeon June 13, 1985.

3/ Staff estimates are based on developments during the first quarter of the fiscal year 1985/86.

4/ New revised GDP series.

Based on a re-examination of revenue estimates in the budget, a downward adjustment in development spending in accordance with the past realization rates and foreign financing patterns, and preliminary returns of the first quarter of the fiscal year, the staff estimates that the fiscal performance in 1985/86 may be better than envisaged in the budget. Higher collections from income taxes, and sales tax on domestic consumption and imports, as well as other taxes, indicate that revenues are likely to have been underestimated in the budget. On the other hand, while current expenditures are exceeding the budgeted amounts, capital outlays are much lower than planned. With some improvement in expenditure control and continuous efforts in tax collections, the overall budget deficit in 1985/86 could be kept at about T Sh 7.2 billion, equivalent to 7.3 percent of GDP, compared to 8.1 percent in 1984/85. 1/

The financial operations of the parastatals, which are predominant in agricultural marketing and processing and in other services, have resulted in persistent deficits which have been financed by direct budgetary support and sizable increases in bank credit. In particular, the major agricultural export marketing authorities have incurred large deficits as their operating costs have continued to rise while export prices have declined, and as the exchange rate has not been adjusted adequately. The combined operating deficits of the five major agricultural export marketing authorities 2/ increased from an estimated T Sh 680 million in 1983/84 to about T Sh 840 million in the 1984/85 crop year. The operations of the National Milling Corporation (NMC), the domestic food processing and marketing agency, also recorded large deficits during the three financial years ended in July 1984, essentially because the controlled retail price of maize flour, its major product line, was set below its costs. Its cumulative deficits, which amounted to T Sh 1.5 billion, were financed by increasingly large bank overdraft and government subsidy transfers. These adverse financial developments prompted the Government to reintroduce cooperative unions, which took over from the parastatals the procurement and transportation of crops. The actual operation of these cooperative unions began around May 1985. In addition, the operations of the agricultural parastatals have been examined with a view to decreasing their operating costs through the reduction of the size of their payroll and other cost-saving measures. Despite these measures, however, the financial operations of the agricultural parastatals are estimated to continue to incur large losses in 1985/86, as export crop prices, except coffee, have declined and costs have continued to remain high.

1/ The analysis above is on a "checks-cashed" basis, as compared to "checks-issued" basis. It may be noted that in the more recent years the float of outstanding checks has not varied significantly.

2/ The Coffee Authority of Tanzania, the Tanzania Tea Authority, the Cotton Authority of Tanzania, the Tanzania Tobacco Board, and the Cashew Authority of Tanzania.

In 1985, the operations of other public enterprises, particularly in the industrial sector, were also adversely affected by a shortage o imported inputs and spare parts, which resulted in low rates of capaci utilization, ranging between 20 and 50 percent. Furthermore, the pric control regime has contributed to the financial difficulties facing manufacturing enterprises as officially determined ex-factory prices have lagged behind their operating costs.

Domestic credit expansion accommodated the public sector demand f credit. Reflecting the deficits in financial operations of the public sector, overall domestic credit increased by 20 percent in 1982, 16 percent in 1983, and 22 percent in 1984 (Table 3). Bank credit to the private sector, including smaller parastatal enterprises, rose at modest rates over the three years, in part due to the decline in the level of imports and economic activity. Because of the persistent balance of payments deficits incurred in recent years (the sizable accumulations of external commercial payments arrears are included in the foreign liabilities of the banking system), the net foreign asset position of the banking system declined precipitously from a net liabilities position of T Sh 3.0 billion in December 1981 to T Sh 7.1 billion as of end-December 1984. Broad money registered a growth of 20 percent in 1982, 15 percent in 1983, and 22 percent in 1984. These growth rates are somewhat higher than those of nominal GDP. However, the national consumer price index has risen at a much faster rate than the GDP deflator, suggesting that real money balances in the economy have declined. Based on developments in the first half of 1985 and subject to the realization of lower expansion of governmen borrowing below the level expected in the 1985/86 budget, monetary and credit expansion is estimated to have decelerated.

The structure of interest rates has been low and negative in real terms. In 1982-84, the treasury bill rate was at 4.3 percent, the 12-month deposit rate at 5.5 percent, and the maximum lending rate at 13 percent, while the average annual increase in consumer prices reach 30 percent. In October 1985 deposit and lending rates were adjusted with the new treasury bill rate moving to 5.5 percent, the 12-month deposit rate to 7.5 percent, and the maximum bank lending rate to 14 percent--all rates still substantially negative in real terms.

During the four-year period ended 1984, Tanzania experienced larg and increasing external imbalances which were reflected in a severe compression of imports, and a large accumulation of arrears in commercial and debt service payments. Underlying these developments were the above-mentioned inadequate pricing and expansionary financial policies, an 18 percent deterioration in the terms of trade, and an exchange rate policy that allowed a real appreciation of the Tanzania shilling by over 100 percent during the five-year period to end-1984, notwithstanding significant devaluations undertaken in 1982, 1983, and 1984.

Table 3. Tanzania: Monetary Survey, 1981-85

	1981	1982		1983		1984		1985
	Dec.	June	Dec.	June	Dec.	June	Dec.	June
	(In millions of Tanzania shillings)							
ign assets (net)	-3,025.4	-3,825.0	-4,187.2	-5,383.0	-5,367.2	-7,510.7	-7,099.2	-7,611.9
nk of Tanzania foreign assets	353.1	313.5	265.9	415.3	408.5	275.1	485.3	373.5
ss Bank of Tanzania foreign liabilities	-1,172.7	-1,283.2	-1,273.0	-1,616.6	-1,384.5	-1,486.9	-1,085.1	-1,067.0
tional Bank of Commerce foreign assets	86.4	217.9	108.0	182.2	369.8	437.1	208.6	325.7
ss NBC foreign liabilities	-2,292.2	-3,073.2	-3,288.1	-4,363.9	-4,761.0	-6,736.0	-6,708.0	-7,244.1
Of which: arrears	(-2,258.3)	(-3,033.4)	(-3,245.1)	(-4,342.1)	(-4,704.4)	(-6,555.0)	(-6,551.0)	(-7,063.0)
stic credit	21,956.7	22,659.0	26,234.0	27,431.0	30,377.9	34,372.4	37,024.4	40,392.2
aims on Government (net)	14,175.5	15,244.7	17,763.2	19,424.1	20,880.2	23,916.4	25,432.4	27,028.2
Bank of Tanzania claims on Govt.	7,990.0	7,857.3	9,483.9	8,790.4	10,016.6	10,692.9	12,453.5	13,483.1
ss Bank of Tanzania government deposits	-1.9	-1.7	-9.8	-96.4	-92.1	-5.5	-21.2	-21.9
National Bank of Commerce claims on Government	6,517.7	7,897.7	9,349.0	11,198.9	11,449.2	14,201.0	13,817.6	13,972.7
ss National Bank of Commerce government deposits	-330.3	-508.6	-1,059.9	-468.8	-493.5	-972.0	-817.5	-405.7
ms on public entities d private sector	7,781.2	7,414.3	8,470.8	8,006.9	9,497.7	10,456.0	11,592.0	13,364.0
y and quasi money	18,104.9	18,997.9	21,787.0	22,107.6	24,664.4	27,646.2	30,197.8	32,885.4
rrency and demand deposits	12,720.2	13,353.2	15,406.6	14,604.7	16,190.3	18,777.5	20,780.3	22,594.7
tional Bank of Commerce time and savings deposits (including foreign currency deposits	5,384.7	5,644.7	6,380.4	7,502.9	8,474.1	8,868.7	9,417.5	10,290.7
r items (net)	826.5	-163.8	260.1	-60.0	346.3	-784.5	-272.6	-105.1
	(Annual percentage change)							
domestic credit		21.6	19.5	21.1	15.8	25.3	21.9	17.5
edit to Government		27.4	25.3	27.4	17.5	23.1	21.8	13.0
her claims		11.3	8.9	8.0	12.1	30.6	22.1	26.1
y (M2)		25.8	20.3	16.4	13.2	25.1	22.4	19.0
city (GDP/M2)		2.9	2.8	2.9	2.7	2.6	2.5	2.7

urces: Data provided by the Tanzanian authorities; and staff estimates.

Reflecting a steady decline in export receipts (27 percent in value and 18 percent in volume terms in the four years 1981-84), import restrictions were intensified. As a result, total imports declined sharply and in 1984 were almost 40 percent lower in volume terms than in 1980. The decline was especially marked in the case of consumer and capital goods. Although the share of intermediate goods, including oil, in total imports rose during the period, such imports also declined in volume terms, resulting in low and falling utilization of industrial capacity and shortages of essential agricultural inputs.

The current account deficit declined from an average level of US$621 million in 1980-82 (12.5 percent of GDP) to US$443 million in 1983-84 (9.7 percent of GDP). Gross capital inflows remained relatively constant during the period, notwithstanding heavy recourse to oil credits since 1983, 1/ but scheduled amortizations rose, thereby resulting in sharply lower net capital inflows. As a result, the overall balance of payments recorded large deficits, which, with the gross foreign reserves already having been exhausted, were mainly financed through an accumulation of arrears.

In view of the considerable time lag of data availability, the balance of payments estimates for 1985 (Table 4) are preliminary and likely to be revised significantly. There are, however, indications that Tanzania's external position showed a further deterioration in 1985, as evidenced by a large accumulation of external payments arrears, including to the Fund and the World Bank, and in respect of oil credits from oil-producing countries, which resulted in the drying up of trade credits and necessitated cash payments for imports, including oil. 2/

Exports in 1985 are estimated to have declined by 12 percent in U.S. dollar terms and 2 percent in volume terms.. Earnings from the major export crops are estimated to have declined on the average by 18 percent, reflecting an average decline in prices of 16 percent and continued unfavorable volume performance, while other exports continued to stagnate. Imports are estimated to have risen by 16 percent or by US$130 million. Most of that increase was accounted for by imports under the "own-exchange" scheme, which are estimated to have amounted to US$120 million in 1985, compared with US$40 million in the previous year. The "own-exchange" scheme, which allows imports paid for with foreign exchange held abroad, was introduced in early 1984 and was substantially liberalized in July 1984 when the list of commodities eligible for such treatment was expanded. The estimated increase in

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1/ Tanzania resorted to oil credits from several oil-producing countries (Algeria, Angola, the Islamic Republic of Iran, and Libya).

2/ Overdue payments obligations to the Fund have accumulated since April 1985. The World Bank suspended disbursements of committed loans in October 1985 and lifted the suspension in December 1985, when arrears were less than 60 days overdue; arrears with respect to the oil credits began accumulating in 1984 and were expected to reach US$120 million by end-1985.

Table 4. Tanzania: Balance of Payments, 1981-88

(In millions of U.S. dollars)

	1981	1982	1983	1984	Official Projections 1985	1986	1987	1988
Trade account	-598.9	-681.5	-440.0	-470.5	-645.9	-792.2	-708.6	-645.7
Exports, f.o.b.	563.4	413.0	378.8	368.9	325.9	414.8	528.4	654.3
Imports, c.i.f.	-1,162.3	-1,094.6	-818.8	-839.4	-971.8	-1,207.0	-1,237.0	-1,300.0
Oil	-260.9	-251.8	-229.9	-227.4	-229.8	-247.0	-256.9	-267.2
Own exchange	--	--	--	-40.0	-120.0	-120.0	-120.0	-120.0
Other	-901.4	-742.8	-589.0	-571.9	-622.0	-840.0	-860.1	-912.8
Services, net	50.9	12.4	-14.6	-43.2	-30.4	-32.0	-31.0	-29.0
Receipts	195.8	117.3	108.1	107.4	129.0	137.0	147.0	156.0
Payments	-144.9	-104.9	-122.7	-150.6	-159.4	-169.0	-178.0	-185.0
Interest	-51.3	-54.1	-55.8	-89.3	-90.8	-92.0	-94.4	-101.3
Other	-93.6	-50.8	-66.9	-61.3	-68.6	-77.0	-83.6	-83.7
Private transfers, net	22.5	25.4	18.9	63.0	130.0	128.0	126.0	124.0
Inflows	44.6	41.5	38.9	80.9	150.0	150.0	150.0	150.0
Outflows	-22.1	-16.1	-20.0	-17.9	-20.0	-22.0	-24.0	-26.0
Current account	-525.6	-643.7	-435.7	-450.6	-546.3	-696.2	-613.6	-550.7
Government transfers, net	107.5	93.7	84.4	96.5	104.5	104.5	104.5	111.5
Inflows	108.6	95.6	88.7	100.0	108.0	108.0	108.0	115.0
Outflows	-1.1	-1.9	-4.3	-3.5	-3.5	-3.5	-3.5	-3.5
Medium- and long-term loans, net	179.9	240.5	149.9	-74.1	-18.5	29.0	25.0	44.0
Inflows	230.2	285.6	252.7	182.8	200.0	210.0	210.0	220.0
Outflows	-50.3	-45.1	-102.8	-256.9	-218.5	-181.0	-185.0	-176.0
Suppliers' credits, net	100.7	57.6	101.8	109.8	-32.0	-4.0	35.0	50.0
SDR allocation	6.0	--	--	--	--	--	--	--
Exceptional financing	111.9	91.7	60.6	49.1	100.0	100.0	130.0	130.0
Other capital n.i.e. and errors and omissions	17.8	66.6	38.8	110.6	113.8	--	--	--
Overall balance	-1.8	-93.6	-0.2	-158.7	-278.5	-466.7	-319.1	-215.2
Financing	1.8	93.6	0.2	158.7	278.5	...	...	...
Arrears (increase +)	21.9	76.3	45.2	183.1	282.7	...	...	...
IMF position, net (increase -)	-14.1	-11.5	-29.9	-27.5	-14.2	-4.4	-4.4	--
Other reserves, net (increase -)	-6.0	28.8	-15.1	3.1	10.0	...	...	...
Financing gap	--	--	--	--	--	471.1	323.5	215.2

Sources: Data and projections provided by the Tanzanian authorities; and staff estimates.

total imports also reflects an increase in other non-oil imports by US$50 million or 9 percent, reflecting mainly increased exceptional financing in the form of import support. The balance of payments projections show an overall deficit of US$279 million, which is likely to be financed, in large part, through a further accumulation of arrears; however, no information is yet available on the financing.

Tanzania's medium- and long-term external debt at end-1984 is estimated at US$3 billion (over 50 percent of GDP and 700 percent of exports of goods and services), of which US$446 million represented arrears on principal and interest payments; 1/ it is estimated to have risen further to US$3.2 billion at end-1985, including US$660 million of arrears on debt service. Short-term debt at end-1984 amounted to US$325 million, of which US$250 million represented commercial arrears, and is estimated to have risen to about US$395 million at end-1985, including US$320 million of commercial arrears. Reflecting in part the unfavorable export performance and a concentration of maturities, the debt service ratio has risen from 17 percent in 1980 to 54 percent in 1985, notwithstanding concessional terms of borrowing.

The Tanzania shilling has been pegged to a composite of the currencies of Tanzania's main trading partners since January 1979, when it was devalued by 10 percent and its peg to the SDR was discontinued. Subsequently, the shilling was devalued by 10 percent in foreign currency terms in March 1982, 20 percent in June 1983, and 26 percent in June 1984, resulting in an exchange rate of T Sh 17 per U.S. dollar. Reflecting the fall of the U.S. dollar against other major currencies, the shilling has appreciated from T Sh 18.4 per U.S. dollar in March 1985 to T Sh 16.4 per U.S. dollar at the end of December 1985; the real effective appreciation of the shilling between end-1978 and 1985 is estimated at about 120 percent (Chart 1). The severe external imbalance has led to the emergence of a parallel market where the prevailing exchange rate was reportedly at about T Sh 150 per U.S. dollar in December 1985, or eight times higher than the official rate.

Tanzania's exchange and trade system has become very restrictive, involving heavy reliance on ad hoc administrative decisions, a breakdown of the foreign exchange budgeting process and a buildup of arrears on commercial and debt service payments. In order to alleviate the domestic shortage of imported goods, "own-exchange" imports were first allowed in early 1984. The list of eligible commodities under the scheme was expanded in July 1984 to include building materials, textile goods, shoes, electrical appliances, tractors and spare parts, trucks, pickup vans, and buses. The domestic price of the "own-exchange" imports generally reflects the parallel market exchange rate. In July 1984, an export retention scheme was introduced, whereby exporters were allowed to keep 10-15 percent of their foreign exchange proceeds and use

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1/ These data are based on a creditors' survey by a Swedish commercial bank, which compiled preliminary estimates of Tanzania's outstanding external debt for end-1983 and 1984.

them for the importation of inputs relating to their activities. Subsequently, the retention rates for some exporters were increased to higher levels on a case-by-case basis. In some instances, however, the Bank of Tanzania has asked parastatals to surrender the retained amount for the purpose of making other priority payments. A tax rebate scheme, under which exporters may claim rebates varying from 5 percent to 20 percent of the f.o.b. value of exports, has been in effect since 1981 and gives rise to a multiple currency practice.

III. Report on Discussions

In concluding the 1984 Article IV consultation, the Executive Board took the view that the policy changes introduced with the 1984/85 (July-June) budget, while being in the right direction, were insufficient to bring about significant improvement in Tanzania's economic and financial situation, and that more comprehensive and stronger adjustment measures were required. Key policy adjustments called for in the Executive Board's conclusions included the following: significant and stepped-up increases in real producer prices; liberalization of domestic price controls and marketing arrangements; flexible management of the exchange rate, involving further adjustments in the real exchange rate; decisive reductions in the financial imbalances of both parastatals and central government operations to ensure an adequately restrictive stance of fiscal and domestic credit policies; and sizable adjustments in interest rates to phase out negative real interest rates.

The staff reviewed with the authorities the recent developments and the effects of the policies introduced in mid-1984, and the rationale behind the policy stance of the 1985/86 budget. The discussions were further widened to include the authorities' medium-term scenario of the balance of payments through 1988 and the policies they proposed to realize that scenario. The staff also raised with the authorities the issue of arrears of payment obligations to the Fund (SDR 18.4 million as of end-1985) 1/ and discussed further modifications to the authorities' policy package that could move Tanzania toward financial and economic viability and enable it to become current with the Fund.

1. Overall developments

The Tanzanian representatives noted that in mid-1982 the Government adopted a three-year comprehensive Structural Adjustment Program (SAP), aimed at dealing with the country's serious structural problems. The 1984/85 budget further strengthened the policy stance, as the Tanzania shilling was depreciated by 36 percent (in local currency terms), producers were given further real increases in commodity purchase prices, the parastatals were subjected to a reform program aimed at cost cutting

1/ Subsequently, Tanzania made a payment of SDR 1.1 million on January 22, 1986 and arrears amounted to T Sh 17.9 million as of January 24, 1986.

and financial balance, food marketing was liberalized, and changes were introduced toward some liberalization of the trade and exchange system.

Overall, in the view of the Tanzanian authorities, the implementation of policies carried out during 1984/85 has met with limited success. There was a slight expansion of output in 1984, but this was, in large part, a result of the favorable weather conditions which led to increased food production. On the financial side, the overall fiscal situation improved, and the rate of inflation moderated in the last half of 1985, but the balance of payments deficit in 1985 might have widened further. The shortage of foreign exchange continued to limit the effectiveness of many of the policy reforms undertaken so far, and the Tanzanian representatives made the general comment that the overall impact of these policies would have been more favorable had additional imports become available. In that respect, they had expected that, particularly after the major policy reorientation introduced with the 1984/85 budget, the international donor response would have been more forthcoming than had been the case. They expressed the view that external support would be most useful if provided in advance of a major new policy initiative.

2. Production policies and marketing arrangements

The Tanzanian representatives underlined the continued scarcity of foreign exchange and stated that their production policies would emphasize rehabilitation and increased efficiency in the allocation of resources which would be channelled primarily into production and export sectors. Over the past three years through mid-1985, they had embarked on a policy of providing higher price incentives to producers of both the food and export crops by raising producer prices by at least 5 percent annually in real terms and by between 30 and 45 percent in nominal terms. However, despite this, marketed agricultural production had failed to increase. This failure of production to respond to price increases had led the authorities to believe that production was constrained by factors other than prices, such as the lack of necessary inputs and transport facilities. For the 1985/86 (for perennial crops) and 1986/87 (for annual crops) seasons, nominal producer prices were increased by only between 10 and 20 percent, or below the current rate of inflation. It was the intention of the authorities, instead, to concentrate their efforts on providing the farmers with a larger supply of necessary inputs and on improving the marketing system. They felt that in the current circumstances, the newly announced prices should provide an adequate financial incentive and that after farmers were assured of additional inputs and after the improved marketing organization was in place, a new round of increases in real producer prices would be considered. The staff mission pointed out that overall agricultural production (as recorded in national income accounts) had increased, but that marketed production had not registered a corresponding rise. In fact, for foodgrains, where prices and marketing had been liberalized, marketed production appeared to have responded favorably. These developments, in the staff's view, reflected that the producers still did not find prices attractive enough, though the importance of adequate marketing and transportation arrangements should not be understated. The staff noted that the real producer prices (i.e., nominal prices deflated by the official NCPI) of most export crops were still around 40 percent below their peak levels in 1976/77 and 1977/78. The Tanzanian representatives, however, felt that this did not contradict their thesis that the output was constrained primarily by factors other than price incentives; this was particularly true for export crops where there could be little auto-consumption and whose marketed volumes had shown little increase. The relatively better performance of food products was attributed primarily to weather conditions, though the impact of the previous producer pricing policies that had favored those crops in comparison to the export crops was also acknowledged.

The Tanzanian representatives stated that the government had taken a number of measures to improve the marketing structure for agricultural products. Thus, the agricultural marketing authorities had been transformed into marketing boards and cooperative unions reintroduced to purchase crops from the farmers. Also, the ownership and management of most agro-processing facilities had been transferred from the marketing boards to the cooperative unions. Marketing boards are now responsible only for the interregional sale and export of crops. Foodgrain marketing had also been liberalized by freely permitting individuals to transport up to 500 kg. In addition, the authorities have agreed under an IDA credit to issue freely transport permits. In the view of the Tanzanian representatives, however, this institutional reform would need to be followed by the resolution of other inherent difficulties--poor roads, poor communications, shortages of rolling stock, as well as fuel and spare parts for road and rail transport--before the production potential of the economy could be substantially realized. The staff mission noted that the overall impact on the cost structure of marketing by the public sector had been minimal, as the parastatals had continued to incur financial losses and there was little evidence that the cooperative unions had been any more efficient. The present monopsonistic structure of marketing export crops still remained, and total marketing cost margins were high, by international standards.

In the industrial sector, the Tanzanian representatives noted that, mainly owing to the lack of raw materials and maintenance imports, capacity utilization had decreased and now averaged about 30 percent. The intention was to rehabilitate and utilize existing production capacity before additional capacity was allowed to be built. To that end, several industries were permitted to retain a certain proportion of their export receipts to meet their import needs, and, where feasible, import licenses were being granted for other industries to improve their production capacities. At the same time, the authorities had reduced the list of items subject to price controls and were considering a further liberalization of the price control regime to allow the needed flexibility to enterprises to cover their costs. The Tanzanian representatives insisted, however, that some price controls on essential commodities would continue to be maintained in pursuance of the sociopolitical goals of the Government.

The above policies are a part of the authorities' medium-term recovery program to be presented to the next planned meeting of the Consultative Group to be convened by the World Bank. That program envisages an investment program that would be confined to the rehabilitation, maintenance, and improvement of existing capacity and to the completion of ongoing projects. The staff mission noted that so long as the exchange rate remained highly overvalued and other prices, including interest rates, were controlled administratively, it would not be possible to accord appropriate priorities within such an investment program, nor would the private sector receive appropriate pricing signals to make sound economic decisions. Given that over the past several years investment in the manufacturing, mainly in the parastatal, sector, had been very large and in industries which were not necessarily economically viable, the authorities also needed to consider whether all the existing industries should be rehabilitated or whether some could be closed down or privatized.

3. Financial policies

The Tanzanian representatives recognized the role of prudent financial policies in bringing about the necessary adjustment over the medium term. In that context, they were relatively satisfied with the outcome of the 1984/85 budget. The reduced deficit, as well as the reduced recourse to bank financing, was primarily the result of actual revenues having exceeded the budgeted revenues, emanating mainly from a higher level of imports made possible under the "own-exchange" import scheme. Current expenditure, on the other hand, was also more than budgeted, partly because the district councils failed to exploit the revenue sources provided to them, necessitating budgetary transfers to meet their expenses, but also on account of slippages in expenditure control. It was also noted that the initial budgetary estimates had not taken full account of the impact of the devaluation of the Tanzania shilling announced with the budget and that some overruns in expenditure (as well as higher revenues) were attributable to that event.

In the context of the current (1985/86) budget, the authorities had taken additional steps to improve expenditure controls. Noting that for the current fiscal year, the overall deficit, as well as the needed bank financing, was higher than that realized last year, the Tanzanian representatives stated that they had been especially cautious in making revenue estimates due to the uncertainty relating to import financing, notwithstanding the introduction of new tax revenue measures expected to yield nearly T Sh 1.2 billion. Still they felt that the proposed bank financing, estimated at 17 percent of the stock of broad money at the beginning of the year, could be accommodated within a relatively prudent overall credit expansion. To the extent that revenues turn out to be higher, as they felt could happen, and provided expenditure controls become more effective, the recourse to bank financing would be reduced correspondingly. The mission noted that the deficit was still large and needed to be reduced substantially. This would require both some structural changes in the tax system, realistic pricing policies, and reinforced expenditure control. Moreover, the overall deficit was not a true reflection of the underlying fiscal imbalance as domestic interest rates were artificially low and the exchange rate highly overvalued. This would imply even tighter fiscal policies.

For 1985/86, the overall credit expansion was envisaged at T Sh 6.5 billion, equivalent to 21 percent of broad money at end-June 1985, which, after allowing for the above-mentioned credit to the Government, would enable credit to the rest of the economy to expand by about 11 percent. The Tanzanian representatives regarded this expansion as adequate to meet the needs of the economy. The overall expansion of credit, in their view, should lead to monetary expansion broadly in line with the projected increase in nominal GDP. As regards interest rates, the Tanzanian representatives considered the October 1985 increase to be appropriate and adequate for a medium-term recovery program. They felt that they must now wait for the inflation rate to come down to achieve a positive rate of return. Any additional increase in interest rates, in their opinion, would only add to the budgetary deficit and produce an inflationary impact on production costs in the country, while having little or no impact on monetized savings. The staff mission, on the other hand, noted that there existed substantial excess liquidity in the economy, and that realistically at this stage there was little prospect for the inflation rate to come down significantly. In the circumstances, positive real interest rates could only be provided by raising the structure of nominal rates, though accompanied by prudent credit expansion to prevent exacerbating the inflation rate.

The Tanzanian representatives stated that substantial improvements had been achieved in the collection and collation of monetary statistics, following the almost complete destruction of records in the fire which engulfed the central bank building in 1984. To date, such data have been prepared for end-June and end-December 1984, and end-June 1985. It should now be possible to prepare the data on a monthly basis for the second half of 1985 and thereafter, and enable a better monitoring of monetary developments.

4. External policies

The policies initiated with the 1984/85 budget included a depreciation of the Tanzania shilling in June 1984 by 26 percent in foreign currency terms, an expansion in the list of allowable imports under the "own-exchange" scheme, and the introduction of a retention scheme under which exporters were permitted to retain a part (10-15 percent) of their export receipts to finance their import requirements. The Tanzanian representatives stated that the exchange rate adjustment was made to improve the financial position of the parastatals and the competitiveness of Tanzanian exports, and signalled their willingness to use the exchange rate instrument within the context of the adjustment policies. Unlike in the past, however, the change in the rate would not be solely dictated by the need to ensure financial balance in the operations of the parastatals, though that consideration would not be entirely ignored. They recognized that since the last depreciation domestic prices in Tanzania had increased by some 35 percent and had wiped out the competitive benefit provided by that exchange rate action. In the circumstances, a further depreciation could be justified and would be considered in the context of the comprehensive adjustment program being presently contemplated. Furthermore, such an action would be supplemented by a flexible policy to avoid a further real appreciation of the rate.

As regards the working of the "own-exchange" import scheme, the list of allowable imports had been expanded since the introduction of the scheme in early 1984 and now included a variety of goods including building materials, electrical appliances, transport equipment, spare parts, etc. Applications for import licences under this scheme were generally approved freely.

The Tanzanian representatives added that before July 1985 the percentage of export earnings which exporters were allowed to retain was between 10 and 15 percent, with the retention rates subsequently increased to higher levels on a case-by-case basis. The commodities each exporter is authorized to import were specifically listed. The mission commented that the operation of the scheme had already resulted in some improvement in the supply situation. It was essential, however, to move to a realistic exchange rate that would obviate the need to maintain the scheme. In the meantime, if the scheme were to be retained, it should be improved by establishing uniform retention rates for all exporters and by allowing the free transfer of retained funds among exporters. The mission also noted with concern that the authorities had occasionally compelled some parastatals to surrender the retained foreign exchange to the Government to meet its needs and thus introduced uncertainty in the operation of the scheme.

The Tanzanian representatives stated that extensive work was still being done on compiling the external debt and arrears data. New procedures to record the external debt information had been designed and were being implemented. The problem of recording arrears was also being resolved by depositing all local currency counterpart funds in the central bank, although it had not been determined whether the Government or the Bank of Tanzania, or the National Bank of Commerce would bear the exchange losses in respect of accounts already deposited.

As regards the arrears to the Fund, the staff mission recalled the communications received by the Fund from the Tanzanian authorities promising settlement. The staff urged the authorities to settle the arrears at an early date and remain current thereafter, by setting aside for this purpose a part of export and other receipts. Most importantly, Tanzania had to adopt a comprehensive adjustment program, which would increase the inflow of resources to meet the Government's payment obligations.

5. Medium-term prospects

In preparation for the next Consultative Group meeting, the Tanzanian authorities have prepared a tentative medium-term (1985-88) balance of payments scenario, which envisages a relatively gradual introduction of adjustment policies spread over a number of years. The Tanzanian representatives stated that this scenario was still subject to significant revisions and should await finalization before being presented in detail. On this basis, the scenario anticipates that the volume of exports would increase by an average annual rate of about 20 percent and that imports could be maintained at an average annual level of about US$1.2 billion. The Tanzanian representatives stated that the import figure was based on the estimates contained in the Minimum Import Requirements program which the authorities had elaborated after examining the rehabilitation and maintenance needs of the various sectors and taking into account the priorities in the public investment expenditures. This scenario does not make any allowance for either the settlement of external arrears, presently estimated at around US$1 billion, or an increase in the gross external reserves of the Bank of Tanzania, which are presently virtually exhausted.

The Government's proposed scenario projects that during the three years 1986-88, the current account (excluding official grants) would register an annual deficit of US$620 million, compared with a deficit of US$450 million in 1984 and an estimated deficit of US$546 million in 1985. On the basis of the assumption that normal gross capital inflows (including grants) would average about US$470 million annually and that amortization would average about US$180 million, the overall balance of payments deficit would average US$330 million per annum, or nearly US$1.0 billion for the three-year period 1986-88. Taking into account the need to clear the arrears gradually, however, and making some additional adjustments to the Tanzanian projections, especially in relation to the price assumptions for exports and the external debt payments, the staff estimates that the overall balance of payments gap in the Tanzanian scenario could well average about US$475 million annually, or nearly US$1.5 billion for the three-year period 1986-88.

In commenting on the above scenario, the mission considered that the projected increases in the volume of exports were unduly optimistic. It also felt that the policy content of the scenario was both vague and weak. In the circumstances, the policies envisaged were unlikely to result in any significant reduction in the balance of payments over several years to come. In the mission's view, the projected balance of payments gaps could not realistically be considered financeable and the authorities could not expect such a large inflow of exceptional assistance for an indefinite number of years. It would be necessary for the authorities to reconsider the policy package supporting their medium-term scenario so as to ensure (i) a decreasing need for exceptional balance of payments assistance over a definite period of, for example, a maximum of five to six years; (ii) gradually rising and sustainable growth rates that promise some increase in per capita income and consumption at least after the initial couple of years of consolidation and stabilization policies; (iii) gradual settlement of arrears and an eventual prospect for the repayment of external debt; and (iv) some buildup of reserves. The staff indicated that these objectives required a careful elaboration of policies encompassing demand-management and structural reform, and a definite timetable for their implementation.

The Tanzanian representatives stated that they would take the above comments into account and would attempt to revise the medium-term scenario by further strengthening and quantifying their adjustment policies, preferably within the context of a program supported by the use of Fund resources. They continued to emphasize, however, that concomitant donor support must be assured for the adjustment policies to succeed, and, indeed, even be announced beforehand; otherwise, they were concerned that the policies would fail to produce the desired impact on production and exports, and could result in social unrest. Thus, they intended to remain in intensive consultations with the Fund and Bank staff, as well as major donor countries, to ensure a satisfactory outcome of an eventual Consultative Group meeting.

IV. Staff Appraisal

In its appraisal of the policies of the Tanzanian authorities following the 1984 Article IV consultation discussions, the staff stated that "the announced policies [in the context of the 1984/85 budget] are in the right direction in that they would prevent a further deterioration," but encouraged the authorities to take stronger and more comprehensive measures in order to achieve an improvement in the economic and financial situation. In concluding the 1984 consultation, the Executive Board underscored this assessment.

Financial and economic developments since then have more than confirmed the above assessment, with the external situation having worsened markedly. Thus, real GDP is estimated to have grown by 2.5 percent in 1985 as in 1984, the fiscal deficit has been reduced with a deceleration in the rate of inflation to about 27 percent, compared with the rate of 36 percent experienced in 1984. However, the external current account deficit (before grants) is projected at about US$550 million, which is almost 20 percent higher than that realized in 1984. Also, exports have maintained their declining trend, shortages of foreign exchange have become more acute, and external arrears have increased further. The major favorable developments were the increase in agricultural production (attributable partly to weather conditions) that contributed toward easing food shortages in the economy, and some increase in the availability of imported goods brought into the country under the "own-exchange" scheme.

The authorities have made some progress in the implementation of their adjustment policies and, in the fiscal field, succeeded in reducing the overall government deficit. Some cost reductions were also achieved for the parastatals, though not by as much as was hoped, cooperative unions were re-established, and some liberalization was introduced in the marketing of foodgrains. In the external sector, in conjunction with the 26 percent depreciation of the Tanzania shilling in June 1984, the authorities further liberalized the system of "own-exchange" imports and expanded the scope of the export retention scheme, with a view to improving the supply situation.

Both the authorities and the staff share the view that despite the execution of these policies in 1984/85, the economy failed to show any marked improvement and that the external financial situation had deteriorated further. The two, however, differ as to the causes for this failure. The authorities feel that the results would have been more beneficial had the international community reacted positively and furnished adequate external assistance to secure the complementary imports, spare parts, incentive goods, etc.. In the absence of such assistance, extra incentives, e.g., higher producer prices and a depreciated exchange rate, in the opinion of the authorities, were of little avail. The staff, on the other hand, believes that the lack of improvement is mainly attributable to the inadequacy of the policies designed to address the prevailing cost-price distortions and the existing and prospective imbalances in the economy. Not only were the adjustments in the exchange rate and producer prices insufficient, but they were also not supported by the needed effective reforms in the pricing and marketing institutions and arrangements. Thus, while the monopsony of parastatals to purchase produce from the producer was revoked, it was replaced by the reintroduced cooperative unions, which effectively act as purchasing agents for the marketing boards. The system of price controls also remained essentially unchanged, and interest rates remained highly negative. Nevertheless, notwithstanding the developments as regards foreign assistance, the deteriorating trends in the economy had stabilized and must be attributed to the beneficial effects of the measures taken during the year. It is worth noting that agricultural production has increased, but marketed production has stagnated, indicating that either the level of producer prices was still not high enough or that the marketing institutions (including transportation) were inadequate. Accordingly, it would have been more appropriate to address these issues.

The staff shares the authorities' sentiments that a substantial increase in foreign assistance could evoke a more positive response from the economy, but this is not to say that appropriate domestic policies, even in the absence of higher external capital inflows, would not improve the situation. In fact, external assistance could be most effectively used only in the context of a comprehensive juxtaposition of appropriate domestic policies.

In the circumstances, it is regrettable that instead of preserving and strengthening the policy stance introduced with the last year's budget, the authorities have reversed the policy course during the present (1985/86) fiscal year. Thus, by taking no action on the exchange rate in the face of a 35 percent rise in prices between mid-1984 and mid-1985, the authorities have offset the earlier real devaluation and have allowed their currency to appreciate in real terms by about 120 percent since 1978. Similarly, by announcing only a 20 percent average increase in nominal producer prices, the real prices were in fact reduced by about 10 percent, thus practically reversing in one year the increase in real producer prices granted gradually over the past years. Real interest rates have also been allowed to remain substantially negative, thereby continuing to provide distorted signals to savers and investors. The government deficit is also budgeted at around 10 percent of GDP, or some one and one-half percentage points higher than that realized in 1984/85, though with adequate expenditure controls and possibly improved revenue collection the deficit could be reduced.

The Tanzanian authorities apparently now accept, in principle, the need for a comprehensive adjustment. In practice, however, they are envisaging a rather slow pace of implementation of these measures and are insisting that the efficiency of these policies would be assured, and their acceptability enhanced, only if additional foreign assistance would be forthcoming simultaneously with the announcement of the policies. The staff believes that, given the large external debt and a substantial external payments deficit projected for the foreseeable future, the pace of adjustment needs to be fast with the objective of achieving sustainability by about the end of the present decade. In the staff's opinion, it is generally problematic that a vigorous adjustment effort can be sustained for a longer period and, even more importantly, that exceptional balance of payments assistance can be assured beyond that period. Thus, if the adjustment period has to be relatively limited, the necessary adjustment policies would have to be introduced within an even shorter period for their full effects to be realized by the end of the adjustment period. The Tanzanian authorities, therefore, have little margin of flexibility in prolonging the period of adjustment or postponing the introduction of adjustment policies. It is, of course, to be expected that initially some economic hardships would ensue from the implementation of adjustment measures, and that certain sectors would be adversely affected. However, the staff believes that the no-policy-change scenario is not a viable alternative and that hardships would be even more severe than if a comprehensive policy action is launched, even assuming little change in capital inflows. But the staff is confident that such an action would evoke sympathetic international response to alleviate some of the hardships. In this belief, the staff has encouraged the authorities to consider urgently an adjustment package, particularly in the current year when satisfactory climatic conditions have yielded a relatively abundant food crop and the inflationary situation is unlikely to be aggravated.

The main thrust of such a policy package would have to aim at providing appropriate signals to the economy by shifting relative prices. In that context, the need to move and maintain the exchange rate to a realistic level is absolutely pivotal as, in its absence, it is doubtful that a meaningfully effective program could be worked out. Additional elements must include the restoration and maintenance of the real level of producer prices for the export crops, structural reorganization and reform of the marketing institutions, rehabilitation of the transport sector, reduction in the fiscal deficit, reform of the major public enterprises, elimination of the presently negative element in the real level of interest rates, and reform of the present restrictive trade and exchange system.

The staff and the Tanzanian authorities have had additional discussions on the policy reform outlined above. Also, given the importance of the structural issues in various sectors of the economy, the Fund and the Bank staff are closely collaborating in devising an appropriate policy package. The Tanzanian authorities are now seriously considering adopting a realistic and feasible adjustment program, and the staff believes that initial significant actions will be taken soon. The staff has encouraged the authorities to announce them at the earliest so as to start the next fiscal year with an appropriate policy environment for the Tanzanian economy and to be able to mobilize adequate external assistance that would be needed to support these measures.

Tanzania maintains restrictions on payments and transfers for current international transactions, including the accumulation of payments arrears, and a multiple currency practice, all of which are inconsistent with the provisions of Article VIII of the Fund's Articles of Agreement. However, the staff believes that the adoption of comprehensive adjustment policies, including, inter alia, an appropriately flexible exchange rate policy, would permit the elimination of these practices. Accordingly, in the meantime, the staff does not recommend their approval.

V. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to Tanzania's exchange measures subject to Article VIII, Section 2 and 3, and in concluding the 1985 Article XIV consultation with Tanzania, in the light of the 1985 Article IV consultation with Tanzania conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Tanzania continues to maintain restrictions on payments and transfers for current international transactions in accordance with Article XIV, Section 2. In addition, exchange restrictions evidenced by the external payments arrears, and a multiple currency practice as described in SM/86/ , are subject to approval under Article VIII, Sections 2(a) and 3. The Fund urges the authorities to adopt adjustment policies which will permit the elimination of these restrictions.

Tanzania - Fund Relations
(As of December 31, 1985)

I. Membership Status

(a) Date of membership	September 10, 1962
(b) Status	Article XIV

A. Financial Relations

II. General Department (General Resources Account)

(a) Quota: SDR 107.00 million

	SDR million	Percent of quota
(b) Total Fund holdings of Tanzanian dollars:	126.20	117.95
(c) Fund holdings subject to repurchase and charges:	19.19	17.93
Of which: credit tranches	(3.23)	(3.02)
supplementary financing facility	(12.21)	(11.41)
compensatory financing facility	(3.75)	(3.50)
(d) Reserve tranche position:	--	--

III. Current Stand-By or Extended Arrangement and Special Facilities

(a) Current stand-by arrangement: None

(b) Previous stand-by arrangements:

Arrangement	Duration	Amount	Utilization (In millions of SDRs)	Undrawn balance
Stand-by	8/21/75-8/21/76	10.50	--	10.50
Stand-by	9/15/80-6/30/82	179.60	25.00	154.60

(c) Special facilities:

Compensatory financing facility — Approval was given on September 15, 1980 for a purchase equivalent to SDR 15.0 million.

Tanzania - Fund Relations (continued)

IV. SDR Department

(a) Net cumulative allocation	SDR 31.37 million
(b) Holdings:	--

V. Administered Accounts

(a) Trust fund loans:	
(i) Disbursed	SDR 41.04 million
(ii) Outstanding	SDR 33.43 million
(b) SFF Subsidy account:	
(i) Payments by Fund	SDR 1.94 million

VI. Overdue Obligations to the Fund (As of January 22, 1985)	SDR 17.90 million

B. Nonfinancial Relations

VII. Exchange System

The Tanzanian shilling is pegged to a basket of currencies; the middle rate in terms of the U.S. dollar, the intervention currency, was T Sh 16.4993 per U.S. dollar as of end-December 1985.

VIII. Last Article IV Consultation

The last Article IV consultation was concluded by the Executive Board on December 7, 1984 (EBM/84/179). The following decision was adopted:

1. The Fund takes this decision relating to Tanzania's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1984 Article XIV consultation with Tanzania conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes that Tanzania maintains restrictions on payments and transfers for current international transactions and a multiple currency practice, as described in SM/84/256. The Fund urges Tanzania to adopt a more rigorous set of adjustment policies that would permit the elimination of these practices.

Tanzania - Fund Relations (concluded)

Tanzania is on the 12-month cycle for Article IV consultations.

IX. Technical Assistance

Technical assistance missions from the Bureau of Statistics were undertaken to improve the compilation of government finance statistics (March 18-29, 1985) and monetary aggregates (September 2-18, 1985). A member of the CBD panel of experts is assigned as short-term technical advisor on foreign exchange operations of the Bank of Tanzania.

Tanzania: Relations with the World Bank Group

1. Relations

Tanzania joined the World Bank Group in 1962. Beginning with an IDA credit for education in 1963, 60 IDA credits and 19 Bank loans, two of these on third window terms, amounting to US$1,134.5 million have so far been approved for Tanzania. Total disbursements amounted to US$1,118.1 million as of September 31, 1985. In addition, Tanzania has been a beneficiary of 10 loans totalling US$244.8 million, which were extended for the development of the common services and development bank operated regionally by Tanzania, Kenya, and Uganda through their association in the East African Community. IFC investments in Tanzania, totalling US$4.7 million, were made to the Kilombero Sugar Company in 1960 and 1964. The IFC has approved investment in other projects : US$1.7 million in soap manufacturing in Mbeya in 1978; US$1.5 million in metal products manufacturing in 1979; and US$3.2 million for the Amboni sisal rehabilitation project in June 1984.

Bank Group lending in Tanzania has been channelled primarily to (i) agriculture; (ii) transport and communications; (iii) industry; and (iv) education and manpower development. Since fiscal year 1981 new Bank Group lending has been focussed primarily on the rehabilitation of existing productive facilities and the introduction of infrastructure and services of long-term use to the economy (such as power generation and education facilities).

In addition to financing specific projects, the Bank Group has provided nonproject assistance on three occasions in support of government efforts to deal with its balance of payments difficulties.

Lending during fiscal years 1986-90, is currently projected at US$405 million. The composition of the proposed lending program will continue to focus on agriculture and on industrial and infrastructural rehabilitation. A "high case" scenario for fiscal years 1986-90 contemplates a substantially greater (IDA plus special facility) lending program if the Government steps up its efforts to restructure the economy and continues to improve performance in project implementation.

The Bank Group experienced delays on payments from Tanzania during 1985. Some of the payments arrears had been outstanding for over 75 days, and, as a result, the Bank Group suspended disbursement of all loans effective October 9, 1985. The suspension was lifted in December 1985 after Tanzania made some payments; the remaining arrears were less than 60 days overdue.

2. Economic Assessment

A summary of the World Bank staff's current assessment of the Tanzanian economy is as follows:

Despite small increases in GDP in the past two years, per capita incomes have been declining since 1980. Production of the main export crops has been falling in volume terms, capacity utilization in industry is at a low level, and the physical infrastructure of the country has deteriorated. The acute shortage of foreign exchange has contributed to bottlenecks in transportation and other services, and the level of imports is insufficient for the proper functioning of the economy. At the same time external arrears are mounting, and the major portion of the country's medium and long-term debt remains unserviced.

Since 1982 the Government has made a serious effort to introduce policies to arrest the decline in the economy and promote recovery. Although there have been positive results, these measures have fallen short of what was needed to reverse the fall in exports and to ease the foreign exchange shortage. The initial efforts in 1982 and 1983 under the Government's Structural Adjustment Program (SAP) were not strong enough to revive the economy. In June 1984 the currency was devalued. Agriculture producer prices were raised and the marketing structure for crops was changed through the reduction in size and scope of agricultural parastatals and the reintroduction of cooperative societies, in order to stimulate agricultural output. A serious effort was made in the 1984/85 Budget to reduce parastatal deficit and strengthen government finances.

The general effect of these measures has been positive. Liberalization of restrictions on the transport of food crops, along with better growing conditions, has stimulated interregional trade in grain. As a result, the food situation has eased and the rise in food prices has been checked. However, the acute shortage of foreign exchange continues to hinder the performance of the economy. Aid flows have diminished, and inflation has wiped out the benefit of the devaluation and eroded the incentive to farmers of higher nominal producer prices.

In the World Bank's view a strong and durable economic recovery is dependent on three things. Firstly: more appropriate macroeconomic policies, in particular vigorous and sustained action to remove the overvaluation of the currency (the parallel market rate is now around eight times the official rate) and so reduce distortions in the economy and the reliance on administrative allocation of scarce resources. Secondly: sectoral policies that will strengthen incentives to producers, improve marketing efficiency, and begin the rehabilitation of the country's social and physical infrastructure. Thirdly: a substantial increase in the level of external assistance to address bottlenecks in transportation and improve the supply of key inputs, coupled with arrangements for the relief and rescheduling of Tanzania's external debt.

Tanzania--Statistical Issues

1. Outstanding Statistical Issues

The statistical base of Tanzania has major weaknesses including long lags in data availability and limitations in data coverage. One source of these limitations is that in several sectors data are limited to mainland Tanzania only, with little or no coverage of Zanzibar. In addition, there have been such other weaknesses as lack of consistency among data series, deficiencies in data classification, and estimation of aggregates from a limited coverage of components. The situation with regard to the currentness of data has deteriorated since May 1984 when the reporting of the monetary authorities' accounts was disrupted by a fire which destroyed the headquarters of the Bank of Tanzania. In these circumstances, a large part of the data requires adjustments and is often no better than "rough estimates". Among the areas where the information gap has been particularly serious are external debt and arrears, foreign assets and liabilities of the commercial banks, and foreign trade indices.

a. Real Sector

A technical assistance mission is likely to be scheduled for April 1986 to review the methodologies underlying the compilation of data on prices, production, and external debt and to suggest improvements in these areas. A task of the proposed mission will be to explore with the authorities the possibility of their compiling a new CPI, based on a new household survey, that would incorporate both controlled/subsidized prices and free market prices.

b. Government Finance

The 1984 GFS Yearbook contains consolidated central government data for the years 1972-74 and only budgetary revenue and expenditure data for the period 1975-81. This is because the government finance statistics' correspondent has encountered difficulties in completing the government finance statistics' questionaries sent by the Bureau, following changes made some years ago in the Tanzanian accounting system. However, in March 1985, a Bureau technical assistance mission visited Tanzania and developed procedures for the compilation of government finance statistics, including the expansion of the coverage of data to include transactions of extra-budgetary units. Additions of more current data to the IFS data series on government finance, which at present end with the year 1979, await the compilation of improved statistics as a follow-up to the work of the technical assistance mission.

c. Monetary accounts

A money and banking statistics mission visited Dar es Salaam in September 1985. The 18-month lag in currentness has been mainly due to the fire at the Bank of Tanzania (BOT) in mid-1984 which destroyed all records; no BOT accounts have been produced since then. Unconsolidated commercial bank returns through March 1985 are available.

While there are no major problems with the National Bank of Commerce's (NBC) new reporting system, the large discrepancy between NBC foreign sector accounts and those of correspondent banks has not been resolved. A task force working on the clearing process of the "nostro" accounts has been able to reduce the discrepancy, but is not expected to complete its work until mid-1986.

d. Balance of Payments

Tanzania reported balance of payments data through the second quarter of 1982 in September 1983. Since then, no data have been reported.

2. Coverage, Currentness, and Reporting of Data in IFS

The table below shows the currentness and coverage of data published in the country page for Tanzania in the January 1986 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the Bank of Tanzania, which during the past year have in general been provided on an irregular basis.

Status of IFS Data

		Latest Data in November 1985 IFS
Real Sector	- National Accounts	1982
	- Prices	Q4 1984
	- Production	n.a.
	- Employment	n.a.
	- Earnings	n.a.
Government Finance	- Deficit/surplus	1979
	- Financing	1979
	- Debt	n.a.
Monetary accounts	- Monetary authorities	Q2 1984
	- Deposit money banks	Q3 1983
	- Other financial institutions: Post Office Savings	Dec. 1984
External sector	- Merchandise trade: Values	Q2 1984
	Unit Value Exports (by commodities)	Q2 1984 1/
	- Balance of payments	Q2 1982
	- International reserves	May 1985
	- Exchange rates	November 1985

1/ Data on unit value of coffee and cotton exports (Wholesale price) are available through September 1985 and on unit value of exports (Wholesale price) through July 1985.

TANZANIA - Basic Data

Area, population

Area		945,100 square kilometers
Population:	Total (1984)	21.1 million
	Growth rate	3.4 percent

	1981	1982	1983	1984	1985
	(In millions of Tanzanian shillings)				
Gross domestic product					
At factor cost					
(constant 1966 prices)	24,163	24,475	24,368	24,972	25,596
Agriculture	10,854	11,140	11,259	11,546	11,950
Manufacturing and Mining	1,997	1,675	1,532	1,356	1,153
Other	11,312	11,660	11,577	12,070	12,493
Gross domestic product at current market prices	50,839	60,508	65,976	75,658	91,576
National consumer price index					
(1970 = 100)					
NCPI (Annual charge)	25.6	28.9	27.1	36.0	27.0

	1981/82	1982/83	1983/84	1984/85 1/	
	(In millions of Tanzania shillings)				
Central government budget					
Total revenue	10,101	11,819	13,995	18,855	20,160
Tax revenue	9,078	11,252	13,407	18,231	19,300
Nontax revenue	1,023	567	588	624	860
Total expenditure and net lending	19,182	18,442	20,894	25,699	27,403
Recurrent expenditure	13,980	14,062	16,174	20,376	21,782
Development expenditure	5,196	4,359	4,733	5,308	5,606
Net lending	6	21	-21	15	15
Overall deficit (checks-issued basis) 1/	-9,081	-6,623	-6,891	-6,844	-7,243
Adjustment to cash and other items (net)	1,213	-412	-154	84	--
Overall deficit (checks-cashed basis) 1/	-7,868	-7,035	-7,045	-6,760	-7,243
Grants	1,656	1,593	1,234	1,892	1,685
Net foreign borrowing	1,204	970	230	608	-9
Domestic nonbank financing	780	469	507	1,231	536
Domestic bank financing	4,228	4,003	5,074	3,029	5,031

	1981 Dec.	1982 Dec.	1983 Dec.	1984 Dec.	1985 June
	(In millions of Tanzania Shillings, end of Period)				
Money and credit					
Domestic credit	21,957	26,234	30,378	37,024	40,392
Of which:					
government	(14,176)	(17,763)	(20,880)	(25,432)	(27,028)
Money plus quasi-money	18,105	21,787	24,664	30,198	32,885

1/ Before grants.

TANZANIA - Basic Data (concluded)

	1981	1982	1983	1984	1985 est.
Balance of payments	(In millions of U.S. dollars)				
Trade balance	-599	-682	-440	-471	-646
Exports, f.o.b.	(563)	(413)	(379)	(369)	(326)
Imports, c.i.f.	(-1,162)	(-1,095)	(-819)	(-840)	(-972)
Services (net)	51	13	-15	-43	-30
Private transfers (net)	22	25	19	63	130
Current account	-526	-644	-436	-451	-546
Government transfers	107	94	84	96	104
Medium- and long-term borrowing	180	240	150	-74	-19
Inflows	(230)	(285)	(253)	(183)	(200)
Outflows	(-50)	(-45)	(-103)	(-257)	(-219)
Suppliers' credits (net)	101	58	102	110	-32
SDR allocation	6	--	--	--	--
Exceptional financing	112	92	61	49	100
Other capital movements and errors and omissions	18	67	39	111	114
Overall balance	-2	-93	--	-159	-279
Monetary movements)	2	93	--	159	279
Arrears	22	76	45	183	283
Net foreign assets (increase -)	-20	17	-45	-24	-4
Gross official foreign reserves 1/ (end of period)	52.8	39.1	62.5	38.3	38.8
In weeks of imports	2.3	1.9	4.0	2.4	2.2
External public debt					
Disbursed and outstanding (end of period) (including trade credit)	2,200	2,450	3,119	3,001	3,181
Debt service as percent of exports of goods and services					
Excluding the Fund	11.7	16.0	28.9	60.9	49.7
Including the Fund	16.7	19.4	35.3	66.4	53.5

Sources : Data provided by the Tanzanian authorities and staff estimates.

1/ Gross foreign assets held by the Monetary authorities and the National Bank of Commerce.