International Monetary Fund

Tanzania and the IMF

Press Release:
Press Release: IMF Executive Board Completes Third PSI Review for Tanzania
January 22, 2016

Country's Policy Intentions Documents

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

December 24, 2015

Letter of Intent

December 24, 2015

Mrs. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Madam Lagarde:

The attached Memorandum of Economic and Financial Policies (MEFP) updates the ones from June 27, 2014, December 18, 2014, and June 18, 2015 under the Policy Support Instrument (PSI). It reports on recent economic developments and sets out macroeconomic policies and structural reforms that the Government will pursue in the coming years. The Government requests modification of the program conditionality as described in the MEFP and a waiver for non-observance of the Assessment Criterion (AC) on tax revenue.

The Government is confident that the policies and measures set forth in the attached Memorandum will deliver the objectives of its program. We stand ready to take further measures that may become appropriate for this purpose and that are in line with the Government's policy objectives. The Government will consult with the IMF at its own initiative or whenever the Managing Director of the IMF requests such a consultation before the adoption of any such measures or changes to the policies described in the attached Memorandum. The Government will provide the Fund with such information as the Fund may request in connection with the progress made in implementing the economic and financial policies and achieving the objectives of the program.

The Government intends to disseminate this letter, the attached MEFP and the Technical Memorandum of Understanding (TMU), as well as related Fund staff reports, and hereby authorizes the IMF to publish the same after consideration by the Executive Board.

Yours Sincerely,

/s/

Dr. Ashatu K. Kijaji (MP)
DEPUTY MINISTER FOR FINANCE AND PLANNING
UNITED REPUBLIC OF TANZANIA

/s/

Prof. Benno Ndulu
GOVERNOR, BANK OF TANZANIA
UNITED REPUBLIC OF TANZANIA

Attachments
Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding on Selected Concepts and Definitions Used in the Monitoring of the Program Supported by the PSI.

Attachment I. Memorandum of Economic and Financial Policies December 24, 2015

I. RECENT DEVELOPMENTS AND PROGRAM PERFORMANCE

A. Recent Developments

Political developments

1. The new government's priorities are to sustain high growth and further reduce poverty. Sustaining high growth will involve development of railway, port, road and air infrastructure development of natural gas resources; industrialization with emphasis in manufacturing; provision of adequate power; and improved agricultural activities, which will necessitate better access to inputs and finance and resolving land disputes. Reducing poverty will require not only high growth, but also more and better jobs and better education to equip the youth with the right skills. To improve national health, the Government will ensure improved health care delivery with higher availability of clinics and hospitals across the country, better trained medical staff, an increased budget for medicine, and higher participation in the national health insurance scheme. Improving access to, and the quality of, education is equally critical; in this regard basic education will be free from primary to ordinary level secondary schools from January 2016. Increasing access to water for rural and urban population will also be priority. The government remains committed to achieving the main objectives of the PSI-supported programs. On the fiscal front, renewed efforts will be required to combat tax evasion and ensure better tax collection and reduce unnecessary expenditure to make room for social and development priorities.

Output and Inflation

2. Growth. GDP is estimated to have grown by 7.2 percent in the first half of 2015, with strong performance recorded in electricity generation (15.6 percent), information and communication (14.1 percent), transport and storage (11.1 percent), construction (11.1 percent), and financial intermediation services (11.0 percent). Economic growth is expected to remain close to 7 percent in the remainder of 2015 and in 2016, supported by vigorous growth of credit to the private sector, particularly in the services and construction activities, completion of the Kinyerezi 1 plant, which will strengthen the availability and reliability of power supply while reducing reliance on expensive generation using heavy fuel plants, and continued dynamism in financial services, notably mobile ones.

3. Inflation. Inflation, which was on a declining trend since September 2014, started to rise gradually beginning February 2015, increasing from 4.2 percent to 6.3 percent in October 2015. This was largely driven by supply side factors, particularly food prices, and the exchange rate depreciation in the first half of 2015, which raised the domestic cost of imports and partly offset the relief from the fall in global oil prices. Core inflation remained at around 2 percent, signaling limited domestic demand pressures. While inflation could increase somewhat more in the coming months, due to the lagged effects of the recent depreciation, it is expected to continue to remain within single digits, helped by expected stable global oil prices as well as continued tight monetary policy. It would gradually decline in 2016/17 back to our objective of 5 percent.

External Sector Developments

4. Balance of Payments. The current account deficit narrowed to US$4.2 billion (or 8.7 percent of GDP) in 2014/15 compared with a deficit of about US$5 billion in 2013/14. Gold exports continued to decline following a sustained fall in world gold prices, reducing its share in the non-traditional exports to 31 percent from 39 percent a year ago. However, this adverse development was more than offset by declining oil prices and imports and improving exports of manufactured goods, fish and fish products, tourism, and re-exports. Gross official reserves amounted to US$4.3 billion as at end-June 2015, sufficient to cover 4 months of projected imports of goods and services. The current account deficit is projected to improve further in 2015/16, thanks to the full year impact of lower oil prices.

Fiscal Performance and Financing in Fiscal Year 2014/15

5. Execution of the 2014/15 budget. The execution of the budget was lower than programmed resources. Budget revenue was lower than expected by 0.3 percent of GDP, on account of tax revenue, reflecting continued challenges in tax administration affecting income tax withholding on civil servants' salaries and lower corporate income tax revenue due to lower than expected gold prices. On the financing side, donor support fell slightly short of expectations. The main shortfall, however, was incurred on external nonconcessional borrowing (ENCB). Budget support ENCB fell short of target by US$300 million, reflecting unfavorable conditions on international financial markets. Tight financing and the need to execute critical expenditure led to further accumulation of payment arrears in the second half of 2014/15 (with a total of 1.1 percent of GDP for the full year). Including arrears accumulation the overall fiscal deficit is estimated at 4.5 percent of GDP, against a program objective of 3.8 percent of GDP.

Monetary Policy and Exchange Rate Issues

6. Monetary and exchange rate developments. Monetary aggregates remained within the program targets, with M3 growing by 13 percent in the year ending June 2015 and private sector credit by 21 percent. The shilling depreciated rapidly against the U.S. dollar particularly in April–June 2015, as demand for the dollar as a safe haven overlapped with high liquidity in the banking system, seasonally low export earnings and high repatriation of corporate dividends. The situation was further compounded by delays in the mobilization of external program financing, which likely fuelled a foreign exchange shortage psychology. During 2014/15 the shilling depreciated against the dollar by about 25 percent. To rein in inflation expectations, the Bank of Tanzania (BoT) tightened liquidity by increasing the statutory minimum reserve (SMR) ratio by two percentage points effective May 29th 2015, thus freezing about TSh 350 billion. This was complemented by increasing the penalty margin on the Lombard facility by 300 basis points and lowering the ceiling on the foreign exchange net open position (NOP) of commercial banks from 7.5 percent to 5.5 percent of core capital. The resulting liquidity tightness was mirrored in the interbank interest rates, which exceeded 30 percent on several occasions. Currency swaps between banks and the BoT helped improve liquidity conditions, which returned to normal in August 2015. On the foreign exchange market, the monetary policy tightening and seasonally higher export earnings helped to stabilize the shilling and led to the waning of the foreign exchange shortage psychology.

7. Recent measures to improve the functioning of markets. Important steps have been taken to strengthen financial market operations, which is one of the prerequisite for a forward looking monetary policy framework. These include broadening the range of government securities that can be pledged by banks as collateral in accessing standby facilities at the BoT effective June 2015. The framework now includes securities which mature within 91 days to 180 days from the date of acquisition. The IFEM Code of Conduct was also recently revised to clarify a number of issues and expectations. The BoT open market operations with commercial banks are now fully collateralized.

Financial Sector and Capital Account

8. Financial sector stability. The banking sector remains sound, liquid and adequately capitalized. Financial institutions are moving ahead of schedule in increasing capital adequacy levels to 12.5 percent and 14.5 percent for core capital and total capital, from 10 percent and 12percent, respectively. As at the end of June 2015, 34 commercial banks (out of 37) complied with the higher capital adequacy ratios, which are expected to be met by 2017. The BoT is reviewing the Bank of Tanzania Act, Banking and Financial Institutions Act, and Foreign Exchange Act with the view to aligning them with the East African Monetary Union (EAMU) Protocol, new developments in the financial sector and international best standards.

9. FBME Bank. The U.S. Financial Crimes Enforcement Network (FinCEN) finalized its investigation and on 23rd July 2015 issued the Final Rule which effectively prohibits U.S. financial institutions from opening or maintaining correspondent accounts or payable through accounts for or on behalf of FBME. FBME shareholders filed a suit against FinCEN's final rule and on 27th August 2015 the United States District Court for the District of Columbia granted a preliminary injunction and enjoined the rule from taking effect until final judgment is entered. FinCEN went back to the Court and offered to reopen its rulemaking proceedings, giving the shareholders and other interested parties up to January 26, 2016 to respond before a Final Rule is handed down by the end of March 2016. In furtherance of that, the Court directed both parties to submit a joint status report no later than two weeks after FinCEN's decision. FBME continues with normal banking operations under close monitoring while the BoT is reviewing the situation with a view to determining an appropriate course of action for the FBME, including resolution options as governed by law. The BoT will continue to engage with key stakeholders, including the Central Bank of Cyprus, in addressing this situation.

10. Consumer protection. Commercial banks' clients from Dar es Salaam have started utilizing the Complaints Resolution Desk, which became operational in April 2015. To date 34 complaints have been registered, centered mostly on ATM fraud with a few on transaction-related issues. The BoT continues to increase public awareness on the existence of the desk and efforts are under way to extend the service up country and ensure full compliance with the guidelines for establishment of the desk by all commercial banks. The BoT has also started to implement a number of actions in line with the National Financial Inclusion Framework including putting in place a financial education strategy as well as developing the legal, regulatory and supervisory framework to enhance financial consumer protection and drafting of mobile financial services regulations following enactment of the National Payment System Act 2015 in April 2015.

11. Capital account liberalization. Since the further opening of the capital account, the Dar es Salaam Stock Exchange has recorded an increase in equities transactions involving non-residents. However, there have been no transactions with respect to government securities, both on the primary and secondary markets.

Structural issues

12. Natural resources sector. About 55 TCF of natural gas has been discovered in Tanzania in recent years and more is expected as exploration activities continue. In the long term, assuming investments are made to the production phase, this could provide Tanzania with substantial revenue to fast track social and economic development and transform the living standard of Tanzanians. Nevertheless, oil and gas resources are finite and require prudent management to ensure sustainable revenue flow. The Oil and Gas Revenue Management Act of 2015 provides that revenue from oil and gas would continue to support the budget until the time when such revenue is above 3 percent of GDP. Once the revenue is above 3 percent of GDP, the excess would be transferred to the Revenue Saving Account of the Fund. Sixty percent of the designated oil and gas revenue that goes to the budget would finance strategic development expenditure. The Act provides for stabilization of government expenditure in light of inherent volatility; maintenance of orderly and reasonable growth of expenditure to ensure consistency with the absorption capacity of the economy; and avoid borrowing where the government holds financial savings. The Act also provides for monitoring of non-resource fiscal deficit to ensure that revenue efforts from non-oil and gas sources are not neglected. Further, as a way of nurturing the National Oil Company (TPDC), the Government would set aside oil and gas revenue equivalent to 0.1–1.0 percent of GDP to finance strategic investment of TPDC. Funds in the Revenue Saving Account would be used to safeguard the interest of future generation through expenditure in strategic investment including human capital development and financial savings. Lastly, the Act stipulates a comprehensive reporting mechanism to ensure transparency and Accountability of oil and gas revenues.

B. Program Performance

13. Quantitative targets and structural benchmarks. All end-June 2015 quantitative targets were met, except for the assessment criterion on tax revenue and the indicative target on domestic arrears accumulation. In the structural area, the BoT established a Modeling and Forecasting Unit effective 1st September 2015, ahead of schedule. Commitment controls were strengthened with a new circular limiting commitments to cash releases; these changes, however, still need to be reflected in IFMS, which requires reprogramming of the system. Delays were incurred, however, in publishing the fiscal risks statement (done in November 2015), producing a strategy to deal with TANESCO's arrears (a draft was completed in September 2015), and publishing the audited financial statements of public enterprises on the Treasury Registrar's website (the accounts of all 80 enterprises whose audits have been completed were available online in early December 2015, out of a total of 147 public enterprises).

II. THE ECONOMIC PROGRAM FOR 2015/16 AND THE MEDIUM TERM

14. MKUKUTA II. The review of MKUKUTA II implementation shows mixed results. Tanzania has made progress in many fronts including robust economic growth, reduction in child mortality, and access to primary and secondary education. However, reduction in income poverty remains a challenge, particularly in rural areas, and maternal mortality too. While access to education at all levels has improved significantly, quality remains an issue to grapple with. These challenges and others related to social services provision, rural development, governance and social protection are the unfinished agenda that will be addressed in the next Five Years Development Plan 2016/17 - 2020/21, which will be combined with the next MKUKUTA. It will focus on social economic transformation through industrialization.

A. Monetary, Exchange Rate, and Financial Sector Policies

15. Monetary and exchange rate policies. In light of the recent pick-up in inflation and possible further inflationary pressures coming from the recent exchange rate depreciation and food prices, we intend to keep a tight monetary policy stance. The BoT will continue to rely actively on a mixture of instruments for liquidity management operations, while ensuring that the target on international reserves is met and treasury bills yields are reflective of market conditions. The recent depreciation of the shilling has illustrated the BoT's commitment to a flexible exchange rate regime, which is critical to help the economy cope with shocks. It has also led to a depreciation of the real effective exchange rate, which earlier was found to be somewhat overvalued. The BoT's participation in the IFEM will continue to be driven by liquidity management objectives, with only occasional interventions to smooth short-term exchange rate volatility.

16. Modernizing the monetary policy framework. The BoT continues to modernize its monetary policy framework by strengthening its analytical tools, reviewing the functioning of key financial markets, and capacity building on inflation forecasting. A core Forecasting and Policy Analysis System (FPAS) model that reflects the policy regime is being developed in collaboration with the IMF and a dedicated Modeling and Forecasting Unit has been established within the BoT. An important step in the transition towards an interest rate-based framework is to stabilize the interbank interest rates, which have been volatile. This can be achieved within the reserve money targeting framework by stabilizing banks' excess reserves, which are highly correlated with interbank rates. The move to partial reserve averaging, which we intend to implement from end-2015, will also help in this respect.

17. Improving market functioning. The recent turmoil on the interbank and foreign exchange markets has illustrated that these markets remain shallow and can sometimes break down. The turmoil has also shown the importance of close communication between the BoT and market players, which was an important contributor to the normalization of the situation after mid-2015. The BoT therefore intends to further strengthen its communication channels with market participants, with at least monthly meetings at the technical level (in addition to existing meetings at the Governor/CEO level). These meetings will be an opportunity to convey more clearly to the markets the BoT's intentions, and for the BoT to understand better what underpins market developments. A better functioning of these markets also requires more and regular information sharing. For this purpose, by end December 2015 the BoT will share with the banks total clearing balances held at BoT with a lag of one day. This will enable banks to get a sense of liquidity conditions in the banking system. The tightening of the NOP and foreign exchange swaps between commercial banks were exceptional measures implemented at exceptional times. These will be reconsidered by end-June 2016, with a view to improving liquidity in the foreign exchange market (new structural benchmark). Finally, the Bank will continue to enhance transparency in its participation in the IFEM, including continuing to provide clear signals to the foreign exchange market to distinguish between measures aimed at liquidity management from those aimed at exchange rate-volatility smoothing. The BOT will continue to work closely with market players to ensure greater efficiency in the determination of market based interest rates. In this regard the BOT's outliers policy, which aims at ensuring that interest rates are reflective of market conditions, will continue to be communicated to markets players on regular basis.

18. Capital account liberalization. The recent liberalization of capital account transactions to EAC residents will be extended to the rest of the world by end-2015. While we intend to keep prudential rules such as minimum holding periods for debt inflows, we will review them to ensure that they are not overly restrictive and clarify and publish the rules for participation in the government securities market.

19. Banking supervision framework. The BoT has developed onsite examination procedures for consolidated supervision with the assistance of East AFRITAC and a pilot examination, involving bank supervisors and technical assistance experts took place in October 2015. The pilot examination's results will inform the implementation of the regulations going forward. To improve macroprudential surveillance, the BoT is also improving its data collection. While lending for real estate has increased rapidly, stress tests conducted by the BoT suggest that there are no systemic implications from this development owing to the small share of these loans in the overall loan portfolio. However, future developments will need to be monitored carefully, and a pilot project to compile property prices is underway. Initially covering Dar es Salaam in 2015/16, the project will be expanded to cover price developments in other large towns in 2016/17.

B. Fiscal Policies

Budget for 2015/16 and Medium-Term Fiscal Policies

20. Budget for 2015/16. The budget has the following priorities: (i) the financing of the 2015 general elections; (ii) the completion of the ongoing capital projects; and (iii) special emphasis on development projects including rural electrification, water supply, and human capital development. This requires stepping up development expenditures, which will be financed through higher domestic revenue collection. A number of tax policy measures were implemented on July 1 for this purpose, including the railway development levy and petroleum taxes. Together with the expected impact of VAT reform, these measures are expected to lead to an increase in the tax revenue to GDP ratio by about one percentage point. The Tax Administration Act, 2015 intends to create modern, effective, fair and transparent tax administration in Tanzania by simplifying, unifying, and harmonizing tax procedures from various tax laws with a view to promoting voluntary tax compliance, fair tax governance and increasing tax revenue.

21. Budget execution challenges and contingency measures. Tight financing conditions on external and domestic markets have constrained the availability of resources in the first half of the fiscal year. Financing conditions should improve in the second half of the year, with the waning of the uncertainty related to the general elections, and the Government still expects to be able to raise the full programmed amount of ENCB and domestic financing. Additional expenditures have to be budgeted for new measures in favor of education, but also on account of expenditure arrears clearance, partial clearance of government arrears to TANESCO, delayed payments to the PSPF, and delayed statutory contributions (0.7 percent of GDP). Although total domestic revenue collection has not reached 100 percent of target, there has been significant improvement in collection rates and the government believes that by end of the fiscal year the budget projections will be met. At this juncture, the fiscal gap is expected to be between 0.8 and 1.2 percent of GDP. The Government will finalize the estimates by end-December based on the most recent information. Technical work is already well advanced on how the budget will be adjusted, with cuts expected to be in non-priority expenditures and postponing projects not yet started. A government decision on a revised budget along these lines is expected by early January 2016. Expenditure ceilings for MDAs will be revised accordingly in IFMS.

22. Dealing with expenditure arrears. Financing constraints have slowed the settlement of verified expenditure arrears, with only TSh 57 billion paid in 2014/15 (out of a stock of verified arrears as of end-June 2014 of TSh 860 billion). Our intention remains to settle these arrears in 2015/16. Arrears accumulated in 2014/15 will be verified and cleared with the 2016/17 budget. More realistic budgets (both on the revenue and financing side) and the tightening of commitment controls will help reduce the occurrence of arrears in the future. The Government will specify the sanctions provided for in the Budget Act in a circular to be issued shortly and intend to apply them effectively to instill more discipline among accounting officers. A lack of control over multi-annual commitments related to investment projects has been a major source of arrears accumulation, as projects can be contracted which eventually commit the government to payments in excess of available funds. Section 51 of the Budget Act provides control over the multi-annual projects. Also, the Government is developing a centralized database to track projects through their entire life cycle, link them to the medium term expenditure framework and support the monitoring and control of multi-annual commitments. This database will be completed by end-March 2016. Finally, IMF technical assistance has been requested to provide advice on how to address these issues.

23. Medium-term fiscal policy. The recent difficulties faced in raising the requisite financing at a moderate cost to execute budgets and the ensuing accumulation of arrears point to the need to base future budgets on more conservative financing assumptions. Medium-term sustainability considerations and commitments made to the East African Community suggest that a fiscal deficit close to 3 percent of GDP remains a reasonable over the medium term.

24. Tax reforms. Despite recent achievements, tax revenue mobilization in Tanzania remains low by regional and international standards. This is a serious constraint on our capacity to address our development needs. The focus of revenue mobilization efforts in the short-term will be on strengthening tax administration. In line with that, the government has already taken robust action to uncover substantial tax evasion and several measures are being instituted to address administrative challenges to enhance tax revenue collection. A tax administration diagnostic mission from the IMF was requested, which will give a comprehensive picture of achievements so far and challenges ahead. The government remains committed to successful implementation of the recent VAT reform and to minimizing exemptions consistent with the VAT Act. The government is also committed to ensuring timely and full payment of VAT refunds, which are critical for the credibility of the reform. The government also reverted to the practice of withholding centrally taxes and other contributions on civil servant wages. We are working on amendments to the Income Tax Act to provide certainty about the tax rules affecting the mining and petroleum sector. In the medium term, further tax policy reforms will be needed to raise more revenue and we plan to use the coming year to explore a number of options.

Fiscal Aspects of Energy and Pensions

25. Power sector. Over the years, TANESCO has been experiencing operational and financial difficulties due to high production cost compared to its revenue streams. As of June 30, 2015, TANESCO had accumulated arrears to its suppliers amounting to TSh 699 billion, most of which related to energy purchases. A Task Force designed a draft strategy to address these arrears consisting of a combination of measures: (i) the settlement by the government of its arrears to TANESCO amounting to TSh 239.1 billion (TSh 154 billion of which have already been paid in recent months); (ii) the collection by TANESCO of 50 percent of unpaid claims from private customers (about TSh 58 billion); (iii) TANESCO to improve its efficiency in revenue collection from 96 to 99 percent (TSh 65 billion); (iv) diversification of generation sources to reduce costs (TSh 41 billion); (v) a reduction of system losses from 18 to 15 percent (TSh 134 billion); and (vi) the residual (TSh 162 billion) to be addressed either through tariff action or government transfers. All these measures are expected to raise the required amount by 2018. The plan still needs to be refined, including to specify the schedule of settlement, and be approved at the government level.

26. Pensions. Progress has been made in the reconciliation of arrears to pension funds. The arrears to the PSPF on account of the 1999 reform amount to TSh 2.7 trillion. We expect to settle them by end-March 2016 (new structural benchmark), through the issuance of non-cash bonds with maturities ranging from 3 to 20 years. Loans from three pension funds to the government have now been reconciled, while work is progressing on loans from three other pension funds (namely the PSPF, LAPF and NSSF). The Government expects to take over these loans entirely and recognize them as public debt, and will issue non-cash bonds to the pension funds in compensation by end-June 2016 (new structural benchmark). New loans to the government will not be extended until the share of these loans to total pension fund assets falls below the regulatory limit of 10 percent; this limit might be further reduced in the future. Future loans will be recorded explicitly as budget financing, with the corresponding expenditure properly recorded in the budget and fiscal reports.

C. Public Finance and Debt Management

27. Debt management. Our updated debt sustainability analysis suggests that reasonable amounts of ENCB can be contracted while keeping debt vulnerabilities low, provided that fiscal policy remains prudent. The next step will be to update our medium-term debt management strategy (by end-December 2015). Once approved, the debt management division will produce by end-April 2016 a detailed borrowing plan for next fiscal year. A recent corporate malpractice case that arose in the context of a 2013 private placement, in which the government was defrauded by a private bank, illustrates the urgency to strengthen and make more transparent our debt management practices. The government will also approve by end-March 2016 the National Debt Management Policy, which will lay out the overarching principles, policy priorities, debt coverage, and institutional arrangement for effective public debt management, and amendments of the Government Loans, Guarantees and Grants Act strengthening the regulatory and institutional framework for effective debt management (new structural benchmark).

28. Monitoring and management of parastatals. A new information system allows the Treasury Registrar (TR) to receive financial reports from parastatals on a quarterly basis. This will allow closer monitoring of their performance. To ensure better expenditure control, TR has introduced a cap on parastatal spending of 60 percent of their revenue. This cap will be individualized when more analysis has been conducted on each parastatal’s performance, and benchmarks have been developed.

29. **Transparency**. A new consolidated financial statement was published in September 2015 for the first time. It provides detailed financial information on the wider public sector for 2013-14. The Government will continue to develop this consolidated financial statement in consultation with stakeholders, in particular to address missing items and recording issues to provide a fuller picture of the government's financial position.

D. Program Monitoring

30. Consistent with the IMF's new debt limits policy, The Government requests that the program no longer include ceilings on ENCB and NDF. To better monitor fiscal sustainability, we propose to introduce an AC on the overall cash fiscal deficit, measured from the financing side, while the current IT on no expenditure arrears accumulation would become an AC for June 2016. With the external financing shortfall recorded in the first half of the year and higher-than-programmed foreign exchange sales, the NIR AC for end-2015 needs to be amended. The AC for tax revenue for end-December 2015 also needs to be reset, in light of recent revenue shortfalls. The Government also requests a waiver for the missed AC on tax revenue for end-June 2015. Assessment criteria for end-December 2015 and end-June 2016, and indicative targets for end-March 2016 are set as per Table 1. The fourth and fifth reviews under the PSI are expected to take place by June 2016 and December 2016 respectively, on the basis of the assessment criteria and structural benchmarks indicated in Tables 1 and 2, attached.

Table 1. Tanzania: Quantitative Assessment Criteria (AC) and Indicative Targets (IT) Under the Policy Support Instrument, March 2015–June 2016

	March 2015				June 2015				Sept. 2015				Dec. 2015		Mar. 2016		June 2016	
	Indicative Target				Assessment Criteria				Indicative Target				AC		IT		AC	
	Program	Adjusted Criteria	Actual	Met?	Program	Adjusted Criteria	Actual	Met?	Program	Adjusted Criteria	Actual	Met?	Program	Revised	Program	Proposed	Program	Proposed
	(Billions of Tanzania Shillings; end of period, unless otherwise indicated)																	
Net domestic financing of the government of Tanzania (cumulative, ceiling) [1, 2]	446	946	1,310	✗	583	1083	800	✓	358	858	767	✓	…	…	…	…	…	…
Average reserve money (upper bound) [3]	6,219	6,219	5,844	✓	6,473	6,473	6,176	✓	6,494	6,494	6,737	✗	6,913	6,913	6,859	6,912	6,955	7,076
Average reserve money target [3]	6,158	6,158	…		6,409	6,409	…		6,430	6,430	…		6,845	6,845	6,791	6,843	6,887	7,006
Average reserve money (lower bound) [3]	6,096	6,096	…		6,345	6,345	…		6,365	6,365	…		6,776	6,776	6,723	6,775	6,818	6,936
Tax revenues (floor)[1]	7,854	7,854	7,426	✗	10,130	10,130	9,980	✗	2,912	2,912	2,803	✗	6,120	5,923	9,250	8,971	12,408	12,229
Priority social spending (floor; indicative target)[1]	1,800	1,800	2,099	✓	2,400	2,400	2,717	✓	700	700	830	✓	1,400	1,400	2,100	2,100	2,800	2,800
Accumulation of domestic arrears (ceiling; AC for June 2016 only, otherwise IT)[1]					0	0	987	✗	0	0		✍	0	0	0	0	0	0
Fiscal deficit (cumulative, floor) [1,7, 8]	…	…	…		…	…	…		…	…	-876		…	-1,992	…	-2,988	…	-3,984
	(Millions of U.S. dollars; end of period)																	
Change in net international reserves of the Bank of Tanzania (floor) [1, 4, 6]	290	-13	-328	✗	176	-127	-31	✓	137	-166	-357	✗	231	-254	305	-120	438	481
Accumulation of external payment arrears (continuous AC ceiling)[1]	0	0	0	✓	0	0	0	✓	0	0	0	✓	0	0	0	0	0	0
Contracting or guaranteeing of external debt on nonconcessional terms (continuous AC ceiling) [5]	2,420	2,420	934	✓	2,420	2,420	1,147	✓	2,420	2,420	1,147	✓	…	…	…	…	…	…
Memorandum item:																		
Foreign program assistance (cumulative grants and loans) [1]	374	374	306		613	613	571		93	93	5		186	173	278	294	371	339
o.w. Program grants [1]	…	…	…		…	…	…		…	…	…		…	24	…	54	…	79
External nonconcessional borrowing (ENCB) disbursements to the budget [1]	846	846	364		1,010	1,010	579		269	269	22		537	79	806	432	1,074	1,093

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 500 billion for the U.S. dollar equivalent of a shortfall in the combined total of foreign program assistance and ENCB from the amounts shown in the memorandum item. To be adjusted downward by any ENCB disbursed for budget financing above programmed amount for the year as a whole. The 2014/15 ceiling be adjusted upward for any amount of expenditure arrears cleared during the fiscal year in excess of the budgeted amount of TSh 170 billion, and to be adjusted downward for any shortfalls compared to the same amount. The end-of-quarter limits in 2015/16 will be adjusted upward by the amount of arrears to pension funds cleared from the beginning of the fiscal year. This adjustor will be capped by the total amount of arrears identified in the strategy to clear arrears to pension funds.

[3] Assessment criteria and indicative targets apply to upper bound only.

[4] Floor will be adjusted downward by the amount in U.S. dollars of any shortfall in foreign program assistance and ENCB financing of the government up to the equivalent of US$300 million.

[5] The cumulative ENCB ceiling of US$2,420 million applies from January 1, 2014 through September 30, 2015.

[6] Starting end-December 2015 the NIR target excludes short-term (less than 1 year) foreign exchange liabilities to residents.

[7] The fiscal deficit is measured on a cash basis from the financing side at the current exchange rates and is defined as a sum of (i) net domestic financing (NDF) of the Government; (ii) net external financing and (iii) privatization receipts as defined in the TMU.

[8] The deficit in 2015/16 will be adjusted upward by the amount of arrears to PSPF on account of the 1999 reform and the amount of loans in arrears made by pension funds to government entities (recognized by the government) that were cleared during the fiscal year. This adjuster will be capped by the total amount of arrears identified in the strategy to clear arrears to pension funds. The deficit will be increased by any shortfalls in foreign program grants up to a cumulative ceiling of equivalent to US$200 million calculated at the program exchange rate.

Table 2. Structural Benchmarks and Prior Action Under the Policy Support Instrument. December 2014-December 2015			
Measure	***Macroeconomic rationale***	***Target date***	***Notes***
Prior Action			
Government decision by early January 2016 on a revised budget framework along the lines described in MEFP ¶21.			
Public Finance Management/Fiscal Risks			
Prepare and publish a fiscal risk statement or subcomponents of it (e.g., a listing of all PPP projects with their key features and information on government guarantees)	To enhance fiscal risk management	June 30, 2015	Not met. Statement published in November 2015
Reintroduce commitment controls in IFMS, which will prevent commitments to be made in the system that are inconsistent with budget appropriations and cash releases	To reduce the risk of arrears accumulation	September 1, 2015	Not met. A circular limiting commitments to cash releases was issued before the deadline but IFMS still needs to be reprogrammed to reflect these changes.
Prepare a strategy to address TANESCO arrears	To enhance fiscal risk management	End-September 2015	Not met. A first draft strategy was produced in September 2015, but required further work to be completed
Settlement of arrears to PSPF on account of 1999 reform	To address fiscal risks	End-March 2016	New
Settlement of arrears to pension funds on loans made to government	To address fiscal risks	End-June 2016	New

Table 2. Structural Benchmarks and Prior Action Under the Policy Support Instrument. December 2014-December 2015 (concluded)			
Monetary, Financial and Exchange Rate Policies			
Unify the Statutory Minimum Reserve and the clearing accounts that banks maintain at the BoT and implement partial reserve averaging for reserve requirements	To reduce excessive volatilities in short term money market interest rates.	December 31, 2015	Ongoing
Establish a modeling and forecasting unit at BoT	To improve liquidity and inflation forecast and facilitate the shift to a price-based monetary framework	End-September 2015	Met
Produce a study making recommendations on the use of foreign exchange swaps between commercial banks and banks' NOP limit.	To improve liquidity in the foreign exchange market	End-June 2016	New
Public Debt Management			
Update the medium-term debt management strategy, and obtain approval by the Minister for Finance	To enhance public debt management	December 31, 2015	Ongoing
Government to approve the National Debt Management Policy and amendments of the Government Loans, Guarantees and Grants Act	To enhance public debt management	End-March 2016	New
Public Enterprise Management			
Treasury Registrar to publish the audited accounts of public enterprises	To improve transparency and accountability of public enterprises	September 30, 2015	Not met. The accounts of all 80 enterprises whose audits have been completed were available online in early December

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

December 24, 2015

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 Tanzania's program supported by the PSI, comprising the quantitative assessment criteria, the indicative targets and structural benchmarks monitored under the PSI.

2. The principal data sources are the standardized reporting forms, 1SRF and 2SRF, as provided by the Bank of Tanzania (BoT) to the IMF, and the government debt tables provided by the Accountant General's office.

3. The program exchange rate is TSh/USD 2,150.

II. DEFINITIONS

Net international reserves

4. Net international reserves (NIR) of the BoT are defined as reserve assets of the BoT minus reserve liabilities of the BoT. The change in NIR is calculated as the cumulative change since the beginning of the fiscal year. The BoT's reserve assets, as defined in the IMF BOP manual (5th 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 acquired through short-term currency swaps (maturing in less than one year) and other assets used as collateral or as guarantee for a third party external liability (assets not readily available). The BoT's reserve liabilities include: (i) all foreign exchange liabilities except government's foreign currency deposits of residual maturities more than one year; and (ii) outstanding purchases and loans from the IMF.

5. NIR are monitored in U.S. dollars, and for program monitoring purposes assets and liabilities in currencies other than U.S. dollars shall be converted into dollar equivalent values using the exchange rates as of September 30, 2015 (as recorded in the balance sheet of the BoT).

	US$ per currency unit
British pound	1.5587
Euro	1.2147
Japanese yen	0.0097
Australian dollar	0.9236
Canadian dollar	0.9082
Chinese yuan	0.1608
SDR	1.4488

Reserve money and reserve money band

6. Reserve money is defined as the sum of currency issued by the BoT and the deposits of Other Depository Corporations (ODCs) 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 for June and December serves as the assessment criterion and that for March and September, the indicative target.

Fiscal cash deficit of the Government of Tanzania

7. The fiscal cash deficit of the Government (central and local governments only) will be measured on cash basis from the financing side at the current exchange rates. The deficit is defined as the sum of: (i) net domestic financing (NDF) of the Government; (ii) net external financing and (iii) privatization receipts. Any amounts in foreign currency will be converted into Tanzanian shillings at the exchange rates as of the dates of the transactions.

i. NDF is calculated as the cumulative change since the beginning of the fiscal year in the sum of:

   a. loans and advances to the government by the BoT and holdings of government securities and promissory notes (including liquidity paper issued for monetary policy purposes), minus all government deposits with the BoT.

   b. all BoT accounts receivable due from the Government of Tanzania that are not included under (i) above;

   c. loans and advances to the government by other domestic depository corporations and holdings of government securities and promissory notes, minus all government deposits held with other domestic depository corporations;

   d. loans and advances to the government, and holdings of government securities and promissory notes by other public entities (e.g. pension funds) not covered by the central government accounts; and

e. the outstanding stock of domestic debt held outside domestic depository corporations and other public entities, 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.

f. NDF will be measured net of 1) government deposits at the BoT, which comprises 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; 2) any accumulation of central government claims on the Tanzania Petroleum Development Corporation (TPDC) as a result of the on-lending of an external credit to finance a gas pipeline.

ii. Net external financing is measured on a cumulative basis from the beginning of the fiscal year and is defined as the sum of disbursements minus amortization of budget support loans, project loans, external non-concessional borrowing (ENCB) including project ENCB directly disbursed to project implementers; and any other forms of Government external debt. 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). Government external debt is understood to mean a direct, i.e. not contingent, liability to non-residents of the Government of Tanzania.

iii. Privatization receipts consist of net proceeds to the Government of Tanzania in connection with the sale/purchase of financial assets that are not included in NDF and the sale of intangible nonfinancial assets, such as leases and the sale of licenses with duration of 10 years or longer. For the 2015/16 budget, privatization proceeds will exclude TSh 212 billion from the sale of shares in Tanzania Breweries Limited and Tanzania Cigarette Company, which were included in non-tax revenue projections.

Domestic expenditure arrears

8. Domestic expenditure arrears are defined as unpaid claims that are overdue by more than 30 days for goods and services and more than 90 days for contract works as set out in the government's Circular No 9 of 8th December 2014. These will include payments for tax refunds, employee expenses (wages and salaries, staff claims for travel, transfer and other non-salary allowances), utilities, rents, recurrent goods and services, and construction works. Accumulation of domestic expenditure arrears is calculated as a cumulative change in the stock of expenditure arrears at the end of each quarter from the stock at the end of the previous fiscal year (June 30).

External payment arrears

9. External payment 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 and arrears previously accumulated and reported to the Executive Board. The ceiling on external payment arrears is continuous and applies throughout the year.

Priority social spending

10. Priority social spending comprises spending on agricultural inputs, and central government transfers to local governments for health and education.

Tax revenues

11. Tax revenues include import duties, value-added tax, excises, income tax, and other taxes.

Arrears to pension funds

12. Arrears to pension funds include government obligations to the Public Service Pension Fund (PSPF) on pre-1999 reform pension benefits paid on government's behalf and overdue payments on loans made by pension funds to public entities.

Foreign program assistance

13. 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.

III. ADJUSTERS

Net international reserves

14. The end-of-quarter quantitative targets for the change in the BoT's net international reserves will be adjusted downward by the amount in U.S. dollars of any shortfalls in (a) foreign program assistance and (b) external nonconcessional borrowing (ENCB) financing of the government budget in U.S. dollars up to a limit of US$300 million.

15. The shortfalls will be calculated relative to projections for foreign program assistance shown in the table attached to the applicable Letter of Intent and Memorandum of Economic and Financial Polices of the Government of Tanzania titled "Quantitative Assessment Criteria, and Indicative Targets under the Policy Support Instrument". For purposes of the adjuster, ENCB is measured excluding any non-concessional financing contracted for the gas pipeline.

Fiscal cash deficit

16. The end-of-quarter limits in 2015/16 will be adjusted upward by the amount of arrears to PSPF on account of the 1999 reform cleared from the beginning of the fiscal year and the amount of loans in arrears made by pension funds to government entities and recognized by the government from the beginning of the fiscal year. This adjuster will be capped by the total amount of arrears and loans to be taken over identified by the authorities at the end to the reconciliation process.

17. The end-of-quarter limits will be increased by any shortfalls in foreign program grants up to a cumulative ceiling of equivalent to US$200 million calculated at the program exchange rate (para 3).

18. The foreign program grant shortfalls will be calculated relative to projections for foreign grants shown in the table attached to the applicable Letter of Intent and Memorandum of Economic and Financial Polices of the Government of Tanzania titled "Quantitative Assessment Criteria, and Indicative Targets under the Policy Support Instrument".

IV. DATA REPORTING REQUIREMENTS

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
Daily excess reserves of commercial banks	BoT	Weekly	1 week
Daily data on transactions trough IFEM by exchange rate and volume, separating BoT and commercial bank transactions	BoT	Weekly	1 week
Daily data on reserve money and its components	BoT	Daily	1-day
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 (1SRF) and the currency composition of official foreign assets and official foreign liabilities.	BoT	Monthly	1 week
Consolidated accounts of other depository corporations and the depository corporations survey (2SRF and the DCS).	BoT	Monthly	4 weeks
Summary of stock of external debt, external arrears, and committed undisbursed loan balances by creditor.	MoF	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
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	Monthly	4 weeks

Information	Reporting Institution	Frequency	Submission Lag
Amount of arrears outstanding that are overdue by more than 30 days for goods and services and more than 90 days for contract works as set out in the government's Circular No 9 of 8th December 2014 for all government ministries.	MoF/AGD	Quarterly	2 months
The flash report on revenues and expenditures.	MoF/AGD	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	6 weeks
Detailed central government account of disbursed budget support grants and loans, and ENCB, 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 14 of the TMU during the period including terms and conditions according to loan agreements.	MoF	Quarterly	4 weeks
Quarterly report on loans and advances to government by pension funds and other public entities not covered by the central government accounts	MoF	Quarterly	4 weeks
Report on priority social spending	MoF	Quarterly	6 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.