

AFRICAN DEVELOPMENT FUND



COMPLETION REPORT
STRUCTURAL ADJUSTMENT LOAN II (SAL II)
REPUBLIC OF TANZANIA

**GOVERNANCE, ECONOMIC AND
FINANCIAL REFORMS DEPARTMENT**

**OSGE
MARCH 2007**

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CURRENCY EQUIVALENTS

(End October, 2006)

Currency Unit = Tanzania Shilling

UA1 = 1.48US\$

UA1 = 1 SDR

UA1 = 1701.95 Tanzanian Shillings

FISCAL YEAR

1 July to 30 June

WEIGHT AND MEASURES

Metric System

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ACRONYMS AND ABBREVIATIONS

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

TANZANIA: SAL II PROGRAMME MATRIX: EVALUATION WITH COMMENTS ON ISSUES & CURRENT STATUS

REFORM OBJECTIVES	VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS	RESULTS AS MAPPED IN THIS PCR (DOCUMENT SECTIONS IN BRACKETS)	CURRENT STATUS AND ISSUES
GOAL 1. To reduce poverty	Progress towards reduction in incidence of poverty in line with PRSP targets.	Household budget surveys by NBS; PRSP Annual progress reports by GOT; Participatory Poverty Assessment Reports;	Sustained commitment to implementation of PRSP	Progress in the main goals of the PRSP (higher growth and further reduction of poverty, guided by MKUKUTA) was broadly on track. All end-September 2005 Program quantitative performance criteria were met, although the net domestic assets (NDA) indicative target was missed. All quantitative indicative targets for end- December were met, except the reserve money and net domestic assets ceilings which were exceeded by small margins. The structural reform agenda is broadly on track. During 2000-05 that encapsulates SAL II, Tanzania's per capita GDP growth rate averaged nearly 2¾ percent. This is an improvement over the 2 percent average during 1996-2006. However, GDP per capita in 2005 was well below GDP growth performance. In addition, at about US\$337, Tanzania's GDP per capita was still well below sub-Saharan Africa's average of US\$568. (<i>Section 4.1, 4.2, Section 5</i>)	A number of structural bottlenecks diminish impact on poverty: Agriculture is the dominant contributor to GDP growth but is running a full 1 percent below overall real GDP growth, while carrying the livelihoods of 80 percent of the population. Food crops, and not more growth oriented cash crops predominate in the rural sector; Infrastructure and skills are poor.
Project Objective: Create an enabling policy environment for growth acceleration and improvement in the delivery of basic social services.	Real annual GDP growth rate of 6 percent by 2002/03 Decline in the rate of inflation from 6.55 in 1999/2000 to 4% in 2002/03 Rise in the level of investment from 15 to 19 percent in 2002/03 Increase in budgetary allocation to pro-poor sectors and activities.	National Accounts and BOT annual economic reports MTEF and PRSP annual progress report. Expenditure Tracking Studies.	Economic Reform remains on track. Strong Donor Support for reform continue	During the implementation of SAL II, the rate of real GDP growth increased from 5.7% in 2001 to 6.2% in 2002 and, and after a dip to 5.6 in 2003 due to drought, it had reached 6.7% by 2004. Inflation figures show 5.5, 4.9, 4.4, 3.5, and 4.1 over 2000-2004; Investment (government and private sector-including stocks- as ratios of GDP) actually fell from 17.6 -16.7 percent over 2000-2002 before recovering to about 18.6 percent in 2003 with shares of 7.4 and 11.2 percent respectively. Social and Development expenditures rose from about 7 percent to 11 percent over the period 2001/02 -2003/04 encapsulating the implementation of SAL II. In addition, the percent of the population living below basic needs has fallen continuously over 1996-2002 (<i>Section 5.1</i>)	Real GDP, Investment and allocation targets are broadly achieved. The underbelly of these achievements is the set of economy-wide structural impediments that diminish growth and poverty reduction momentum: <ul style="list-style-type: none"> • A poor private sector environment that maintains high start-up costs and costs of doing business; • A low level of financial deepening that weakens the uptake of loanable funds in the system; • Weal multiplier and productivity impact of otherwise healthy FDI inflows into the mining sector;

<p>Outputs: Constraints on private investment removed.</p>	<p>Expansion and upgrading of Commercial court to speed up the settlement of commercial disputes and enforcement of contracts.</p> <p>Rationalization of tax regime through elimination of nuisance taxes and clearer demarcation of powers of taxation at the central and local government level.</p> <p>Removal of restrictions on internal and cross-border trade in agricultural products.</p> <p>Enactment of new company law and issuance of regulations for implementing the new land law.</p>	<p>Legal Sector Reform Programme reports. SAL ILPSAC supervision mission reports</p> <p>SAL II/PSAC progress reports and Tanzania Investment Centre reports</p> <p>SAL II/PSAC progress reports</p>	<p>Strong investor response to reform</p>	<p>Some 20 new judges have been appointed and sworn in. This was part of an exercise to de-congest the courts;</p> <p>The GOT continues with medium-term revenue targets, taking a range of measures to bolster tax administration substantially, including adoption of a new medium-term corporate plan for the Tanzania Revenue Authority, refocusing of management and administrative resources that will broaden coverage of large taxpayers; strengthening of the administration of VAT and presumptive taxation, and actions to broaden the tax base through curtailing exemptions. Exemptions have been increasingly limited to charitable organizations and donor funded projects.</p> <p>Removal of restrictions on border trade is making progress under GOT notice to local authorities to stop restrictions of cross-border trade; domestic trade is improving with access to credit.</p> <p>The Companies Act was passed by Parliament in April 2002. However, there was a delay in establishing the necessary regulations. The GOT requested and obtained ADB's 'no objection' (on 23 July 2003) to move to the second tranche conditions since the funds were factored into fiscal year 2002/03, which had <i>already</i> ended in June 2003.</p> <p>GOT is making progress in the land registration system for enabling land to be used as collateral against credit or mortgages; (Section 4.1, 4.2, Section 5)</p>	<p>The PCR preparatory mission was briefed and given documentary evidence by the leadership of the Legal Sector Reform Program on the vast benefits of the investments in the legal initiative of SAL II, including many positive externalities.</p> <p>A hidden factor in this restriction is local taxes on commodities which can amount to as much as 20 percent.</p> <p>The case of the Company Act demonstrates the quandaries caused by three frequent problems with the Bank's conditions: 1) numerical overload unrelated to efficacy; 2) 'cascading' where failure of one condition <i>outside</i> the competence of the Borrower (GOT in this case, while Parliament was the competent authority for passing the Act) knocks on other conditions that the Borrower is competent to fulfill; and 3) poor targeting. In the latter, the Bank pitted a tri-directional set of triggers that could not work: Condition (v) could not be cleared without establishment of the Company Act & Regulations; Disburse't could thus not take place; and Condition (iii) on adopting cash flow planning & manage't of budget for FY2002/03 could not be implemented without First tranche disbursement because the first tranche of SAL II was programmed to support that condition in the budget of FY 2002/03 which ended June 2003. Failure of the conditions on the Companies Act and the Regulations undermined that objective and caused a search for alternatives through the Bank of Tanzania.</p>
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Key public enterprises in utilities and transport divested and divestiture strategies for others adopted. Regulatory frame-works in infrastructure and public utilities developed.	Award of lease for DAWASA Concessioning of TRC. Adoption of strategy for unbundling TANESCO and of privatisation of corporatized businesses. Divestiture strategy for THA businesses adopted Multi-sectoral and cross sectoral regulatory and legal frameworks developed covering utilities and transport.	PSRC progress reports PSRC progress reports PSRC & Planning Commission reports Progress Reports from the Corruption Prevention Bureau. PSAC/SAL II supervision mission reports	Buyers of the enterprise found.	The tender process was completed and DAWASA was awarded to City Water Company (Letters to the ADB from PPSRC, 11 Dec., 2002. However, during the time of lease, City Water failed to abide with some of the conditions of the service contract, even after several reminders and follow-ups. The Government, after consultations with all the stakeholders including ADB, terminated the services of City Water Company in 2005 and in the transition period, leased the services to a local company, Dar es salaam Water Supply and Sanitation Company. The government is still committed to lease the services to a private company through international open bidding. Divestiture was being guided via a study on options; In progress The Government has made adequate allocations in the Budget to fund the implementation of the Anti-corruption action plans for the Ministries of Works, Health, Education, the Attorney-Generals' Chambers, Home Affairs and the Tanzania Revenue Authority, and has commenced implementation of the plans.	The DAWASA saga proves the unusual case of reverse-privatization as the outcome failed to yield the expected outcome. The process indicated has placed Tanzania in an alarming stranglehold vis avis divestiture. The country was suffering a crisis in the energy sector during the past 2 years.
Good Governance policies and practices adopted in the areas of budget management and public financial management and the public sector.	Anti-corruption action plans prepared in the ministries of health, education, home affairs, works and in the attorney-general chambers, TRA. Coverage of the IFMS extended to all ministries, sub-treasuries and the phase local government reform districts. Public finance and procurement legislation enacted by Parliament and regulations issued.	PSAC/SAL EI mission reports. Public Financial Management Reform progress reports. PSAC/SAL mission reports. Public Financial Management Reform progress reports.		IFMIS has been extended to all 19(now 20) sub-treasuries. This has been done.	The GOT has shown strong commitment in pursuing its anti-corruption agenda articulated from the Office of the President. The PCR mission was briefed by the leaders of the Unit in the Office of the President and there was a useful exchange of ideas on the future. A leading outcome of SAL II in this segment is the twin National Anti-Corruption Strategy and Sector Specific Action Plans for all government Ministries and Agencies and for all Local Government Authorities. The Action Plans are budgeted and are based on the National Anti-Corruption Strategy and Action Plan for Tanzania (NACSAP) launched in 1999. The GOT has launched Phase two of the same that will run from 2006-2010. IFMIS has been extended to 20 sub-treasuries and 85 districts. Its coverage has widened to the security forces and mainly needs to be sustained.

<p>The Judiciary strengthened</p> <p>Implement policies in the rural sector strengthened.</p>	<p>Budgetary allocation to priority sectors increased in line with the MTEF and PRSP.</p> <p>The ratio of actual court sessions to planned sessions increases</p> <p>Agriculture and rural development strategies are adopted by Cabinet.</p>	<p>MTEF document and PRSP annual progress reports</p> <p>Legal Sector Reform Programme Progress Reports. SAL II supervision mission reports. PRSP progress reports</p> <p>PRSP progress reports</p> <p>Ministry of Agriculture and Food reports. PRSP progress reports</p>		<p>This stipulation was implemented within PRSP priorities.</p> <p>Similarly, this is ameliorated with gradual increase of capacity, e.g., appointment of new judges.</p> <p>Government finalized the Agriculture Sector Development Strategy (ASDS) in November 2002. Implementation is ongoing and seeks to promote higher agricultural growth and improve rural incomes as well as food security by raising productivity and improving the profitability of agriculture. The ASDS has 3 Components: Agriculture Sector Support and Implementation at District and Field Level; Agriculture Sector Support at National Level and; Cross-Cutting Issues with other Sectors at the National Level.</p>	<p>The supply response will take some time in agriculture due to structural factors in the sector as well as in the agricultural sector. These are addressed in Lessons Learned and should be addressed in future budget support.</p>
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BASIC PROGRAMME DATA

1.	Country:	The United Republic of Tanzania	
2.	Name of Programme:	Structural Adjustment Loan II (SAL II)	
3.	Loan Number:	P-TZ-K00-004	
4.	Borrower:	The United Republic of Tanzania	
5.	Beneficiary:	The United Republic of Tanzania	
6.	Executing Agency:	Ministry of Finance	
A.	Loan (Agreement No: 2100150006656)		
		Appraisal Estimate	Actual
1.	Amount (UA Mil)	40.0	40.0
2.	Service Charge	0.75%	same
3.	Commitment Charge	0.50%	same
4.	Repayment Period (Years)	50	same
5.	Grace Period (Years)	10	same
6.	Repayment (Years 11 - 20):	1%	same
	(Years 21 - 50)	3%	same
7.	Loan Negotiation Date	August 2001	August 2001
8.	Loan Approval Date	September 2001	September 2001
9.	Loan Signature Date	November 2001	December 2001
10.	Date of Entry into Force	November 2001	December 2001
B.	Project Data		
1.	Total Cost (US Mil)	882.3	882.3
2.	Financing Plan (US Mil)		
	ADF	51.0	51.0
	MDF/PRBS	446.7	446.7
	World Bank PSAC	190.0	190.0
	IMF	168.0	168.0
	Others	26.6	26.6
3.	Date of 1st Disbursement	November 2001	October 2003
4.	Date Last Disbursement	July 2002	February 2004
5.	Preparation of PCR/Audit	December 2002	April 2007
C.	Performance Indicators		
1.	Cost Over/Under-run	NIL	NIL
2.	Time Overrun (Months)	NIL	23
	Slippage - Effectiveness	NIL	NIL
	- Completion Date (Months)	NIL	23
	- Last Disbursement (Months)	NIL	23
	- No. of Extensions	NIL	1
3.	Project Implementation Status		Completed
4.	Institutional Performance		
5.	Contractor Performance	N/A	N/A
6.	Consultant Performance	N/A	N/A

D.	Missions		No. of Persons	Man-days
1.	Preparation			
2.	Appraisal			
3.	1 st Supervision		2	15
4.	Mid- Review	-	-	
5.		-	-	
6.	PCR		1	12

E.	Disbursement (UA Mil.)	Appraisal	Actual	% Disbursed
1.	Total Disbursed	40.0	40.0	100
2.	Amount Cancelled	0	0	0
3.	Unused Balance	0	0	0
F.	Contractors	No Contractors		
G.	Consultants	No Consultants		

EXECUTIVE SUMMARY

1. Programme Setting, Goal and Objectives

During the late 1990s, the Government of Tanzania (GOT) deepened the transition from the socialist framework of the 1970s and 1980s. It ingrained liberal macro-economic policies as a foundation for growth and poverty reduction. After slippages in macro-management between 1993 and 1995, the GOT focused on the HIPC Initiative. It qualified for HIPC relief during 2001. Its first Poverty Reduction Strategy Paper (PRSP) was approved in late 2000. The Bank's Structural Adjustment Loan II (SAL II) supported financing of the PRSP for the fiscal years 2001/02 - 2003/04. The objective was to promote growth and poverty reduction through a comprehensive package of structural reforms spanning three areas. The Components taken from the GOT strategy were: Private Sector Reforms; Economic Governance, and; Agriculture and Rural Development.

2. Analysis of Start-up and Main Implementation Activities

2.1 SAL II became effective on September 2003. A special account named Structural Adjustment Loan II (SAL II) A/C No. 9931202961 was opened with the Bank of Tanzania to which all SAL II resources were disbursed. The first tranche carried seven conditions (Annex II) as contained in section 5.01 of the Loan Agreement. All conditions were satisfied except for Conditions (iii) and (v) of the Conditions Precedent to disbursement of the First Tranche. The latter condition required Government to enact a new Companies Act and prepare draft regulations to govern its implementation. This illustrates how targeting in SAL II was problematic. The Bank pitted a tri-directional set of triggers that caused critical delays. Condition (iii) on adopting cash flow planning and management of the budget for FY2002/03 could not be implemented without First Tranche disbursement, since these proceeds of SAL II were programmed to support that condition in the budget of FY 2002/03, ending June 2003. The disbursement failed because GOT could not fulfill Condition (v) of the First Tranche. This directly undercut Condition (iii). The GOT was forced to unhinge the impasse in three actions. It drew down the equivalent of the SAL II First Tranche in its deposits the Bank of Tanzania and met Condition (iii) to make progress on its PRSP. It then applied for an exemption and transfer of Condition (v) to Second Tranche conditions. With approval accorded by the ADB Board, it secured the First Tranche disbursement from the Bank Group, and used it to replenish the draw-down at the BOT. This 'accounting' solution and ensuing delay would have been unnecessary if First Tranche draw-down had been made easier by making Conditions (iii) and (v) monitorable requirements of Second Tranche disbursement, subject to verification during the supervision missions that followed SAL II effectiveness.

2.2 Cascading of conditions (in which the failure of a poorly-aimed condition holds up fulfilment of other conditions or causes them to fail, thus leading to implementation and disbursement delays) also became evident. The Executing agencies or even the GOT were not the competent actors to fulfil some of the conditions. Calendar dates for Parliamentary or legislative actions for example are not in the competence of the Ministry of Finance, the executing agency. Parliament set its own calendar, actions, and standards independently of the executing agency, the Bank Group, or even Cabinet and GOT. In this case, Parliament passed the Companies Act engaged by the Bank in Condition (v) of First Tranche release in April 2002. But competencies for drafting of the regulations were pitched high, causing procurement delays. Implementation of SAL II was trapped, causing an application for exemption and transfer to Second Tranche conditions. Conditions thus need to be calibrated to the appropriate competences.

3. Assessment of Performance and Results

SAL II was embedded in the GOT reform programme to support Tanzania PRSP. The targets of ADB's SAL II and their stipulations performed satisfactorily.

3.1 The Private Sector component

3.1.1 As stipulated, the operations of the Commercial Court have been devolved and expanded notably to Mwanza and Arusha in late 2002. In 2003 the services were extended to Mbeya and Moshi and are being implemented in phases. The computerization of the case filing and Registry System has been accomplished at the High Court Headquarters and at three centers (Mwanza, Mbeya and Arusha).

3.1.2 Reform of the land registration system for enabling use of land as collateral against credit or mortgages is ongoing. The Land Regulations were gazetted through Government Notice (GN) No. 71-85 published on 4th May 2001, thus making the Land Act No. 4 of 1999 effective.

3.1.3 Measures to harmonize and rationalize central and local government's taxes, aimed at reducing and eventually eliminating the tax burden and multiplicity of taxes on investors have been implemented. The GOT established the Tanzania National Business Council (TNBC) chaired by the President of the United Republic of Tanzania and the Investor's Roundtable (IRT). These are dialogue mechanisms with the business community for improving the business environment. A Private Sector Development Strategy (PSDS) is in place, incorporating a focus on SMEs and drawing from several sectoral policy documents. Implementation on a pilot basis of selected activities under the PSDS commenced in November 2004.

3.2 Economic Governance Component

3.2.1 The Government budget for FY 2001/02 adopted PRSP priorities focusing on water, basic education, health, agriculture (research and extension), rural roads, the legal and judicial system and HIV/AIDS, in line with the 3-year cycle of MTEF 2001/02 – 2003/04. Allocation to priority sectors increased to 40.1% of total recurrent budget in 2001/02, well above the SAL II target of 33.2 percent. The share of 'Other Charges' for priority sectors in total recurrent budget, stipulated to rise from 11.3 percent to 13.4 percent over FY 2000/01 to FY 2001/02, increased from 16% in FY 2000/01 to 23% in FY 2001/02, again well above SAL II targets. Similarly, the budget guidelines for FY 2002/03 adopted the PRSP expenditure priorities in accordance with the MTEF 2001/02 – 2003/04. The Bank Mission of May 2002 was able to verify satisfactory progress in its BTOR.

3.2.2 Public Expenditure Management has been strengthened with cash flow planning in preparation and management of the budget. This limits expenditures to resources availability through the implementation of a centralized payment system which is facilitated by the IFMIS. In the Guidelines for the preparation of the Medium-Term Plan and the Budget Framework (2002/03 – 2004/05) issued in December 2001, all MDAs, Regions and Councils were instructed to provide cash-flow plans which would form basis on which funds will be released. In response, all MDAs, Regions and Councils prepared cash-flow plans using formats provided in the Budget Guidelines.

3.3 Rural Sector Development

The Government commenced implementation of the Agriculture Sector Development Strategy (ASDS), focusing promotion of higher agricultural growth and improved rural incomes as well as food security by raising productivity and improving the profitability of agriculture. The

strategy continued to be implemented in five strategic areas of intervention: (i) strengthening the institutional framework; (ii) creating a favourable environment for commercial activities; (iii) identifying public and private sector roles in improving support services; (iv) strengthening the marketing efficiency for inputs and outputs and; (v) mainstreaming planning for agricultural development in other sectors.

3.4 The Results in Retrospect and Medium term Policy Options

A number of structural impediments appear frequently in the review and policy discussion of Tanzania. One is the size and quality of gross private capital formation as a share of GDP. This needs to be strengthened to maintain and propel the pace of GDP growth. Foreign Direct Investment in natural resource extraction seems not to yield proportionate impacts on poverty reduction or revenues. Value-addition domestically could improve gains. The quality of private sector development needs to be improved. Weaknesses include a poor business climate. The World Bank's 2006 *Doing Business* report ranks Tanzania 140th in the overall ease of doing business out of 155 countries surveyed. Tanzania is ranked 101st out of 117 countries in the Global Competitiveness Report relating to production of electricity, and energy production bottlenecks add to costs that reduce competitiveness. In the financial sector as well, there emerges a weak response to available bank credit, raising the question of financial deepening and poor access to credit for the rural sector and informal sector that host the majority of Tanzanians. Finally an emerging issue is that of the Bank's role on growing donor coordination and efficiencies of aid harmonization. The Poverty Reduction Budget Support Facility (PRBS) is a vehicle made up of nine donors. It seeks to support the implementation of the Government's poverty reduction strategy by ensuring adequacy and predictability of resources provided to priority sectors in the budget. The PRBS uses the Performance Assessment Framework (PAF) matrix and Public Expenditure Management and Financial Accountability (PEFMA) as tools to benchmark progress. This has widened the voice of policy players from multilateral donors. It has proved effective in reducing the transactions costs of policy dialogue. The Bank should develop a strategy for engaging in this process.

4. Socio-economic Impact

Real GDP growth over 2004/05 and 2005/06 was running at about 7 percent in line with projections. The leading sectors in 2005 were trade and tourism, manufacturing, mining and construction, whose combined contribution to GDP was about 40 percent. In line with PRSP-linked expenditures and increases in priority areas, the data shows that expenditures have tracked the conditions of the GOT Programme and the SAL II support. Priority social and development expenditures rose from about 7 percent to 11 percent of GDP over the period 2001/02 -2003/04 encapsulating the implementation of SAL II. The percent of the population living below basic needs was falling continuously over 1996-2002. Institutional capacity has also improved, including stronger structures for domestic revenue mobilization, public expenditure management, and the financial sector.

5. Conclusions

The main conclusion of this PCR is that SAL II was successfully implemented, but with very substantial delays, despite the multiple conditions that had already been fulfilled (substantially in some cases) before the program commenced. The analyses of the PCR bring out some lessons some of which are highlighted below.

6. Lessons Learned

6.1 Building on the lessons of SAL II, the implementation shows how policy-based support may succeed, yet leave marginal effects in terms of targeted outcomes, e.g. private sector development, agriculture and rural development and overall poverty reduction in this case. Structural conditionalities in key sectors do not necessarily lead to outcomes in specific sectors. Supply responses take time, but a prolonged series of macro-stabilising interventions without comparable results on the real sectors pose the risk of eventually derailing macro-stability itself. The principal lesson learned is that macro-stability and GOT commitment must be maintained but, in addition, attention must in future focus the *quality and progress on the program outcomes*. This suggests a shift in future budget support towards assisting Tanzania to remove the structural factors that hamper the achievement of more robust results. This PCR indicates some key structural factors that could be addressed:

6.2 Private Sector Development

- Address investment climate issues such as financial deepening and widening the currently narrow base of private sector players that have access to credit;
- Remove burdensome licensing procedures that lead to high start-up costs in Tanzania;
- Ease restrictive labor regulations, obstacles in registering property, poor property rights; ameliorate poor infrastructure, exemplified in recent years by the crisis in the energy sector;

6.3 Economic Governance

- Upgrade the fight against corruption and poor governance that undermine private investment. In the latter context, corruption is induced by government regulations susceptible to rent seekers; complex business licensing systems; overlapping regulatory mandates; ad hoc provision of tax exemptions; and loopholes in dispute resolution.

6.4 Agriculture and Rural Development

- Deepen agriculture sector growth to match or exceed real GDP growth. Currently it is the predominant contributor to GDP growth and livelihoods for 80 percent of the population, yet its growth is running a full 1 percent in real terms below GDP growth rate;
- Diversify agricultural production, especially towards cash crops;
- Address supply-side constraints, e.g. multiple local commodity taxes; weak rural infrastructure; inadequate skills;

7. Recommendations

The overall summary recommendations are as follows:

- In future budget support, the Bank should address structural impediments in the economy that hinder macro-stability, investment, growth and poverty reduction.
- The Bank should adopt a sector or issues-based strategy for engagement in ongoing donor/GOT policy dialogue (PRBS). Using the Country Office as the main foothold, sector studies should guide participation and intervention. This PCR suggests issues of investment climate and credit to rural and informal sectors would have been beneficial.
- To minimize the risks of delayed disbursement and implementation, multi-tranche Bank loans should be assigned flexible triggers or the Bank Should move to multi-year single tranche operations. This avoids the cascading of conditionalities shown in this PCR.

1 INTRODUCTION

1.1 BACKGROUND TO POLICY REFORMS IN TANZANIA

1.1.1 Poverty reduction has been a major preoccupation of policy in Tanzania for decades. Agriculture heavily influences economic activity accounting for about half of GDP. It provides 85% of exports and employs 80% of the work force. Topography and climatic conditions, however, limit cultivated crops to about 4% of the land area. Industry mainly features the processing of agricultural products and light consumer goods.

1.1.2 Multilateral and bilateral donors have in recent decades provided funds to rehabilitate Tanzania's economy from a highly state-controlled economy, characterized by a rigid economic system that operated under monopolistic and heavily regulated structures of production. The transition continues to score substantial success in helping revitalize economic growth. Key planks of the assistance have focused on down-sizing government economic activity, economic infrastructure and poverty alleviation. The post-socialist economy has scored substantial industrial production and an increase in output of minerals. Banking reforms have propelled private-sector growth and investment. In 2005, real GDP growth reached more than 6%.

1.1.3 The Structural Adjustment Loan II (SAL II) of UA 40 million was approved on September 3, 2001. It was the ADB Group's fifth policy-based loan to Tanzania. It succeeded SAL I, while the first three PBLs were sector adjustment loans to support policy reforms in the agricultural and transport sectors (Sector Rehabilitation Loan - Agriculture and Transport), the industrial sector (the Industrial Rehabilitation and Trade Adjustment Loan) and the financial sector (Financial Sector Adjustment Loan). The previous four PBL operations were funded from ADF resources and involved a total commitment of UA 128.81 million.

1.1.4 Recent PBLs (notably SAL I and SAL II) have focused fiscal performance as a central plank of macroeconomic stabilization. Within fiscal policy, the support has targeted two main actions: reallocation of budgetary support to the social sector, poverty reduction and development expenditure; and limiting the recourse to domestic financing as a tool to moderate the inflation.

1.1.5 During the implementation of SAL II, a key concern of macroeconomic policies in Tanzania was the country's position in the list of possible HIPC beneficiaries, with four main qualification criteria: (a) remain IDA-only and PRGF-eligible; (b) having an unsustainable debt burden, beyond traditionally available debt-relief mechanisms; (c) establish a track record of reform and sound policies through IMF and IDA-supported programs, and; (d) develop a Poverty Reduction Strategy Paper (PRSP).

1.1.6 In line with the enhanced HIPC framework, arrangements at decision point, the Government of Tanzania had to fulfil the following five main conditions to reach the completion point:

1. Adoption of a full PRSP and its satisfactory implementation for at least one year;
2. Maintenance of macroeconomic stability through satisfactory implementation of the IMF-supported PRGF programme;
3. Progress in meeting specific social sector targets (two objectives in HIV/AIDS, three criteria in education and four targets in health);
4. Satisfactory implementation of key structural reforms, one in the electricity sector, and one in the financial sector;
5. Satisfactory implementation of two public expenditure management processes.

1.1.7 The GOT addressed existing policy gaps within the above framework to stay on course for HIPC. Measures undertaken under SAL II have helped Tanzania obtain debt relief under the enhanced HIPC Initiative thus allowing the country to reach debt sustainability and support higher social sector spending. Additional debt relief from the International Development Association (IDA) and the African Development Fund (ADF) through enhanced HIPC and MDRI was granted 2006.

1.2 OVERALL PROGRAMME

1.2.1 The GOT's medium term reform agenda, 2000/01-2002/03 (at the onset of SAL II) was an integral part of the country's PRSP. The overarching goal was poverty reduction through accelerated and equitable growth and the improvement of human capabilities, survival and social well being. The GOT Programme focused on two broad areas of the economy. First, it aimed to strengthen growth through consolidating macroeconomic stability. To achieve this component, it would improve rural infrastructure, create an enabling business environment, promote and diversify exports, and improve agricultural productivity. Second, the programme would improve human capabilities, survival, and well being. To achieve this, it would increase budgetary support for key poverty reduction programs, improve governance, reduce the vulnerability of the poor, protect the environment and strengthen the poverty monitoring and evaluation process. Presented briefly, the PRSP had targets in two main areas of the economy.

1.2.2 **Macroeconomic targets:** to increase the growth rate to 6% by 2003/2004, increase agricultural value-added growth by 5 % annually; to reduce inflation to approximately 4% per annum and maintain gross official reserves at about 4 months of imports; to keep the overall deficit at a modest level; and to raise the investment ratio to GDP from 15 % to 17% with private investment contributing a major share of the increase.

1.2.3 **Poverty Reduction Targets:** The targets were to reduce the incidence of poverty from 48 percent in 2000 to 42 percent in 2003 and to 24 percent in 2010. The proportion of rural population below the poverty line was targeted to decline from 57 percent to 49.5 percent and that of the proportion of the food poor from 27 percent to 23.5 percent. Human development targets focused on: 1) increases in gross primary school enrolment ratios from 78 to 85 percent and achievement of universal primary education by 2010; an increase in transition rate from primary to secondary education from 15 to 21 percent; lowering of the infant mortality rate from 99 per 1000 to 85 per thousand; increasing the coverage of the supply of clean water and sanitation from 42 to 56 percent. In addressing governance, the reforms targeted the speed up of settlement of cases in primary courts by reducing the shortage of magistrates; speeding up court decisions and increasing the ratio of decided to filed cases from 63 to 80 percent by end-2003; and increasing the ratio of actual court of appeal sessions to planned sessions from 50 to 100 percent.

2 PROGRAMME GOALS, OBJECTIVES AND FORMULATION

2.1 PROGRAMME OBJECTIVES

2.1.1 The specific objectives of SAL II were to support the GOT's implementation of the reform program which formed an integral part of the PRSP. The loan was to be disbursed as a budget support action but with the Bank's specific areas of focus and conditions culled from the more comprehensive PRSP.

2.1.2 As described in Section 1.2, the GOT reform Program focused two broad components: strengthening growth through consolidating macroeconomic stability and improving human capabilities. At the onset of SAL II, a wide array of measures was already in place in GOT's reform program supported by the World Bank's Programmatic Structural Adjustment Credit (PSAC).

2.2 PROGRAMME OUTPUTS AND COMPONENTS

The reform measures supported under the SAL II focused on 3 areas of the economy that were in line with the Bank Group Vision Statement and ADF VIII Lending Policy and also the country's PRSP: Private Sector Development; Economic Governance; and Rural Development. The measures formed a narrower set of actions and conditions than the Programme Structural Adjustment Credit (PSAC) but incorporated the PRSP, the MTEF and the 2001 Country Financial Accountability Assessment Study. Table 1 is a snapshot matrix focusing the three components of the intervention. .

Table 1: Matrix of Measures of the SAL II

COMPONENT	MAIN POLICY FOCUS
Private Sector Development	<ol style="list-style-type: none"> 1. Expansion of the Commercial Court 2. Implementation of the new land Law 3. Revision of Business Laws 4. Labour Law Reform 5. Privatization
Economic Governance	<ol style="list-style-type: none"> 1. Budgetary Management 2. Other Governance Components <ol style="list-style-type: none"> a. Expansion of IFMIS to all 19 (now 20) Districts under the Local Government Reform Program b. Issuing of Regulations on implementation of the Public Finance Act and new accounting manual; similar regulations on new procurement law; c. Implementation of corruption diagnostic surveys as part of operationalisation of the National Anti-Corruption Action plan and Strategy adopted in 1999; develop anti-corruption action plans for ministries of Works, health, Education, Home Affairs, AG's Chambers, and TRA; d. improved performance of the public sector (part of PSAC actions); e. Improve the judiciary:- raise ratio of High Court and Court of Appeal Sessions to planned sessions from 50 percent to 75 percent and 100 percent respectively by end-2003;
Agriculture and Rural Development	<ol style="list-style-type: none"> 1. Finalise the Agriculture Sector Development Strategy and the Rural Development Strategy

2.3 LOAN DESCRIPTION

2.3.1 The Bank extended an ADF loan of UA 40 million to support the GOT in its implementation of its PRSP. SAL II was developed as a two-tranche budget support. The understanding was that the counterpart funds generated by the proceeds would first make an entry point into Tanzania's program in the budget exercise of 2002/03, in line with the scheduled disbursement of the First tranche. This initial injection of budget support did not occur in time as described in Section 3.1 on Disbursements.

2.3.2 The overall financing co-shared among a number of donors amounted to US\$882.3 million. In proportion to the GOT external financing requirements, the amount was less than half of the financing procured under the sharply increased debt relief at US\$1718.0 million, as analyzed in section 3.6. Of the co-financed amount, SAL II yielded UA40 million, equivalent to US\$51 million and 5.7 percent of the donor-financed package. The importance of debt relief poses the issue of medium-term sources of financing of the PRSP given that Tanzania has qualified for HIPC relief since 2001.

2.4 PREPARATION, APPRAISAL, NEGOTIATION AND APPROVAL

2.4.1 SAL II preparation and appraisal were closely linked to the GOT overall reform program and the PRSP. It also shared components and was parallel financed with the more comprehensive World Bank Poverty Structural Adjustment Credit (PSAC) and also the PRGF. It would seem there would have been capturable economies-of-scale from joint preparation and appraisal in the ADB/World Bank/IMF axis. The Bank extensively consulted the IMF and the World Bank during the preparation, appraisal and implementation of SAL II but the sequencing in each institution seems not to have created the momentum for optimal joint activities. In the event the Bank's SAL II was highly complementary to PSAC and PRGF but it focused and emphasised a narrower scope of conditions. In addition to pursuing these complementarities, the Bank Group worked actively with the PRBS, a major coordination mechanism of parallel co-financiers combining *bilateral* and *multilateral* creditors.

2.4.2 The nine-member PRBS is a framework for coordinating direct budget support from donors that the Government of Tanzania and its development partners have developed. The PRBS seeks to support the implementation of the Government's poverty reduction strategy by ensuring that adequate resources are provided to priority sectors in the budget. It aims to increase the predictability of donor funding so as to ensure smooth budget execution. It has developed the Performance Assessment Framework (PAF) matrix and the Public Expenditure Management and Financial Accountability (PEFMA) as tools to benchmark progress. Although The Bank timed its missions to coincide with the Annual PRBS, in order to be represented and lately to strengthen the ADB Regional Office representation, it would seem that the Bank should reformulate a more focused technical capacity for this dialogue aimed at more coordinated policy-oriented operations and a rationalization of donor policy conditions, and value addition.

2.4.3 The emergence of PRBS and the PAF among other consultative and aid delivery modalities towards Tanzania raises the issue of whether the Bank should actively participate. The reasons for strengthening participation are overwhelming. The modalities lessen the transaction costs placed on Government agencies that currently now have to cope with diverse donors' procedures. This also works against a project approach and augers well for sector-wide approach and direct budget support. One suggestion would be to strengthen the capacity for policy dialogue and coordination within the ADB Regional Office.

3 PROGRAMME IMPLEMENTATION (ACTIVITIES/COMPONENTS)

3.1 LOAN EFFECTIVENESS AND INITIAL DISBURSEMENT

3.1.1 SAL II became effective on September 2003. A special account named Structural Adjustment Loan II (SAL II) A/C No. 9931202961 was opened with the Bank of Tanzania to which all SAL II resources were disbursed. The first tranche was subject to the seven conditions shown in Annex II and as contained in section 5.01 of the Loan Agreement. All conditions were satisfied except for Condition No. (v) of the Conditions Precedent to disbursement of the First tranche. The condition required Government to enact a new Company Act and prepare draft regulations to govern its implementation. The Companies Act was passed by Parliament in April 2002. The new Company legislation sought to modernize rules governing business operations including licensing and bankruptcy laws. However, there was a delay in establishing the necessary regulations¹. The

¹ The main reason for the delay was that, after loan approval, the Government decided to sub-contract the assignment on Regulations due to its specialized nature and to bypass limitations in drafting capacity in the Ministry of Justice and Constitutional Affairs. Securing funding for the activity caused further delays but after funds were available, even further delays occurred in recruiting the consultant.

GOT indicated that continued delay in release of the funds would affect smooth budget execution, as the ADF SAL II funds were projected for fiscal year 2002/03, which had *already* ended in June 2003. The GOT request met with ADB Board approval in a case of no objection on 23 July 2003, and the condition was moved to the Second tranche conditions to accommodate the unforeseen delay in preparing the Regulations.

3.1.2 The SAL II was among the budget support instruments programmed in the same way as domestic resources. The First Tranche payment amounting to UA 20 million (US\$ 28,628,375.00) was effected at the Bank of Tanzania SAL II special account on 22nd October 2003. The same amount was transferred to the Exchequer Account on 24th November 2003. In other evidence that the tranche was critical to the programme, the GOT had taken interim measures to fill the gap for fiscal 2002/03. Due to adoption of the cash budget management system (itself part of the Conditions Precedent to release of the First Tranche:- Condition iii, which required GOT to have introduced cash flow planning in the preparation and management of the budget) the first tranche of SAL II was programmed for spending during FY 2002/03 which ended June 2003. The GOT covered the interim delay with a draw down of an equivalent amount from its deposit in the Bank of Tanzania. With the receipt of the First tranche in October 2003, the GOT replenished the draw down of the BOT deposit.

3.2 DISBURSEMENT OF THE SECOND TRANCHE

The second tranche of the Loan amounting to UA 20 million (equivalent to US\$ 30,093,308.11) was disbursed in February 2004 after the fulfillment of conditions precedent to its release as set out in Annex II. This included the condition on the Companies Act and related regulations carried over from Conditions for the release of the First Tranche. The proceeds of the Tranche were deposited to a special account named Structural Adjustment Loan II (SAL II) A/C No. 9931202961 at the Bank of Tanzania.

3.3 MONITORING AND REPORTING

3.3.1 During the appraisal of the project it was agreed that, since the loan is policy based budget support, the implementing agency for the project was the Ministry of Finance. Monitoring, evaluation and audit were to be assured through its structure and mechanisms. The Ministry has so far submitted two progress reports and also the government's PCR of SAL II. However monitoring and evaluation of Budget Support by the GOT and donors has become an elaborate process through the Annual PRBS reviews. Participation of the Bank needs to be upgraded for an elaborate and decisive role.

3.3.2 The Public Expenditure Review (PER) Consultative Meetings and the Poverty Reduction Budget Support Facility (PRBS) – which includes a detailed Mid-Term Review, have become the key processes through which donors and other stakeholders engage dialogue and monitor Government's policy performance and expenditure allocations to key PRSP priority sectors. This was the case for example in the Supervision mission of April 2002 and PRSL Identification Mission of March/April 2004. However, participation should generate value addition to the dialogue, the Bank needs to increase its technical preparedness on the ground based in the ADB Country Office.

3.4 IMPLEMENTATION SCHEDULE

3.4.1 Table 2 presents the implementation schedule of the programme showing benchmarks against actual timing.

Table 2: Implementation Schedule: Appraisal vs. Actual

Activity	Planned Timing	Actual Timing
1. Appraisal	March 2001	March 2001
2. Board Presentation	September 2001	September 2001
3. Loan Effectiveness	November 2001	December 2001
4. Release of First Tranche	December 2001	October 2003
5. Supervision Mission	-	May10-17 (2002) May19-29, 2003
6. Second Review (Mid-term)	April 2002	-
7. Release of the Second Tranche	July 2002	February 2004
8. GOT PCR/Audit	September 2002	Issued June 2006; submitted to ADB
9. Bank PCR	December 2002	April 2007

3.4.2 At Appraisal, SAL II was scheduled for implementation during the next 10 months. The Appraisal and Board Presentation phases of the Implementation Schedule show few slippages according to Table 2. However, Loan Effectiveness was delayed for about 10 months. Release of the First Tranche was delayed by some 23 months. There is no trace of a planned Mid-Term Review, but an early supervision mission (May 10- 17, 2002) was paired to a CSP preparation mission. At this point however, no disbursement had taken place, due to the non-fulfilment of one condition prior to release of First tranche: Condition iii on the passage of the Companies Act and accompanying regulations. Another supervision mission visited Tanzania during May 19-29, 2003. Similar delays were carried over in the schedule. The release of the second tranche (expected in 2002) came about almost two years late (19 months than scheduled)

3.5 IMPLEMENTATION

3.5.1 At Appraisal, SAL II was scheduled for implementation during the next 10 months. It was scheduled to be part of the GOT's budget operations and yielded proceeds for that purpose. During the PCR field mission, the Consultant undertook detailed discussions with the Accountant General and Senior members of the Office. The early obstacle to release of the First tranche analysed elsewhere in this report was a disruptive factor.

3.5.2 The Accountant General's Office was a key player in fulfilment of some key conditions in SAL II, especially the Economic Governance component. The roll out of the IFMIS system to 19 (now 20) sub-treasuries is credited mainly to that Office. Connectivity in IFMIS for example was affected through the Office to 85 districts. The GOT accounts are online, in a system centered in that Office, which has attracted the interest and inquiry on 'Best Practices' from neighbouring countries such as Malawi.

3.5.3 Yet, involvement of the above Office in SAL II preparation, appraisal and negotiation, was limited. It would expedite matters where key players in budget support activities are apprised of the interventions, as they can provide useful inputs. In the case of IFMIS, there were substantial collateral expenditures required to use generators for electricity, as well as the need to sustain equipment as technology changes.

3.6 FINANCIAL SOURCES AND DISBURSEMENT

3.6.1 Projections of Tanzania's financing requirements during 2000-2002 indicated a Financing Gap of \$2635.0 million. External debt relief under the various arrangements (HIPC and non-Paris Creditors) were expected to cover \$ 1718 million. This left a financing Gap of \$917 million. Table 3 shows Tanzania's External Financing Requirements during 2001-2002. Debt relief during this period thus carried far greater significance to the financing of Tanzania's Program than all development partners combined in the financing of the residual gap. Of the \$ 917 million, development partners financed \$882.3 million, mostly in balance of payments support and budget support. Table 3 shows the relative shares of the partners. ADB's SAL II financed about 5.9 percent of the requirements.

Table 3: Tanzania's External Financing Requirements 2001-2002

Source	Amount US\$ Millions	%
ADF	51.0	5.87
WorldBank PSAC	190.0	21.62
MDF/PRBS ²	446.7	50.50
IMF	168.0	19.0
Others	26.6	3.01
TOTAL	882.3	100.0

Source: Appraisal Report

3.6.2 The financing availed left a gap of \$34.7 million which was to be met with disbursements on new commitments. The Bank's loan was fully disbursed in two tranches, September 2003 and February 2004.

3.7 AUDIT

As agreed at appraisal, the implementing agency for the project was the Ministry of Finance through its structure mechanism of monitoring, evaluation and audit. The Ministry submitted two reports to the Bank and were deemed satisfactory.

4 PROJECT PERFORMANCE AND RESULTS

4.1 OVERALL GOVERNMENT PROGRAMME

4.1.1 SAL II was embedded in the GOT reform programme. The review of outcomes focuses on both the overall programme and the SAL II. Strengthening growth and human capabilities were the two overarching objectives. The process continued with medium-term revenue targets, taking a range of measures to boost tax administration substantially, including adoption of a new medium-term corporate plan for the Tanzania Revenue Authority (TRA), refocusing management and administrative resources that will help broaden coverage of large taxpayers; strengthening of administration of VAT and presumptive taxation, and actions to broaden the tax base through

² Poverty Reduction Budget Support (PRBS) donors are UK, Netherlands, Sweden, Finland, Denmark, Ireland Norway, Switzerland and European Union.

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

4.1.2 A key outcome over an extended period (1996-2006- that includes the three years during which SAL II, 2001-2003 supported the process) is that real GDP has averaged 5 percent. Inflation fell from about 16 percent to about 4 percent over the same period. This is a remarkable achievement given the dependence of the economy on rain-fed agriculture and the role of agriculture in generating about half of GDP.

4.1.3 The principal downside of the above macro-based success is that it has not propelled an equivalent pace and impact in poverty reduction or private sector development. The persistence of poverty in Tanzania, especially in the rural areas, is cause for concern because of the relatively marginal progress made relative to overall GDP growth. Tanzania's per capita GDP growth rate averaged about 2 percent during 1996-2006, and nearly 2¾ percent during 2000-05. Its GDP per capita in 2005, at about US\$337, was well below sub-Saharan Africa's average of US\$568. Tanzania was ranked 160th on the 2001 Human Development Index, below the average for sub-Saharan Africa. In addition poverty has deepened as a rural phenomenon. While it declined by 10 percentage points to about 18 percent in the capital Dar es Salaam between 1991 and 2001, it declined by only 2 percentage points to 39 percent in the rural areas. Some 87 percent of all poor people live in rural areas.

4.1.4 Poverty and private sector investment are correlated facets of Tanzania's economy. Increasing and shifting growth of private investment to generate a supply response, especially in the rural sector, would generate incomes through employment in the sector. It would help quicken the pace of poverty reduction.

4.2 THE STRUCTURAL ADJUSTMENT LOAN II

4.2.1 The Bank Group's policy-based loan was embedded in the GOT reform programme to support Tanzania PRSP. Under the overall program, the specific components of ADB's SAL II and their stipulations have performed well. Their implementation in SAL II as per required actions is analysed below. The rate of GDP growth in real terms increased from 5.7% in 2001 to 6.2% in 2002 and reached 6.7% in 2004. Growth stemmed from relatively strong performances in agriculture, mining, manufacturing, construction and tourism. Inflation rate dropped to 4% in 2004. Foreign reserves have stayed well above six months of imports of goods and services. Domestic revenue mobilization increased from less than 50 billion shillings per month in late 1990s to 145 billion shillings per month during the FY 2004/05.

Component 1: Private Sector

4.2.2 The GOT undertook the measures stipulated for this component in SAL II and expansion is ongoing. Firstly, the operations of the Commercial Court which was established in 1998 to strengthen the enforcement of commercial contracts and speed up the resolution of commercial disputes to regions outside Dar es Salaam, had remained centralised in Dar-es-Salaam. Services were expanded and implemented, notably in Mwanza and Arusha in late 2002. Later on in 2003 the services were extended to Mbeya and Moshi and are being implemented in phases. The computerization of the case filing and Registry System has been accomplished at the High Court Headquarters and three centers (Mwanza, Mbeya and Arusha) and it is being implemented in phases to cover the remaining centers.

4.2.3 Secondly, reform of the land registration system for enabling land to be used as collateral against credit or mortgages is ongoing. The Land Regulations were gazetted through Government Notice (GN) No. 71-85 published on 4th May 2001, thus making the Land Act No. 4 of 1999 effective. Thirdly, measures to harmonize and rationalize central and local government's taxes aiming at reducing and eventually eliminating the tax burden and multiplicity of taxes on investors have been implemented. Fourthly, the Government established the Tanzania National Business Council (TNBC) chaired by the President of the United Republic of Tanzania and the Investor's Roundtable (IRT) as dialogue mechanisms with the business community for improving the business environment. Fifthly, a Private Sector Development Strategy (PSDS) is in place, incorporating a focus on SMEs and drawing from several sectoral policy documents. Implementation on a pilot basis of selected activities under the PSDS commenced in November 2004.

4.2.4 A major hurdle in fulfilment of conditions under this component involved Condition (v) of the Conditions Precedent to disbursement of the First tranche. The condition required Government to enact a new Company Act and prepare draft regulations to govern its implementation. The Companies Act was passed by Parliament in April 2002. However, there was a delay in establishing the necessary regulations, triggering a 'no objection' request that was granted by the Bank on July 23, 2003, to move the condition to Second tranche conditions. The consequences invited scrutiny of the structure of the Bank's conditions.³

4.2.5 Recognizing business licensing as a regulatory rather than a revenue raising instrument, the Government eliminated business license fees for small business and limited it to Shillings 20,000 (about USD 20) for others. The Government has also adopted a strategy for business license reform to limit the time it takes to obtain a license to only two days. The lead role of the Ministry of Industries and Trade is being limited to assessing and administering applications.

4.2.6 Other initiatives are in place to enhance the environment for development of the private sector. A Better Regulation Unit (BRU) has been established as a supportive unit for monitoring implementation of the Business Environment Strengthening in Tanzania (BEST) programme. The Unit has been strengthened with the recruitments of the Chief Executive Officer (CEO) and the Lead advisor. Further, the first phase of the Labour Law Reform was approved by Parliament in

³ Adoption of the cash budget management system (itself part of the Conditions Precedent to release of the First Tranche:- Condition iii) required GOT to have introduced cash flow planning in the preparation and management of the budget). Delay of condition (v) thus undermined programmed spending for FY 2002/03 which had *already* ended in June 2003 when the 'no objection' was being processed. This exposes three frequent problems with the Bank's conditions in the recent past: 1) number and efficacy; 2) 'cascading' where failure of one condition *outside* the competence of the Borrower (GOT in this case, while Parliament was the competent authority for passing the Companies Act) knocks on other conditions that the Borrower is competent to fulfill; and 3) poor targeting, in this case involving tri-directional triggers: Condition (v) could not be cleared without establishment of the regulations; Disbursement could not take place; and Condition (iii) could not be implemented without disbursement.

April 2004. It addresses employment relations, collective labour relations, dispute resolutions, and labour market institutions. This measure will contribute to improving the environment for investment and domestic bank lending.

4.2.7 The bids for leasing the services of DAWASA were invited, evaluated and awarded to City Water Company. However, during the time of lease, City Water failed to abide with some of the conditions of the service contract, even after several reminders and follow-ups. The Government, after consultations with all the stakeholders including ADB, terminated the services of City Water Company in 2005. In the transition, GOT leased the services to a local company, Dar es salaam Water Supply and Sanitation Company. The government is still committed to lease the services to a private company through international open bidding. Finally, labour law reforms are in the pipeline as focused in the SAL II Loan. The Government prepared the Terms of Reference for conducting a study on the functioning of the labor market and sent a copy of TOR to the Bank.

Component 2: Economic Governance

4.2.8 The Government budget for FY 2001/02 adopted PRSP priorities focusing water, basic education, health, agriculture (research and extension), rural roads, the legal and judicial system and HIV/AIDS). It was in line with the 3-year cycle of MTEF 2001/02 – 2003/04. The allocation to priority sectors increased to 40.1% of total recurrent budget in 2001/02, well above the SAL II target of 33.2 percent. The share of ‘Other Charges’ for priority sectors in total recurrent budget was stipulated to move from 11.3 percent to 13.4 percent over FY 2000/01 to FY 2001/02. It increased from 16% in FY 2000/01 to 23% in FY 2001/02, again well above SAL II targets. Similarly, the budget guidelines for FY 2002/03 also adopted the PRSP expenditure priorities and were in accordance with the MTEF 2001/02 – 2003/04. The Bank Mission of May 2002 was able to verify satisfactory progress in its BTOR.

4.2.9 Public Expenditure Management has been strengthened with cash flow planning in preparation and management of the budget. This limits expenditures to resources availability through the implementation of a centralized payment system which is facilitated by the IFMIS. In the Guidelines for the preparation of the Medium-Term Plan and the Budget Framework (2002/03 – 2004/05) issued in December 2001, all MDAs, Regions and Councils were instructed to provide cash-flow plans which would form basis on which funds will be released. In response all MDAs, Regions and Councils prepared cash-flow plans using formats provided in the Budget Guidelines.

4.2.10 Due to improved expenditure control, budget deficit has been kept inline with the IMF-PRGF programme targets. Further, the PER and the MTEF processes involving all stakeholders have continued to be strengthened resulting in improved expenditures prioritization. Budget execution has also improved by releasing funds to priority sectors on a quarterly instead of a monthly basis. The Government continues with implementation of the revised Public Financial Management Reform Programme (PFMRP) which was updated with the Country Financial Accountability Assessment (CFAA) and Report on Observance of Standards and Codes (ROSC) as well as rolling out the IFMS to all Government agencies including all LGA.

4.2.11 A number of other dimensions of Economic Governance were targeted in SAL II conditions. First, the GOT was to issue the regulations for the 2001 Public Finance Act. These were published through GN No. 132 of 6th July 2001. The new Accounting Manual was prepared and circulated to the accounting Staff for use with effect from FY 2002/03. The GOT was to publish regulations for the implementation of the new Public Procurement Law, and develop an action plan to strengthen capacity in procurement for Central Tender Board, Ministerial Tender Boards, and District and Regional Tender Boards. The regulations for the 2001 Public Procurement Act were published through GN No. 137 and 138 of 13th July 2001; and the Government prepared Action Plans for

strengthening capacity in procurement of the Central Tender Board, Ministerial Tender Boards, and District and Regional Tender Boards.

4.2.12 The SAL II also targeted operationalisation of the National Anti Corruption Strategy and Action Plan (NACSAP) adopted in 1999 but updated for 2003-05. Quarterly reports are being prepared to track progress made in the implementation of anti-corruption plans in the MDAs. Reporting by MDA has improved significantly. The Good Governance Coordination Unit (GGCU) in the President's Office has commissioned work to include more quantitative and qualitative data in areas of monitoring and controlling public procurement, public finance and legal and judicial processing. This data is expected to provide guidance for future policy reform on governance. In addition, in order to ensure that complaints from the public are adequately addressed, a revision of the code of conduct for public servants has been carried out in consultation with stakeholders and has been published. Human and financial resources capacity to coordinate and implement the NACSAP is being addressed under the Public Service Reform Programme (PSRP). Finally, the Public Service Act was passed by the Parliament in April 2002 and assented by the President of the United Republic of Tanzania on 27th May 2002

Component 3: Rural Sector Development

4.2.13 The Government commenced implementation of the Agriculture Sector Development Strategy (ASDS), focusing promotion of higher agricultural growth and improved rural incomes as well as food security by raising productivity and improving the profitability of agriculture. The strategy continued to be implemented in five strategic areas of intervention: (i) strengthening the institutional framework; (ii) creating a favourable environment for commercial activities; (iii) identifying public and private sector roles in improving support services; (iv) strengthening marketing efficiency for inputs and outputs and; (v) mainstreaming planning for agricultural development in other sectors. In addition, the GOT undertook the participatory development of the Agriculture Sector Development Programme (ASDP) aimed to operationalize the ASDS. The latter was finalized in November 2002, with three sub-components: Agriculture Sector Support and Implementation at District and Field Level; Agriculture Sector Support at National Level; and Cross-Cutting Issues with other Sectors at the National Level. The next phase of the ASDP entails formulation of sub-programmes and components and funding of the same. Three Task Forces have been established for the detailed formulation of the sub-programmes. In the background of these developments is the Rural Development Strategy, which is being implemented as the overall framework for coordinating and integrating policies and strategies to improve rural livelihoods.

4.3 RESULTS IN RETROSPECT & MEDIUM TERM POLICY OPTIONS

4.3.1 Despite substantial successes of the GOT Programme and SAL II, on the policy front, the outcomes are relatively poor in the principal target objectives of rapid economic growth *with* poverty reduction. Poor structural and supply responses and impediments tend to diminish the *impact* of good macroeconomic management, and reduce the potential dividends of growth for poverty reduction. To quicken the pace of the outcomes/dividends of macro-policy stability on the poverty reduction outcomes, the impediments to the supply response should be addressed in medium-term interventions.

4.3.2 A number of structural impediments appear frequently in the review and policy discussion. One is the size and quality of gross private capital formation as a share of GDP. This declined from about 13½ percent during 1995–99 to about 11 percent since 2000. Paradoxically for an economy in transition from socialism, the share of private capital formation in total capital formation declined

from about 80 percent in 1999 to 60 percent in 2005. This needs to be reversed to maintain and propel the pace of GDP growth.

4.3.3 In one segment of private sector investment, FDI, there are worrisome trends that do not yield proportionate impacts on poverty reduction. Having in recent years attracted substantial FDI, Tanzania has enjoyed growth of these investments mainly in natural resource extraction, especially gold mining, which has limited multiplier effects or productivity impetus. Value-addition domestically could be one way of capturing further gains from FDI.

4.3.4 On the other hand, measures need to be developed to improve the quality of private sector development. The weaknesses of the sector include a poor business climate attested by a number of global benchmarks. The World Bank's 2006 *Doing Business* report ranks Tanzania 140th in the overall ease of doing business out of 155 countries surveyed. Tanzania is ranked 101st out of 117 countries in the Global Competitiveness Report relating to production of electricity, and energy production bottlenecks add to costs that reduce competitiveness. The World Economic Forum 2005, ranks Tanzania 82nd out of 116 countries in the quality of the national business environment, and 71st in the Growth Competitiveness Index out of 117 countries. Three key factors account for deficiencies in the investment climate: a) burdensome licensing procedures, reflected in high start-up costs, insufficient access to credit, restrictive labor regulations, difficulties in registering property and poor property rights; b) a poor infrastructure, recently exemplified by the crisis in the energy sector; and c) corruption and poor governance that undermine private investment. In the latter context, corruption is induced by government regulations susceptible to rent seekers complex business licensing systems, overlapping regulatory mandates, ad hoc provision of tax exemptions, and a susceptible legal system, that leaves loopholes in dispute resolution.

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

4.3.6 In the financial sector as well, there emerges a weak response to available bank credit, raising the question of financial deepening. Although the off-take of bank credit (growth of private sector credit) was broadly equivalent to the net availability of funds to the private sector as a percent of GDP over the implementation period of SAL II -2001/02-2002/2003- this is an exception to previous and recent years. Liquidity has increased while bank claims on the private sector remained relatively low. In addition, the credit absorbed by the private sector is concentrated in about 200 'bankable' enterprises while credit access to the rural private sector is virtually zero. Financial deepening as well as diffusion of credit services to more borrowers should be designed as intervention targets.

4.3.7 In another worrisome area targeted by the SAL II Programme (promotion and diversification of exports: - Component 1, growth through macroeconomic stability) a sluggish export supply response has defied both the Programme support and substantial depreciation of the Tanzania shilling during the implementation of SAL II. The latter should have improved competitiveness and generated poverty-reducing exports since Tanzania exports mainly agricultural commodities. .

4.3.8 Finally an emerging issue is that of the Bank's position on growing donor coordination and the efficiencies of aid harmonization. In Tanzania, this is evidenced by the influence of the Poverty Reduction Budget Support Facility (PRBS) made up of nine donors. It seeks to support the implementation of the Government's poverty reduction strategy by ensuring adequacy and

predictability of resources provided to priority sectors in the budget. PRBS and GOT have developed the Performance Assessment Framework (PAF) matrix as a tool to benchmark progress. This has widened the voice of policy players from the narrow scope of multilateral donors and proved effective in reducing the transactions costs of policy dialogue.

4.3.9 Although The Bank now times its missions to coincide with the Annual PRBS meetings in order to be represented and lately to strengthen the ADB Regional Office representation, it would seem that the Bank should reformulate and upgrade technical capacity for this dialogue to give effective value added to the dialogue as a key player on the continent. Coordination of policy-oriented operations, a rationalization of donor policy conditions, and value addition are thus important factors in future lending in Tanzania. The Bank's case for strengthening participation is overwhelming. The modalities lessen the transaction costs placed on Government agencies that currently have to cope with diverse donors' procedures. The process also entrenches donor coordination in policy support.

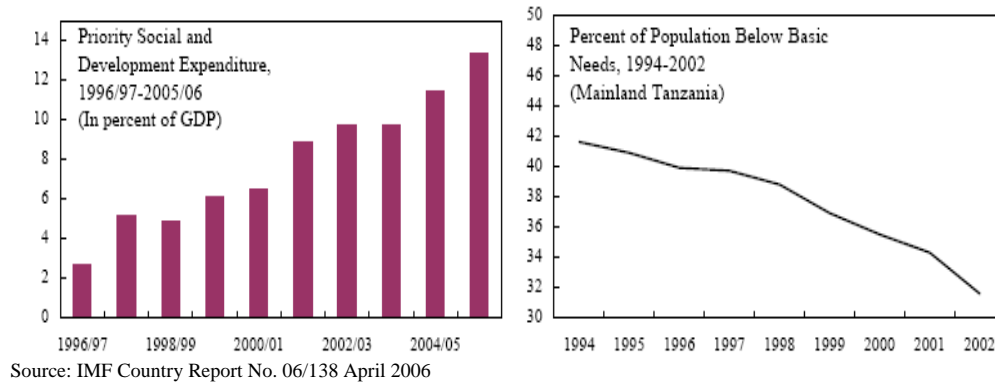
5 ECONOMIC, SOCIAL AND ENVIRONMENTAL IMPACT OF SAL II

5.1 THE SOCIO-ECONOMIC IMPACT

5.1.1 The GOT reform programme had several players and the financing coincided with HIPC debt cancellation. Social impact indicators take time to concretize. Additionally, joint funding of the same program by various players makes it difficult to calibrate impact to assign the contribution of SAL II. With this caution a summary analysis of outcome of the interventions supported under SAL II is discussed as follows.

5.1.2 The implementation of SAL II came at the mid-point of a decade that has seen a decisive change in policy thinking in Tanzania. Socio-economic conditions have improved. During 1996-2006 the gains came from a combination of good economic performance and macro-stability. A good illustration of the twin factors that have laid the foundation for growth performance is that declining inflation and GDP growth over the last decade, helped real per capita GDP growth to accelerate to nearly 5 percent. Inflation has declined to around 5 percent from about 30 percent in the mid-1990s. Sustained economic reforms have thus paid dividends in strong macroeconomic performance. Real GDP growth over 2004/05 and 2005/06 was running at about 7 percent in line with projections. The leading sectors in 2005 were trade and tourism, manufacturing, mining and construction, whose combined contribution to GDP was about 40 percent. This progress has been mirrored by a significant increase in the provision of PRBS.

5.1.3 In line with PRSP-linked expenditures and increases in priority areas, the data shows that expenditures have tracked the conditions of the GOT Programme and the SAL II support. Fig 1 shows that as priority social and development expenditures rose from about 7 percent to 11 percent of GDP over the period 2001/02 -2003/04 encapsulating the implementation of SAL II, the percent of the population living below basic needs was falling continuously over 1996-2002. Institutional capacity has also improved, including stronger structures for domestic revenue mobilization, public expenditure management, and the financial sector.

Fig. 1: Increased Priority Social & Development Spending & Decrease in Poverty

5.1.4 Other dividends supportive of positive social impact emerge from the easing of expenditures (subsidies) to support parastatals. A series of privatizations have neutered the leakage of revenues to these enterprises paved the way for reduced fiscal burden of public enterprises and created room for increased priority social and development expenditures.

5.2 ENVIRONMENTAL IMPACT

The environmental impact has not been measured and it was not a specific objective of SAL II. However, indirect and limited positive effects are likely due to investments and progress made in the priority sectors of the PRSP supported by the SAL II Loan: Agriculture, Infrastructure (rural roads), Education, Health, Water, HIV/AIDS and Judiciary. Tanzania has an Environmental Protection Agency was despite capacity constraints is becoming more effective.

6 PROGRAMME SUSTAINABILITY

6.1 SUSTAINABILITY OF OUTPUTS

6.1.1 The GOT has shown a strong commitment to ownership of the policy actions. Initial delays occurred due to the design of the SAL II program, especially the conditions. This PCR assumes that the commitment will be continued in the medium-term when it is proposed that the Bank/GOT address structural impediments that can help translate growth into more significant poverty reduction and for a wider base of society.

6.1.2 The PCR mission saw evidence at a high level in the Office of the Accountant General that public accounting and auditing practices are being improved. A computer-based Integrated Financial Management System (IFMIS) is in operation and has helped the tracking of the flow of resources from the Treasury to spending units in Ministries and districts. Spending units have autonomy in expenditure and are also held accountable for result. An anti-corruption unit in the Office of the President is highly visible and could help sustain the gains made in Economic Governance.

6.1.3 The GOT is making commendable efforts to manage the existing financial resources well. The introduction of MTEF and regular annual PERs (called PEFAR since the 2004 amalgamation of World Bank's Public Expenditure Reviews with similar reviews by other donors), the dialogue through the PRBS and PAF reviews are rendering greater efficiency in monitoring the reform process with common reference points among co-financiers.

6.2 SUSTAINABILITY OF INPUTS

There is regular formal and informal dialogue on the reform among government agencies, and between Government agencies and the development partners. The progressive reduction in reliance on donors will prove difficult however. Government revenue is weak and skewed. While most development and some recurrent expenditure are still financed by donors, revenue collection is concentrated in Dar-es-Salaam region. The results of reforms in poverty reduction are the prerequisite for success in resource mobilization to fund an increasing share of the budget from domestic revenue. Furthermore, the key staffs managing the reform agenda are capable but over-stretched. There is limited capacity in many Government agencies.

6.3 SUSTAINABILITY OF SOCIAL OUTCOMES

The important concern is the distribution of the economic benefits from the reforms. In order to marshal continued popular support for the reforms, policy-makers need to deliver gains from the reform demonstrating benefits to most Tanzanians. If the policy actions do not deliver on the axis: macro-stability, investment, growth and poverty reduction sufficiently to become inclusive and to empower the majority of Tanzanians, popular support for the reforms could diminish.

7 PERFORMANCE OF THE BANK AND THE BORROWER

7.1 PERFORMANCE OF THE BANK & COORDINATION WITH CO-FINANCIERS

7.1.1 SAL II reflected the Government's Letter of Development Policies, and the policy actions were well timed and relevant. The Staff Appraisal Report (SAR) followed closely the GOT overall reform program but was too uncritical of the now well-known disconnect between the pursuit of macro-stability and poor real sector outcomes in Africa. SAL II could have been more conceptually innovative in foreseeing and addressing the structural impediments in the axis: macro-stability, investment, growth and poverty reduction that are recommended for follow-up in this PCR. SAL II was also ambitious, particularly in the area of privatizations that eventually malfunctioned and spawned the current skepticism, disruptions and high costs especially in the energy and water sectors. While the design of the Bank Group PBLs has been broadly appropriate in Tanzania, Bank conditions have also exhibited three main problems: excessiveness, poor targeting, and the related outcome of cascading. SAL II was not immune to these issues.

7.1.2 The conditions of SAL II were scaled down compared to the previous SAL I intervention. The operation also had two tranches compared to three in the previous operation. However, targeting was a problem as illustrated by three conflicting situations created during implementation. The Bank pitted a tri-directional set of triggers that could not work. Condition (iii) on adopting cash flow planning and management of the budget for FY2002/03 could not be implemented without First Tranche disbursement, because these proceeds of SAL II were programmed to support that condition in the budget of FY 2002/03, ending June 2003. When disbursement failed because GOT could not fulfill Condition (v) of First Tranche disbursement on establishment of the Companies Act and Regulations, this directly undermined any hope that the objectives of Condition (iii) could be met. Commencement of implementation of SAL II was trapped. The GOT unhinged the impasse through the Bank of Tanzania. It drew down the equivalent of the SAL II First Tranche in its deposits and met Condition (iii). It then officially applied for an exemption and transfer of Condition (v) to Second Tranche conditions, secured the First Tranche disbursement from the Bank Group, and used it to replenish the draw-down at BOT. This 'accounting' solution and ensuing delay would have been unnecessary if First Tranche draw-down had been made easier by making

Conditions (iii) and (v) monitorable requirements of Second Tranche disbursement, subject to verification during the supervision missions that followed SAL II effectiveness.

7.1.3 Cascading of conditions (in which the failure of a poorly-aimed condition holds up fulfilment of other conditions or causes them to fail, thus leading to implementation and disbursement delays) also became evident. The Executing agencies or even the GOT were not the competent actors to fulfil some of the conditions. Conditions set as calendar dates for Parliamentary or legislative actions for example are not in the competence of the Ministry of Finance that took on the role of executing agency. Parliament set its own calendar, actions, and standards independently of the executing agency, the Bank Group, or even Cabinet and GOT. In this case, Parliament passed the Companies Act engaged by the Bank in Condition (v) of First Tranche release in April 2002. But competencies for drafting of the regulations were pitched high, causing procurement delays. Again implementation of SAL II was trapped, triggering an official application for exemption and transfer to Second Tranche conditions. Conditions thus need to be calibrated to the appropriate competences.

7.1.4 Spanning 5 interventions to date, in tandem with other major partners of Tanzania's economic transition, a dilemma also emerges on the funding and achievements of economic activity with macroeconomic stability. The approach has set the stage for rapid and non-inflationary economic growth. Enhanced with HIPC and MDRI debt relief, growth has also strengthened the external sector.⁴ Specifically, during the implementation of SAL II, the rate of real GDP growth increased from 5.7% in 2001 to 6.2% in 2002 and had reached 6.7% by 2004. Growth stemmed from relatively strong performances in agriculture, mining, manufacturing, construction and tourism. The inflation rate had dropped to 4% by 2004, down from double digits in the 1990s. Foreign reserves have stayed well above six months of imports of goods and services. Domestic revenue mobilization increased from less than 50 billion shillings per month in late 1990s to 145 billion shillings per month during the FY 2004/05. Yet revenue mobilization is still low. For example, over 80 percent of the revenue is accounted for by Dar-es-Salaam region alone.⁵ This poses a quandary for revenue mobilization and the associated expectation of reduction in aid dependency. In theory, this strategy would only succeed where incomes were rising.

7.1.5 This PCR rates the Bank's performance satisfactory nevertheless (Annex III) influenced particularly by the substantial activities in the SAL II operation to appraise the Bank on the changing strategy on development coordination and efficiencies on transactions costs of policy lending in Tanzania. The first SAL II supervision mission of May 10-17 2002 set the pace by closely examining the PER Consultative Meeting and the Poverty Reduction Budget Support Facility (PRBS) Mid-Term Review. These are the key processes through which donors and other stakeholders are now monitoring Government's policy performance and expenditure allocations to key PRSP priority sectors. Nevertheless, the mission's analyses do not seem to have elicited new thinking or proposals on Bank approaches to coordination and dialogue within the new strategy. An appraisal of instruments that the Bank could use to increase its presence and value added in this engagement was not developed or given with the subsequent supervision mission. Thus, the level of co-ordination with the other multilateral and bilateral donors increased, but without Bank gearing itself on the strategy and its interests in it. While extensive effort had been made to harmonise SAL II to the work of joint financiers such as the World Bank through its PSAC, and while the Bank is recognised in the Borrower's PCR of June 2006 as a highly appreciated actor in policy based lending, it needs to

⁴ The Government decided to place the IMF's MDRI resources in a special account at the BoT to be used to fund the foreign exchange component of high priority pro-poor social outlays and growth-critical economic projects. During 2005/06 it was envisaged that some of the funds would be spent to redress the impact of the drought to alleviate food and power shortages.

⁵ See TANZANIA: PUBLIC EXPENDITURE AND FINANCIAL ACCOUNTABILITY REVIEW MISSION FOR 2004/05, Aide Memoire, May 12, 2005.

apply its authority in regional development financing and experience to pursue two main objectives in the new coordination strategy.

7.1.6 First, more value-adding, active and frequent involvement in the policy dialogue would be required. Second, to deepen engagement and bring niche value added to the strategy, Bank policy lending should be supported by some independent economic and sector studies, especially on perspectives to fight structural impediments in the axis: macro-stability, investment, growth and poverty reduction. These studies should be used to strengthen the work of the ADB Office in the coordination and dialogue between donors and GOT.

7.1.7 SAL II conducted two supervision missions, the first in May 2002 when First Tranche disbursement was held up. The missions were adequate and appreciated by the Borrower. They also benefited from the emerging joint donor activities in dialogue and monitoring vis a vis GOT. Yet they drew few insights on the Bank's need to craft a coordination strategy to guide its role in the new approach. In addition the structural impediments highlighted in this PCR should have attracted multi-sectoral concerns in the subsequent supervision mission to include private sector specialists, and perhaps a consultant focusing on the weaknesses in the financial sector.

7.1.8 Co-financiers: SAL II drew its policy reasoning substantially from the World Bank's PSAC (Appraisal Report, para. 4.2.1) but had a narrower scope. It also shared Components with the World Bank on Private Sector Development and Economic Governance and thus complemented PSAC. During program appraisal and implementation the ADF collaborated closely with the World Bank in exchange of information.

7.2 PERFORMANCE OF THE BORROWER AND EXECUTING AGENCY

7.2.1 The Ministry of Finance (MOF) was the executing agency and BOT was delegated to handle financial management. The performance of the borrower was satisfactory and innovative in the face of the contradictions in conditions analyzed in section 7.1. By and large, implementation of the operation went smoothly after initial disruption by Conditions (iii) and (v). Except a few strategic (or in some case unforeseen) delays and outcomes in the privatisation of parastatals, most policy actions were implemented as per the agreed schedule. It is a mark of the Borrower's strong commitment to the stipulations of SAL II and the overall reform program that they persevered with privatization even in the case of DAWASA despite unpalatable outcomes in the sector.

7.2.2 Monitoring of the overall programme, of which SAL I was a component, was adequate. Except for the Borrower's PCR, the PCR exercise was unable to trace reports, including audit reports, to the Bank although they almost certainly exist for donors resident in Tanzania. The Bank's recent set-up on the ground should make it easier to obtain timely reports and to participate in the regular dialogue between GOT and donors.

7.2.3 Following the implementation of the first generation PRS, the Government in collaboration with stakeholders conducted a comprehensive review of the first cycle (three years) implementation of the PRSP. The review process was a long consultative and participatory process involving a wide range of domestic and international stakeholders. The twin objectives of the review process was to (i) collect views and build consensus on poverty reduction measures, and (ii) build national ownership of the poverty reduction initiatives in the country. Out of the exercise has emerged the formulation of the second generation of PRS, the National Strategy for Growth and Reduction of Poverty (NSGRP) in Kiswahili MKUKUTA. This is an outcome/ result based strategy and is more effectively linked with the Millennium Development Goals (MDGs).

7.2.4 The MKUKUTA/NSGRP has sharpened the focus of the Tanzania's development, growth and reduction of poverty policies and strategies. It provides a coherent framework for coordinating and channelling resources for growth and poverty reduction programmes with clear targets and set.

8 OVERALL PERFORMANCE AND RATING

8.1 OVERALL PERFORMANCE

The overall performance is rated satisfactory using detailed criteria that aggregate Overall Implementation Performance and Bank Performance, see Annex III. Ratings show that the Borrower performed better than the Bank.

9 CONCLUSIONS AND POLICY LESSONS LEARNED

9.1 CONCLUSIONS

SAL II was a successful operation as all the agreed policy actions were implemented, though behind schedule. The early transfer of Condition (iii) to Second Tranche conditions was critical for SAL II startup and implementation. The program focused on policy areas that are critical to poverty reduction. As in previous PBLs the Bank was not involved in policy design. Except for the Completion Report, the SAL II does not seem to have been well reported to the Bank, although the reporting almost certainly exists for progress of the reforms to donors resident in Tanzania. This suggests a lack of follow-up by the Bank Group and lack of coordination with other donors, specifically the emerging PRBS group.

9.2 LESSONS LEARNED

Important lessons learned may be listed as follows:

- The success exposes a number of structural constraints that hinder the translation of macro-stability into improved private sector performance and better livelihoods.
- The GOT continues to demonstrate strong commitment to the reforms.
- The Bank is insufficiently represented in policy design and accompanying dialogue and coordination among donors and GOT.
- Reporting requirements seem to have lapsed although the Bank is probably not receiving the reports made available to donors on the ground in Tanzania.

9.3 RECOMMENDATIONS

- It is recommended that the Bank should shift policy attention to the structural impediments that hinder the strength of the axis: macro-stability, investment, growth and poverty reduction.
- The design of conditions should take into account more realistically possible slippages in the implementation schedule.
- A start can be made especially with economic and sector studies that examine the investment climate and the methods of credit delivery to the rural and informal sectors which host the majority of Tanzanians.

- Given that the Bank did not adopt a clear decision on participation in the donor/GOT policy coordination and dialogue that took place on the ground during SAL II, this needs to be addressed. The Bank has a Country office now, and donors have developed an elaborate system of coordination and dialogue and instruments for doing so.
- The Bank needs to take its proper role in this strategy with some authority and niche value added. It needs to back up its Country Office-based participation with the studies that can have an innovative bearing on the policy design and content of the country's programs. The information will have other critical uses such as the development of the CSP.
- The studies can also help re-gear the Bank's proper role in the new strategy of donor engagement with GOT in policy lending. The Bank's field office should collaborate with Headquarters in tightening the reporting requirements of policy based lending.
- Multi-tranche Bank operations raise the risk of delayed disbursement, through possible cascading of conditionalities. Therefore the Bank should move to multi-year single tranche operations, within the PRBS framework.

Main Conditions of the Programme

The second Structural Adjustment Loan (SAL II), amounting to UA 40 million was signed on the 28th of September 2001. According to the Agreement, the Loan resources were to be disbursed in two tranches. The first tranche amounting to UA 20 million was released in October 2003 after fulfilling the conditions precedent to its release. One condition, submission of Companies Act Bill to Parliament and preparing its Regulations, was moved to the second tranche conditions after an unforeseen delay in preparing the Regulations. The specific conditions for the release of the first tranche and actions for their fulfilment were as follows:

- 1.1 Opening of a Special Foreign Exchange Account on conditions acceptable to the Fund into which the proceeds of the loan shall be disbursed;
- 1.2 The Government Budget for FY 2001/02 has (a) adopted the Poverty Reduction Strategy Paper (PRSP) priorities and in accordance with the Medium Term Expenditure Framework (MTEF) for FY 2001/02 – 2003/04; (b) increased the allocation to priority sectors to at least 33.2% of total recurrent budget; and (c) increased the share of ‘Other Charges’
- 1.3 The Government has introduced cash flow planning in the preparation and management of the Budget.
- 1.4 The Government has issued and published (in the Gazette) regulations for the implementation of the new Land Act in order to facilitate the use of land as collateral for bank credits and other commercial transactions.
- 1.5 The Government has issued and published regulations for the implementation of the 2001 Public Finance Act and issued a new Accounting Manual based on the Public Finance Act.
- 1.6 The Government has published regulations for the implementation of the new Public Procurement Law. And developed an action plan to strengthen capacity in procurement for Central Tender Board, Ministerial Tender Boards, and District and Regional Tender Boards.

The second tranche of the Loan amounting to UA 20 million was disbursed in February 2004 after the fulfillment of conditions precedent to its release as presented below:

- 1.7 The Government to provide justification for the use of at least fifty percent (50%) of the first tranche.
- 1.8 The 2002/03 Budget guidelines have adopted PRSP expenditure priorities, and are in accordance with the MTEF 2001/02 – 2003/04.
- 1.9 The Government has made adequate allocations in the Budget to fund the implementation of the Anti-corruption action plans for the Ministries of Works, Health, Education, the Attorney-Generals’ Chambers, Home Affairs and the Tanzania Revenue Authority, and has commenced implementation of the plans.
- 1.10 The Government has prepared action plans satisfactory to the Fund to (a) ensure that court cases are heard and determined timorously, and (b) raise the ratio of actual High Court and Court of Appeal sessions to planned sessions from 50 percent to 75 percent and 100 percent respectively by end of 2003, and in addition, made appropriate budgetary allocations to implement the plans.
- 1.11 The government has extended the coverage of the Integrated Financial Management System (IFMS) to all 19 Sub-Treasuries in the regions and has prepared action plans to extend IFMS to all district councils under the Local Government Reform Programme by end of 2002/03 fiscal year.
- 1.12 The government has invited bids for the lease of Dar es Salaam Water Supply and Sewerage Authority (DAWASA) and has evaluated bids arising there from.
- 1.13 The Government has adopted the new Agriculture Sector Development Strategy and the Rural Development Strategy including the implementation plans for each strategy respectively
- 1.14 The Government has prepared the Terms of reference (T.O.R) for conducting a study or studies on the functioning of the labour market.
- 1.15 Public Service Legislation has been enacted.
- 1.16 The Government has commenced the implementation of a project plan to expand the operations of the Commercial Court to the regions, and to computerize the case filing and registry system in the High Court.

ANNEX III

Rating of SAL II Programme

PROGRAMME IMPLEMENTATION PERFORMANCE, MAINLY Govt. of Tanzania		
Component indicators	Score	Remarks (mapped from PCR with references in brackets)
1. Compliance on Time, Cost & Covenants		
a. Adherence to Time Schedule	1	Substantial slippages accumulated from the beginning, extending completion by about 23 months. The GOT alone can not be blamed as the text explains (3.1)
b. Adherence to Cost Schedule	3	Loan amounts were adhered to.
c. Compliance with covenants	1	There were delays and difficulties even with conditions for the First Tranche (3.1 and 3.2)
d. Reporting	2	Two Reports were submitted(3.4).
e. Adequacy of Monitoring and Evaluation and Reporting	2	No interim reports were seen, but the PCR was submitted(3.6)
2. Procurement Performance		
a. Procurement of Consultancy Services	2	There were no direct and identifiable procurements from the budget support. (3.4)
b. Procurement of Goods and Works	2	There were no direct and identifiable procurements from the budget support. (3.4)
3. Financial Performance		
a. Availability of foreign exchange	2	The loan was critical for public debt positioning in the progress to HIPC completion. The loan availed resources that Tanzania applied to public finances. However, the 1 st Tranche came too late, forcing the GOT to undertake an accounting solution at BOT(3.7).
b. Availability of local currency	2	Counterpart funds are a problem in Tanzania. Unrealistically, GOT had to supplement SAL II at the beginning; (3.1)
c. Disbursement flows	1.5	Disbursements were problematic from the start because of onerous conditions; (3.7)
d. Cost management	2	No serious 'accounting' cost overruns for the Bank loan. However, the GOT had to supplement a financing gap initially (3.1)
4. Activities and Works		
a. Performance of Consultants and Technical Assistants	2	There were no direct and identifiable procurements from the budget support. (3.4)
b. Performance of Project Management	2	The Ministry of Finance performed well but seems overstretched (3.6)
TOTAL	24.5	
OVERALL ASSESSMENT OF IMPLEMENTATION		
	1.88	
BANK PERFORMANCE		
Component indicators	Score	Remarks
a. Appraisal	1.5	In policy focus the appraisal and components were appropriate. The conditions of the loan turned unrealistic and they faced issues of the calendar of parliament. (4)
b. Supervision	2	The programme was supervised twice but missions should have applied expertise on structural impediments (3.1; 3.3; 3.6)
c. Mid-term review	-	The MTR was not traced in activities, (3.1)
TOTAL	3.5	
OVERALL ASSESSMENT OF BANK PERFORMANCE		
	1.75	
PROJECT OUTCOME		
Component indicators	Score	Remarks
1. Relevance and Achievement of Objectives		
a. Macroeconomic Policy	3	The SAL II focused and sensitised the authorities to an awareness of public finance questions that are critical to Tanzania's medium-term macroeconomic stability, (4.2).
b. Sector policy	2	The SAL II assisted in Tanzania's historic progress to HIPC/MDRI (2.1). Despite robust growth and good macro-policy outcomes, sector outcomes are marginal. Economic diversification and livelihoods remain weak(5.1).
c. Financial cost	3	Outcomes came at modest cost to Bank Group (Table 1 and 2.1)
d. Poverty alleviation, Socio-econ, Gender	2	The outcomes are positive for poverty reduction, but not sufficiently so.

e. Environment	2	The environment will benefit from diverse outcomes (5.2)
f. Private sector development	2	The cost of doing business is still high but could go down after policy measures of SAL II
2. Institutional Development		
a. Institutional framework including restructuring	2	These factors are strengthened by development in SAL II.
b. Financial and Management Information Systems	3	This will improve in medium term, especially in budgeting (4.1) The IFMIS was working adequately in public accounts. (4.2)
c. Program Audit	2	Auditing was not traced but the GOT issued two reports on SAL II. .
3. Sustainability		
a. Outputs	3	Sustainable (6.1)
b. Inputs	3	Donors seem satisfied, but donor dependence will continue(6.2)
TOTAL	27	
OVERALL ASSESSMENT OF PROGRAMME OUTCOMES	2.45	
OVERALL PROGRAMME ASSESSMENT	2.04	
Legend:		
3 = Highly satisfactory; 2 = Satisfactory. Occasional problems, Bank should monitor; 1 = Unsatisfactory. Problems. Bank should monitor closely, but no immediate action is required; 0 = Highly unsatisfactory. Serious problems. Action required.		

Source: Consultant's ratings