International Monetary Fund

Tanzania and the IMF

Press Release:
IMF Executive Board Completes Second Review Under Policy Support Instrument for Tanzania
May 6, 2011

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Tanzania: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

April 15, 2011

The following item is a Letter of Intent of the government of Tanzania, which describes the policies that Tanzania intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Tanzania, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

LETTER OF INTENT

Dar es Salaam
April 15, 2011

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. Strauss-Kahn:

1. Tanzania has continued to record good progress in the implementation of its economic and financial programme under the Policy Support Instrument (PSI). The Government remains committed to maintain sound policies with the aim of sustaining macroeconomic stability and accelerating economic growth and poverty reduction.

2. Performance against PSI targets remained on track with all quantitative assessment criteria for December 2010 and all continuous assessment criteria being met, some with substantial margin. Similarly, progress has been made in implementing the structural reform program.

3. Based on the preliminary data on economic performance during the first nine months, and performance in some key indicators during the fourth quarter of 2010, GDP growth for 2010 is estimated to have reached 7.0 percent. Economic activity is projected to slow down during 2011 owing to the projected below normal rains and power shortages during the first half and higher international oil prices. Owing to the unexpected power crisis and the uncertainty regarding its length and severity, the GDP forecast is subject to higher than usual uncertainty. However, in the medium term, growth is projected to stabilise above 7 percent.

4. Annual headline inflation increased to 7.5 percent in February 2011 from 5.6 percent in December 2010 and 7.2 percent in June, 2010 mainly due to increases in the prices of food items and energy reflecting global trends, as well as the 18 percent rise in electricity tariff starting in January 2011. Going forward, and incorporating a number of cost push factors, inflation is targeted at 7.5 percent by end June 2011. Inflation is projected to decline to around 5 percent in the medium term.

5. The Government's policy framework will continue to focus on sustaining the macroeconomic stability, including fiscal sustainability, through implementation of appropriate fiscal and monetary policies, with the aim of powering the economy to its growth trajectory. The policy framework will include implementation of measures to increase revenue efficiency; and scaling up good-quality investment spending to address the infrastructure bottlenecks and sustain gains realized in social sectors, while containing growth in recurrent expenditure. In addition to financing infrastructure development through concessional and non–concessional borrowing, the Government will improve value for money of its infrastructure spending, including through Public Private Partnership (PPP) arrangements.

6. The Government is continuing with implementation of it structural reform agenda based on its four core reform programmes—the Public Sector Reform Programme, the Public Financial Reform Programme, the Local Government Reform Programme, and the Legal Sector Reform Programme—in order to enhance efficiency in resource utilization and service delivery. In addition, the Government is continually improving the business environment to support private sector led growth, through the Roadmap for Improving the Business Climate that was adopted by stakeholders in 2010.

7. Following discussions and consultations with the Fund staff, I hereby transmit this letter of intent and the attached Memorandum of Economic and Financial policies, which reviews the implementation of the programme during the first half and the projected outturn for 2010/11, and describes the objectives and policies that the Government intends to pursue during the fiscal year 2011/12 and over the medium term.

8. The Government of Tanzania requests the completion of the second review under the PSI in support of good performance and policy intentions going forward. The Government is confident that the policies set forth in the attached MEFP are adequate to achieve the objectives of its programme and will, in further consultation with the Fund, take any appropriate measures for this purpose. We will regularly update the Fund on developments in our economic and financial policies, and provide the data needed for the monitoring of the programme. In addition, the Government will consult regularly with the Fund on any relevant developments at the initiative of the Government or the Fund.

9. The Government of Tanzania intends to disseminate this letter and the attached MEFP as well as related Fund staff reports, and hereby authorizes the IMF to publish the same on its website after consideration by the Executive Board.

Yours Sincerely,

/s/

Mustafa H. Mkulo

MINISTER FOR FINANCE
UNITED REPUBLIC OF TANZANIA

Attachments:
Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

ATTACHMENT I. TANZANIA: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

April 15, 2011

Recent Macroeconomic Developments

1. Tanzania's economy has continued on a recovery path from a slowdown associated with the global economic downturn. Preliminary national accounts statistics indicate that real GDP (at market prices) grew by 6.7 percent in the first three quarters of 2010 compared with 4.8 percent in the corresponding period of 2009. The growth was contributed mostly by trade and services (22.2 percent), agriculture and fishing (20.7 percent), transport and communication (10.7 percent), and manufacturing (10.0 percent). Following good performance in the first three quarters, and an indication of good performance in key indicators in manufactured exports, and construction, the earlier projected GDP growth of 7.0 percent in 2010 is likely to be achieved.

2. Following favorable weather conditions in 2009/10, food supply improved in the East African region, leading to a reduction in inflationary pressures. Inflation took a downward trend in 2010, from 12.7 percent in October 2009 to 4.5 percent in September 2010. The National Bureau of Statistics (NBS) released the revised CPI series beginning October 2010. Based on this revision, inflation was 4.2 percent in October 2010, but started inching up from November 2010 to 5.6 percent in December 2010, mainly on account of an increase in prices of some food items and energy. In January 2011, the pressure was exacerbated by an 18 percent increase in electricity tariffs, and inflation rose in February to 7.5 percent.

3. The trade account for the year ending December 2010 experienced a widening deficit with imports increasing faster than exports partly due to high prices of oil in the world market, and partly due to substantial recovery of capital and intermediate goods imports. Imports of goods and services rose by about 19 percent in 2010 compared with a decline of 13 percent in the preceding year. Improvement in global demand also led to an increase in world commodity prices, resulting in improved export performance. Exports of goods and services rose by about 23 percent, with gold remaining dominant, largely due to the increase in export prices. In the first half of 2010/11, the current account deficit decreased by 9.9 percent to USD 798 million compared with a deficit of USD 886 million recorded in the corresponding period last year following a significant increase in official current transfers.

4. However, an upward trend in oil prices in the world market is taking place given the escalating instability in the Middle East and North Africa. This will in turn increase the import bill in the second half of 2010/11. In addition, hydro power generation has been substantially reduced due to inadequate short rains during 2010/11 season, leading to power rationing that may be exacerbated if the long rains in 2011 are below normal, as is projected. The ongoing power rationing is expected to negatively affect exports of manufactured goods in the second half of 2010/11. Consequently, the current account (excluding official current transfers) for 2010/11 is projected to record a deficit equivalent to 12.6 percent of GDP compared with 11.4 percent of GDP in 2009/10. On the other hand, the overall balance of

payments is projected to record a surplus of USD 334 million. Official gross reserves by end-June 2011 are estimated to increase to USD 3,831 million, sufficient to cover 4.7 months' imports of goods and services.

Performance under the program

5. Performance against PSI targets for end-December 2010 remained on track with all quantitative assessment criteria being met (Table 1). In particular, net international reserves amounted to USD 3,594 million, above the target by USD 332 million, while the net domestic financing of the Government budget was TSh 109 billion, which was below the ceiling by TSh 356 billion. The average reserve money closed at TSh 3,524 billion, below the target by TSh 34 billion.

6. Progress has been made in implementing the structural reform benchmarks, although slower than planned in some areas (Table 2). A report on outstanding payment claims as at end December 2010 was prepared and a core inflation index has been introduced, while the Medium Term Debt Strategy (MTDS) report will be published by end June 2011. However, while progress has been made on each of the remaining structural benchmarks, it was not possible to complete them yet, and thus the Government requests their re-phasing as discussed below.

Fiscal policy

7. Fiscal policy in the first half of the fiscal year remained within the PSI targets, thanks to a proactive management of spending. The deficit before grants stood at TSh 1,762 billion (5½ percent of GDP), or TSh 139 billion lower than programmed. External program financing exceeded PSI projections by TSh 321 billion, allowing the Government to meet the NDF target with a significant margin. The Government's cash-budgeting system helped contain monthly expenditure within available resources in order to meet the domestic financing target.

8. During the first six months of 2010/11, government revenue increased significantly but fell short of budget estimates. Total domestic revenue collection including Local Governments Authorities (LGAs)' own sources increased by 20 percent compared with last year. Revenue collection reached TSh 2,779 billion, exceeding PSI targets by about 4 percent, helped by the continuous implementation of measures outlined in the November 2010 MEFP to strengthen revenue collection. However, revenue collection fell significantly short (about 10 percent) of budget estimates, reflecting the ambitious revenue targets, including for VAT and excises. Large tax exemptions (about 1/3 of gross tax collections) continued to erode the tax base and hamper revenue collection performance.

9. Total cash expenditure for the first half of 2010/11 remained within the PSI envelope, but large unpaid claims have surfaced from infrastructure projects. The execution of expenditure during the first half was held to 91.3 percent of budget estimates, while

protecting priority sectors, including health and education, from budget cuts. Recurrent expenditure was in line with estimates, while development expenditure stood at 74 percent of the estimates. In addition, significant claims (TSh 255 billion or 0.7 percent of GDP) were accumulated because spending on long-term infrastructure projects went faster than anticipated under the budget, thus pushing total expenditure committed in the first half of the year above the target. Foreign financed development expenditure experienced delays in disbursement of project funds as well as delays in data reporting of direct-to-project funds.

10. Total grants for the first half of 2010/11 were TSh 1,000 billion, equivalent to 75 percent of estimate, reflecting delayed disbursement of foreign project funds and data reporting of project grants. Disbursements of budget grants were TSh 654 billion, while basket support funds amounted to TSh 243 billion. The higher than estimated disbursement of GBS and basket funds was mainly due to frontloading and exchange rate fluctuations. Total foreign financing of the deficit after grants was 8 percent above the budget estimate for the period, mainly due to higher than projected disbursement of general budget support and basket funds. On the other hand, net domestic financing was 23 percent below the estimated TSh 465 billion due to delays in execution of development projects.

Prospects for the reminder of FY2010/11

11. The Government has taken steps to accelerate the implementation of administrative revenue measures to improve revenue collection performance, but significant risks cloud the outlook to end June 2011. Data for end-February indicates some improvement in domestic revenue collection, but growing downside risks are emanating from the impact of the protracted power rationing on corporate activity and profits. As a result, revenue collection is projected to reach 16.1 percent of GDP for FY2010/11, slightly below the PSI targets and around 90 percent of budget estimates.

12. The Government has made progress in raising funds from external non-concessional borrowing. Negotiations with a reputable bank for USD 197.8 million are at advanced stage and the Mandate Letter has already been signed. The Government is currently reviewing the loan agreements to ensure suitability of loan terms. This loan will be used for the installation of 100MW gas fired plant in Dar es Salaam and 60MW heavy furnace oil power plant in Mwanza. The Government is also discussing a Mandate Letter for USD 250 million with a second bank, and the loan agreement is expected to be signed before end June, 2011. Taking into account commitment and insurance fees estimated at about USD 40 million, the total amount available from these two loans to finance expenditures in 2010/11 is expected to be about USD 408 million. The Government is cautiously scrutinizing additional proposals from these and other financial institutions to identify possible candidates to raise the remaining balance from the USD 525 million ceiling on non-concessional financing.

13. Spending will be adjusted to available resources while protecting key expenditure items including investment and priority social spending. Accordingly, the mid-year budget

review capped total expenditure at 95 percent of estimate and 29.6 percent of GDP. In addition, spending was reallocated to allow payment of TSh 255 billion in unpaid claims. The Government has halted the process of signing new contracts for infrastructure projects that are not funded. Given the severity of the power outage, it is essential to step up investment in electricity generation. In addition, further pressures could also arise in recurrent spending due to the need for increased fuel purchases to supply generators to maintain power availability in the very near term. Any increased expenditures related to the power crisis will be covered by reducing planned spending in other areas. In all, the revenue shortfall and additional power-related spending will call for a further adjustment in expenditure of about 1.1 percent of GDP. To cope with these additional shocks, the Government will focus cuts mainly on lower priority areas, and where possible delay the implementation of some projects.

14. The Government continues with the efforts to enhance the capacity of Cash Management Unit (CMU) in order to improve in-year cash flow projection and accordingly advise the cash management committee. This will include enhancing the capacity of CMU to perform detailed historical trend analysis as a basis for projecting and scrutinizing Ministries and Development Agencies (MDAs) submissions.

15. The Government has begun to compile outstanding payment claims from MDAs on a quarterly basis, while strengthening commitment control and expenditure tracking and monitoring. The Government monitors expenditure development arising from such claims to facilitate a more accurate projection of cash requirements. The claims once verified are incorporated and submitted for payment through the monthly cash budgeting committee, pending available resources. The Government ensures that such claims are settled before the end of the fiscal year to avoid accumulation of arrears in the following fiscal year. On a provisional basis, the unpaid claims of three ministries have been reported to the Fund. Now that the data is available for all MDAs, it will be shared with the Fund on a quarterly basis, with a four week lag.

16. The Government has developed the National Social Protection Framework (NSPF) through extensive consultation with key stakeholders. The NSPF establishes guidelines for stakeholders involved in the planning, funding, and provision of social protection measures in line with MKUKUTA II, and provides a mechanism for collective state-led measures implemented by the Government and its partners. However, the elections and formation of a new government have delayed the formal adoption of this framework. As a result, the Government requests a re-phasing of the related structural benchmark to end-June 2011. To further assist in meeting the goals of MKUKUTA II, an index for monitoring priority social spending is also being developed. However, this has proven technically more challenging than anticipated, and thus the Government requests a re-phasing of the related structural benchmark from end-March to end-December 2011. The Government is also seeking technical assistance from a development partner to accelerate the work and support capacity building in this important area.

17. Foreign assistance in the form of General Budget Support and basket funds are expected to be realized broadly within budget estimates. General budget support will be slightly higher than the approved budget especially due to fluctuations in the exchange rate, partly contributing to the narrowing of the resource gap emanating from domestic revenue shortfall. Thus, in 2010/11 foreign grants are expected to be 5.6 percent of GDP, while loans (including non-concessional borrowing) will be 5.5 percent.

18. The Government has, with the help of IMF-World Bank technical assistance, in January 2011 adopted a new tool to assist in formulating a Medium Term Debt Strategy (MTDS). The new tool incorporates non-concessional borrowing and contingent liabilities, including those arising from government guarantees. Significant progress has been made on developing an MTDS consistent with resource needs under the MKUKUTA II and reflecting contingent liabilities, but the process is not yet complete. Thus, the Government is requesting a re-phasing of the related benchmark from end-March 2011 to end-June 2011. The Government also intends to establish a unified data base of debt statistics, under a single monitoring unit, and proposes that this be added as a new structural benchmark to be completed by end-December 2011

19. According to the report on Debt Sustainability Analysis (DSA) published in December 2010, Tanzania's public debt is expected to remain sustainable. However, the Government recognizes that debt sustainability is sensitive to the terms of borrowing and its utilization, and is committed to contracting external debt only on reasonable terms, and to ensuring that all non-concessional debt is used to finance high-priority investment projects. The Government will continue to control the issuance of guarantees on loans to various public institutions in order to maintain sustainability of the public debt.

Monetary and exchange rate policies

20. The pace of credit to private sector growth continued to pick up in the first seven months of 2010/11, reflecting recovery of banks' confidence in the economy following easing of the global financial crisis. Credit to private sector grew by 21.5 percent in January 2011, far above the 9.8 percent recorded in the year ending January 2010. Consistent with this development, broad money (M3) grew by 25.4 percent, compared with 20.1 percent recorded in the year ending January 2010. The fastest growing component of M3 was foreign currency deposits following the strengthening of US dollar against major currencies and the shilling which led to higher demand for US dollars. The Shilling depreciated against the US dollar by 6.1 percent in the first seven months of 2010/11.

21. The Bank's policy rate remained unchanged. Nevertheless, as credit growth accelerated and banks' excess reserves declined, money market interest rates increased in the last quarter of 2010. The overall Treasury bill yield increased to 7.14 percent in January 2011, from 3.33 percent in June 2010, while the overnight interbank rate increased to 7.93 percent in January 2011, from 0.97 percent in June 2010. The same pattern was also

observed in the Treasury bond market, where average yields increased across all maturities. This began to reverse in mid February 2011, as Treasury securities tender sizes were reduced, coupled with build up of banks' reserves following seasonal repayment of agricultural credit. The overall weighted average Treasury bill yield fell to 5.70 percent by mid March 2011 and the overnight interbank rate fell to 2.0 percent.

Programme for 2011/12 and the Medium term

22. The Government will continue to focus on sustaining macroeconomic stability through implementation of prudent monetary and fiscal policies. Building on the MUKUTA II framework, the Government is in the process of developing a five year development plan for 2011/12 – 2015/16, whose main thrust is on unlocking Tanzania's growth potentials. The Plan will prioritize key interventions and orderly sequence in their implementation so that they can complement each other to enable effective and optimal resource allocation. Focus will be on key areas within agriculture, infrastructure, investment in human resources, environmental sustainability and land management. The Government will sustain achievements made in social sectors and improve value for money of its infrastructure program, including through private sector participation in infrastructure development.

23. The Government is continuing with implementation of its structural reform agenda based on four core reform programmes—the Public Sector Reform Programme, the Public Financial Reform Programme, the Local Government Reform Programme, and the Legal Sector Reform Programme— in order to enhance efficiency in resource utilisation and service delivery. In addition, the Government is continually improving the business environment to support private sector led growth, through a Roadmap for Improving the Business Climate that was adopted by stakeholders in 2010. The Roadmap identified several "quick wins" and short-term actions that the Government intends to implement quickly.

24. Real GDP growth is expected to slow in 2011 on account of the ongoing power rationing, projected lower than normal rains in the 2011 crop season and soaring international oil prices. As the global economy continues to recover and demand for exports improves, real GDP growth is expected to return to an average rate above 7 percent. Over the medium term, growth is expected to increase further. On the other hand, it is expected that the continued surge in world oil and food prices will increase headline inflation to 7.5 percent in June 2011. In the medium term, it is expected that inflationary pressures will ease, with inflation slowing to 5.5 percent in 2012 and remaining around 5 percent thereafter.

Fiscal policy

25. As a baseline projection, domestic revenue is expected to trend upward given the expected recovery in economic activities and continued efforts to strengthen tax administration, and implement measures to increase revenue efficiency and bring it in line with other countries in the East African region. Thus, in the baseline the revenue to GDP ratio is projected at 16.3 percent of GDP in 2011/12. The Government is committed to

including in the budget realistic estimates of the revenue impact of measures in the tax area that are not included in the baseline. This will ensure that the overall projection of revenues in the budget provides a reliable foundation for determining the level of spending in the budget.

26. Foreign grants and loans are projected to remain at 6.4 percent of GDP in 2011/12, with concessional loans also little changed from 2010/11 at 3.3 percent of GDP. Non-concessional foreign borrowing is projected at an additional 2.1 percent of GDP, with net domestic financing remaining at 1 percent of GDP. The Government will ensure that resources realized from non-concessional borrowing are utilized to address critical infrastructure gaps, including increasing capacity for energy generation and improving transportation networks, with borrowing decisions made in line with Government's commitment to sustaining macroeconomic stability consistent with the PSI programme.

27. Based on the available financing and the need to maintain fiscal sustainability, the deficit after grants will be reduced to 6 percent of GDP in 2011/12. Given this deficit and the baseline projection for revenues, total expenditure is projected to decline to 28.3 percent of GDP. Only realistically projected increases in baseline revenues on the basis of quantified estimates of policy changes will be reflected in total expenditure. Growth in the wage bill will be kept in line in nominal GDP to safeguard Tanzania's competitiveness. While making room for increases in priority spending, including in health and education, total spending on goods and services will be brought to their level relative to GDP prior to the global financial crisis. In addition, the Government will continue to improve the quality of public investment, and over the medium term will ensure that reported public investment refers only to actual accumulation of physical capital. In addition, the contingent reserve in the 2011/12 budget will be increased to five percent of total expenditure to create a sufficient buffer for unexpected developments on revenue, spending, or financing.

28. In the medium term, the Government will implement revenue policies aimed at improving tax administration and maximizing domestic revenue collection. The Government will undertake various reforms to strengthen domestic resource mobilization and limit tax leakages. This will be achieved through: (i) improving tax structure; (ii) widening the tax base by bringing the informal sector into the tax net, implementing the properties and businesses formalization programme and introducing National Identity Cards; (iii) strengthening bloc management, supervision and managing performance; (iv) intensifying enforcement of collection of tax arrears and tax compliance; and (v) improving tax administration by implementing the Tanzania Revenue Authority's Third Five-year Corporate Plan. In addition, the Government will undertake policy reform measures in non tax revenue collection, and strengthen the management and control of tax exemptions.

29. The Government's medium-term fiscal policy will help to ensure fiscal sustainability. The overall deficit after grants is projected to gradually narrow from 6.5 percent estimated

for 2010/11 to below 4 percent by 2015/16, benefitting from the projected improvement in domestic revenue collection and decline in overall expenditure. The projected deficit is expected to be financed by both concessional and non-concessional loans. The proceeds from non-concessional borrowing are intended to be used to support development projects particularly infrastructure development. As a result, Tanzania's total public debt will remain below 45 percent of GDP over the medium-term.

Monetary and exchange rate policies

30. The Bank of Tanzania will continue to implement monetary policy that is consistent with low inflation, while providing room for private sector credit growth. Upside risk to inflation from the second round effect of tariff hikes, power rationing, and increasing global oil and food prices remain. The Bank of Tanzania will monitor inflation closely and make appropriate adjustments to monetary targets in the events that core inflation begins to exhibit indications of rising inflationary pressures. During 2011/12, the annual growth rate of average reserve money and M3 is targeted at 19 percent, which should provide room for private sector credit to grow by 21 percent in the year ending June 2012.

31. The exchange rate will remain market determined and the Bank of Tanzania will participate in the foreign exchange market with the main objective of implementing its monetary policy and smoothing short-term exchange rate volatility, while maintaining an adequate level of international reserves.

Financial sector stability

32. The Bank is committed to ensure stability and soundness of the financial sector. In this regard, the Bank has prepared an MOU to establish a financial regulators forum to assume joint responsibility of safeguarding the stability of the financial system, and coordinating crisis management and resolution. The Bank of Tanzania has also introduced new measures to ensure availability of liquidity to the banking system, should the need arise. Firstly, measures to recognize impending liquidity shortfalls have been stepped up by strengthening surveillance of the banking system. This is done on a daily basis by examining developments in a set of leading indicators. Secondly, access to emergency facilities at the Bank of Tanzania has been eased to allow commercial banks to have access to these facilities on short notice and at reasonable rates. In addition, a mission to develop further options for resolution of crises was concluded in February 2011 and a report containing recommendations is expected in the fourth quarter of 2010/11. The first published Financial Stability Report was issued in December 2010, and the next half year report will be published by May 2011. In light of the actions taken to date, the Government requests that the structural benchmark on the establishment of a framework for emergency liquidity management be dropped.

33. Efforts are underway to reform the Deposit Insurance Board (DIB). A final report and recommendations of the study on legal and operational framework for DIB has been

submitted by the consultant. A proposal for the reformed DIB will be considered by the Inter-Institutional Committee before approval by the Government.

34. Data on financial soundness indicators for end December 2010 indicate that the banking system continues to be sound and stable on the whole. However, there was a significant increase in non-performing loans (NPLs) in the second half of 2010. This was a result of targeted examination on some key banks which revealed that a number of loans, granted to sectors that had been affected by the global financial crisis, had not been properly reclassified and provided for as required for bad and doubtful debts. This was followed by full scope examination of those banks. The banks have been directed to strengthen their credit risk management systems to reduce the NPLs. According to self assessment on the 25 Basle I Core Principles for effective banking supervision, the Bank has fully complied with 8 Core Principles and largely complied with 16 Core Principles, but is materially not compliant with one Core Principle. This will be addressed in the context of preparation for the issuance of a sovereign bond.

35. Progress has been made in the establishment of a credit reference system. Credit Reference Bureau and Databank Regulations, were finalized and gazetted. The bidding documents for a databank solution provider have been finalized and interested vendors have been invited to purchase the same. The expected deadline for submission of bids is March 23, 2011. A public notice intended to entice interested and eligible private credit reference bureau operators to apply for a license has also been issued.

36. The National Social Security Authority has been formed and the CEO of the Authority was appointed in September 2010. The regulator is now working in consultation with the Bank of Tanzania to prepare investment guidelines for pension funds, and has initiated an actuarial review of the pension funds as part of this process. Issuance of the investment guidelines was a structural benchmark under the PSI for end-March 2011, but the Government is requesting a re-phasing of the benchmark to end-September 2011 in order to allow the actuarial review to be completed. Tanzania received technical assistance in February 2011 to assist in the implementation of a reporting system for the collection of data from insurance companies and pension funds. These reports will be compiled, disseminated, and reported to the Bank of Tanzania on a quarterly basis, beginning with the quarter ending June 2011.

37. Regarding the national payment system, the Bank has continued to support banks and mobile network operators in development of mobile banking through a mobile payment policy partnership. Mobile Payment Regulations have been drafted by the Bank to promote financial inclusion of the under-banked and unbanked. These will be reviewed by stakeholders before June 2011. In addition, utilization of TISS has continued to expand reaching 50.3 percent of total government expenditure by January 2011. It is expected that

once most ministries make payments through TISS, cheque capping for Government payments exceeding TSh 10 million will be implemented.

38. Following the ratification of the Common Market Protocol by all EAC Partner States in July 2010, EAC central banks have taken steps towards implementing a Cross Border Payment System, which will help to promote trade among the East Africa countries. Business and technical functional specifications for the development of the East African Payment System (EAPS) were agreed by all members and signed-off in September 2010. The EAPS regulatory framework is in the process of being finalized. In the meantime, the enhancement and testing of the system has commenced. The system will go live in the fourth quarter of 2010/11.

39. Measures to liberalize capital account continue to be implemented following their inclusion in the East African Common Market Protocol. A National Task Force which was formed to review national laws has identified a list of laws and regulations which need to be amended to facilitate removal of existing restrictions on capital and financial account transactions. In the meantime, the Bank has started reviewing the Foreign Exchange Act of 1992.

Statistical issues

40. Revision of the composition of the consumer basket was finalized by the National Bureau of Statistics (NBS) on the basis of results from the 2007 household budget survey (HBS) and the new CPI series was released as planned in November 2010. The rebased CPI follows the internationally recommended COICOP and has a lower weight for food and larger weights for communications and some other household expenditure items. The new classification incorporates a number of methodological improvements, including the use of geometric mean for compiling elementary index aggregates, the use of an improved index compilation system, and improved procedures for collecting and processing prices. The reference period was also changed from December 2001 to September 2010. The revision of CPI compilation makes it comparable to most other EAC member states. Work is now underway to develop a harmonized core inflation index for the EAC. In the meantime, the NBS is publishing a CPI measure excluding food and energy prices as a proxy for core inflation, thus meeting the related benchmark under the PSI.

Programme Monitoring

41. Progress in the implementation of the policies under this program will be monitored through assessment criteria (ACs), indicative targets (IT), and structural benchmarks (SBs) detailed in the attached Tables 3 and 4 and through semi-annual reviews. The modification of the end-June 2011 AC on net international reserves is being requested while ACs for end-December 2011 are being proposed, to be assessed respectively at the third and fourth reviews. The third review is expected to be completed by end-December 2011 and the fourth review by end-May 2012. The attached Technical Memorandum of Understanding contains definitions and adjustors.

Table 1. Tanzania: Quantitative Assessment Criteria and Indicative Targets, September–December 2010

	September				December			
	Indicative Targets	Adjusted Targets	Actual	Met?	Assessment Criteria	Adjusted Targets	Actual	Met?
	(Billions of Tanzania shillings; end of period, unless otherwise indicated)							
Net domestic financing of the government of Tanzania (cumulative, ceiling) [1,2]	250	449	507	X	465	465	109	✓
Average reserve money (upper bound) [3]	3,406	3,406	3,451	X	3,558	3,558	3,524	✓
Average reserve money target [3]	3,372				3,523			
Average reserve money (lower bound) [3]	3,338				3,488			
	(Millions of U.S. dollars; end of period)							
Net international reserves of the Bank of Tanzania (floor) [4]	3,061	2,862	3,233	✓	3,262	3,262	3,594	✓
Accumulation of external payments arrears (ceiling)	0	…	0	✓	0	…	0	✓
Contracting or guaranteeing of external debt on nonconcessional terms (continuous ceiling) [5]	525	…	0	✓	525	…	0	✓
Memorandum item:								
Foreign program assistance (cumulative grants and loans) [1]	329	…	192		643	…	879	

Note: For precise definitions of the aggregates shown and details of the adjustment clauses, see the Technical Memorandum of Understanding (TMU).

[1] Cumulative from the beginning of the fiscal year (July 1).
[2] To be adjusted upward by up to TSh 250 billion for the U.S. dollar equivalent of a shortfall in foreign program assistance from the amounts shown in the memorandum item.
[3] Assessment criteria and benchmarks apply to upper bound only.
[4] Floor will be adjusted downward for any shortfall in foreign program assistance from the amounts shown in the memorandum item up to the equivalent of TSh 250 billion.
[5] To be used exclusively for infrastructure investment projects. Continuous assessment criteria; ceiling applies throughout the year.

Table 2. Tanzania: Structural Benchmarks for 2010/11

Measure	Target Date	Status
Poverty Reduction Strategy		
Approval by Government of a new National Social Protection Framework.	End-March, 2011	In progress. Proposed re-phasing to end-June 2011.
Financial Sector		
Issuance of investment guidelines for pension funds.	End-March, 2011	In progress. Proposed re-phasing to end-September 2011 to allow completion of ongoing actuarial assessment.
Establish framework for emergency liquidity assistance beyond day-to-day liquidity management and tools.	End-March, 2011	Not met. Proposed to be dropped in view of other actions taken to establish a comprehensive crisis management framework.
Fiscal		
Debt management: Prepare a Medium-Term Debt Strategy consistent with resource needs under the new PRS and reflecting contingent liabilities.	End-March, 2011	In progress, expected to be completed by end-June.
Develop an index for monitoring priority social spending.	End-December, 2010	In progress. Proposed re-phasing to end-December 2011 to incorporate requested technical assistance.
Prepare a report on payment claims outstanding over 30, 60, and 90 days in Ministries of Infrastructure, Health, and Home Affairs for end-June, 2010.	End-December, 2010	Met.
Statistics		
Develop core inflation index.	End-March, 2011	Met.

Table 3. Tanzania: Quantitative Assessment Criteria and Indicative Targets Under the Policy Support Instrument, June–December 2011

	June	September	December
	Assessment Criteria	Indicative Targets	Assessment Criteria
	(Billions of Tanzania Shillings; end of period, unless otherwise indicated)		
Net domestic financing of the government of Tanzania (cumulative, ceiling) [1, 2]	347	122	160
Average reserve money (upper bound) [3]	3,804	4,147	4,235
Average reserve money target [3]	3,766	4,106	4,193
Average reserve money (lower bound) [3]	3,729	4,065	4,151
	(Millions of U.S. dollars; end of period)		
Net international reserves of the Bank of Tanzania (floor) [4]	3,477	3,622	3,901
Accumulation of external payment arrears (ceiling)	0	0	0
Contracting or guaranteeing of external debt on nonconcessional terms (continuous ceiling) [5]	525	525	525
Memorandum item:			
Foreign program assistance (cumulative grants and loans) [1]	1,058	299	690

Note: For precise definitions of the aggregates shown and details of the adjustment clauses, see the Technical Memorandum of Understanding (TMU).

[1] Cumulative from the beginning of the fiscal year (July 1).
[2] To be adjusted upward by up to TSh 250 billion for the U.S. dollar equivalent of a shortfall in foreign program assistance from the amounts shown in the memorandum item.
[3] Assessment criteria and benchmarks apply to upper bound only.
[4] Floor will be adjusted downward for any shortfall in foreign program assistance from the amounts shown in the memorandum item up to the equivalent of TSh 250 billion.
[5] To be used exclusively for infrastructure investment projects. Continuous assessment criteria; ceiling applies throughout the fiscal year.

Table 4. Tanzania: Structural Benchmarks for 2011/12

Measure	Target Date	Macro criticality and status
Poverty Reduction Strategy		
Approval by Government of a new National Social Protection Framework.	End-June, 2011	Provides a reliable and comprehensive social safety net targeted to the most vulnerable. In progress. Rephased to end-June 2011.
Financial Sector		
Issuance of investment guidelines for pension funds.	End-September, 2011	Mitigates risk to the financial system and public finances of large, unregulated pension funds. Rephased to end-September 2011 to allow completion of ongoing actuarial assessment of pension funds.
Fiscal		
Debt management: Prepare a Medium-Term Debt Strategy consistent with resource needs under the new PRS and reflecting contingent liabilities.	End-June, 2011	Critical for ensuring sustainability of the government's borrowing strategy and for facilitating broader access to capital markets. In progress. Rephased to end-June 2011.
Establish a unified public debt statistics database under a single monitoring unit.	End-December, 2011	Critical for effective monitoring of debt obligations.
Develop an index for monitoring priority social spending.	End-December, 2011	Facilitates monitoring the implementation of social spending. In progress. Rephased to end-December 2011 to allow time for technical assistance mission.

Attachment II. Technical Memorandum of Understanding on Selected Concepts and Definitions Used in the Monitoring of the PSI-Supported Program

April 15, 2011

I. Introduction

1. The purpose of this Technical Memorandum of Understanding (TMU) is to describe concepts and definitions that are being used in the monitoring of the quantitative PSI assessment criteria and indicative targets under Tanzania's program supported by the PSI arrangement. The principal data sources are the standardized reporting forms, 1SR and 2SR, as provided by the Bank of Tanzania to the IMF, and the government debt tables provided by the Accountant General's office.

II. Definitions

Net international reserves

2. Net international reserves (NIR) of the Bank of Tanzania (BoT) are defined as reserve assets minus reserve liabilities. The BoT's reserve assets, as defined in the IMF BOP manual (5^{th} edition) and elaborated in the reserve template of the IMF's special data dissemination standards (SDDS), include: (i) monetary gold; (ii) holdings of SDRs; (iii) the reserve position at the IMF; (iv) all holdings of foreign exchange; and (v) other liquid and marketable assets readily available to the monetary authorities. Reserve assets exclude assets pledged or otherwise encumbered, including but not limited to assets used as collateral or guaranteed for a third party external liability (assets not readily available). The BoT's reserve liabilities include: (i) all short-term foreign exchange liabilities to nonresidents, of original maturities less than one year; and (ii) outstanding purchases and loans from the IMF.

Reserve money and reserve money band

3. Reserve money is defined as the sum of currency issued by the BoT and the deposits of commercial banks with the BoT. The reserve money targets are the projected daily averages of March, June, September, and December within a symmetrical one percent band. The upper bound of the band serves as the assessment criterion or indicative target.

Net domestic financing of the Government of Tanzania

4. Net domestic financing of the Government of Tanzania (NDF) includes financing of the budget of the central (union) government of Tanzania ("government") by the banking system (BoT and commercial banks) and the nonbank public. NDF is calculated as the cumulative change since the beginning of the fiscal year in the sum of: (i) loans and advances to the government by the BoT and holdings of government securities and promissory notes (including liquidity paper issued by the BoT for monetary policy purposes), minus all government deposits with the BoT; (ii) all BoT accounts receivable due from the Government of Tanzania that are not included under (i) above; (iii) loans and advances to the

government by other depository corporations and holdings of government securities and promissory notes, minus all government deposits held with other depository corporations; and (iv) the outstanding stock of domestic debt held outside depository corporations, excluding: government debt issued for the recapitalization of the NMB and TIB; debt swaps with COBELMO (Russia) and the government of Bulgaria; mortgage on acquired sisal estates; compensation claims; and debt of parastatal companies assumed by the government.

Government deposits at the BoT

5. Government deposits at the BoT include government deposits as reported in the BoT balance sheet, 1SR -including counterpart deposits in the BoT of liquidity paper issued for monetary policy purposes, and foreign currency-denominated government deposits at the BoT, including the PRBS accounts and the foreign currency deposit account.

External payments arrears

6. External payments arrears consist of the total amount of external debt service obligations (interest and principal) of the government and the BoT that have not been paid at the time they are due, excluding arrears on external debt service obligations pending the conclusion of debt-rescheduling arrangements. The ceiling on external payments arrears is continuous and applies throughout the year.

Contracting or guaranteeing of external debt on nonconcessional terms

7. The term "external debt" will have the meaning set forth in Point 9 of the Guidelines on Performance Criteria with Respect to External Debt (Executive Board's Decision No. 6230-(79/140), as amended by Decision No. 14416-(09/91), effective December 1, 2009). External debt will be determined on the basis of currency of denomination of the debt. Government external debt is outstanding debt owed or guaranteed by the Government of Tanzania, the Bank of Tanzania, subnational governments, and companies in which the government has at least 50 percent ownership, unless otherwise stipulated.[1] The ceiling on external debt is continuous and applies throughout the year.

8. Government debt is considered nonconcessional if the grant element is lower than 35 percent, calculated using discount rates based on Organization for Economic Cooperation and Development (OECD) commercial interest reference rates (CIRR), adjusted as appropriate for different maturities. For maturities of less than 15 years, the grant element will be calculated based on 6-month averages of commercial interest rates. For maturities longer than 15 years, the grant element will be calculated based on 10-year averages. This PSI assessment criterion applies not only to debt as defined in Point 9 of the Guidelines

[1] Excluded for these purposes, except if the government offers an explicit guarantee on the debt, are: Tanzania Investment Bank; Tanzania Port Authority; Tanzania Petroleum Development Corporation; Dar es Salaam Rapid Transport Authority; Economic Processing Zones Authority; National Development Corporation; Small Industries Development Organization; National Housing Corporation; National Identity Authority; Dar es Salaam Water and Sewage Authority; and Tanzania Airport Authority.

on Performance Criteria with Respect to External Debt (Executive Board's Decision No. 6230-(79/140), as amended by Decision No. 14416-(09/91), effective December 1, 2009), but also to commitments contracted or guaranteed for which value has not been received.

Foreign program assistance and program exchange rates

9. Foreign program assistance is defined as budget support and basket grants and loans received by the Ministry of Finance (MoF) through BoT accounts and accounts at other depository corporations and is calculated as the cumulative sum, since the beginning of the fiscal year, of the receipts from (i) program loans and (ii) program grants. Program assistance does not include nonconcessional external debt as defined in paragraphs 7 and 8.

10. Foreign program assistance and program exchange rates for the period April 1, 2011 through December 31, 2011 are:

	Q4 End-June	Q1 End-September	Q2 End-December
Cumulative program assistance (US$ millions)	1058	299	690
TSh/US$ average	1517	1527	1540
TSh/US$ end-period	1520	1533	1547

III. Adjusters

Net international reserves

11. The end-June, end-September and end-December 2011 quantitative targets for the BoT's net international reserves will be adjusted downward by the amount in U.S. dollars of any shortfall in foreign program assistance in U.S. dollars (up to a limit of TSh 250 billion), with each quarterly shortfall converted from U.S. dollars to Tanzanian shillings using that quarter's program average exchange rate. The cumulative shortfall will be the sum of all quarterly shortfalls in Tanzanian shillings up to the date of assessment, relative to projections shown in the Quantitative PSI Assessment Criteria and Indicative Targets Table attached to the applicable Letter of Intent and Memorandum of Economic and Financial Polices of the Government of Tanzania.

Net domestic financing

12. The end-June, end-September and end-December 2011 quantitative limits on the net domestic financing of the Government of Tanzania will be adjusted upward for any shortfall in foreign program assistance in U.S. dollars (up to a limit of TSh 250 billion), relative to projections shown in the Quantitative PSI Assessment Criteria and Indicative Targets Table attached to the applicable Letter of Intent and Memorandum of Economic and Financial Polices of the Government of Tanzania. Each quarterly shortfall will be converted from U.S. dollars to Tanzanian shillings using that quarter's program average exchange rate. The cumulative shortfall will be the sum of all quarterly shortfalls in Tanzanian shillings up to the date of assessment.

IV. DATA REPORTING REQUIREMENTS

13. For purposes of monitoring the program, the Government of Tanzania will provide the data listed in Table 1 below.

Table 1. Summary of Reporting Requirements

Information	Reporting Institution	Frequency	Submission Lag
Issuance of government securities.	BoT	Bi-weekly	1 week
Yields on government securities.	BoT	Bi-weekly	1 week
Consumer price index.	NBS	Monthly	2 weeks
The annual national account statistics in current and constant prices.	NBS	Annually	6 months
The quarterly national account statistics in constant prices.	NBS	Quarterly	3 months
Balance sheet of the BoT (1SR).	BoT	Monthly	1 week
Consolidated accounts of other depository corporations and the depository corporations survey (2SR and the DCS).	BoT	Monthly	4 weeks
Summary of stock of external debt, external arrears, and committed undisbursed loan balances by creditor.	BoT	Monthly	2 weeks
External trade developments.	BoT	Monthly	4 weeks
Balance of payments	BoT	Quarterly	4 weeks
Standard off-site bank supervision indicators for other depository corporations.	BoT	Quarterly	6 weeks
Financial Soundness Indicators for other depository corporations.	BoT	Quarterly	6 weeks

Information	Reporting Institution	Frequency	Submission Lag
Other depository corporation lending by activity.	BoT	Monthly	4 weeks
Commercial banks interest rate structure.	BoT	Monthly	4 weeks
Summary table of: (i) average reserve money; (ii) net domestic financing of the government; (iii) stock of external arrears; (iv) new contracting or guaranteeing of external debt on nonconcessional terms; and (v) net international reserves.[1]	BoT and MoF	Quarterly	4 weeks
Amount of payment claims outstanding of more than 30 days, 60 days, and 90 days for all government ministries. For each ministry, total claims outstanding to be divided into: (i) unverified claims; and (ii) claims verified but not yet paid.	MoF	Quarterly	4 weeks
The flash report on revenues and expenditures.	MoF	Monthly	4 weeks
The TRA revenue report	TRA	Monthly	4 weeks
The monthly domestic debt report.[1]	MoF	Monthly	4 weeks
Monthly report on central government operations.	MoF	Monthly	4 weeks
Detailed central government account of disbursed budget support grants and loans, and external debt service due and paid.	MoF	Monthly	4 weeks
Detailed central government account of disbursed donor project support grants and loans.	MoF	Monthly	4 weeks
Statement on new external loans contracted and guarantees provided by the entities listed in paragraph 7 of the TMU during the period including terms and conditions according to loan agreements.	MoF	Quarterly	4 weeks

[1] The MoF and BoT will reconcile data on BoT claims on the government, to ensure that such claims recorded in the BoT balance sheet are the same as those reported by the Accountant General of the MoF.