Analysis of Budget Sustainability in Tanzania

Joel S. Kaswalalah and Remidius Ruhinduka

Research Report 2022/15

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Author: Joel S. Kaswalalah and Remidius Ruhinduka
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1. INTRODUCTION

1.1. Background

Tanzania Development Vision 2025 instigates the transformation of the socio-economic environment so as achieve the inspiration of making Tanzania a middle-income country by 2025. Attainment of this vision and inspirations relies much on the capacity of financing different development projects to enhance attainment of national development goals and objectives. Related to financing, in Tanzania, the main challenges have been on availability of funds or underfunding; delay in/untimely disbursement and unpredictability in budget execution. One of the possible sources of finance in presence of such constraints is the private sector, which can serve as a remedy that will ensure sustainability of projects' funding. The fundamental question in this regard is "How can the private sector be engaged more actively and effectively in Financing Public Projects?"

Furthermore, changing the nation's socio-economic course certainly requires a dramatic adjustment in the level and mix of government spending and/or higher revenues. This relies much on two key dimensions: solvency, growth, stability, and fairness. The first dimension, solvency, refers to the ability of a public-sector entity to satisfy its financial obligations. It should be noted that solvency has been an issue in Tanzania due to high levels of debt to finance Government expenditures. This has been attributed to many factors including the recent shocks i.e., the 2008 global financial crisis and the COVID-19 crisis.

The second dimension, growth, refers to a fiscal policy that aims at sustaining economic growth. Generally, to sustain growth, Government should avoid budget imbalances while maintaining debt below a specific level. In certain contexts, specific levels are defined by international organizations, and central governments are expected to comply with them. For example, in the European Union (EU) context, budget imbalances of member countries should be below 3 percent of the GDP, and gross debt should be below 60 percent. The basic idea supporting the growth dimension is that improving the economic condition of a country will guarantee higher tax revenues in the future because citizens and businesses will pay higher taxes on increased private income. This could pave the way for future budgetary manoeuvrers geared toward cutting taxes and/or increasing public investments to improve the well-being of future generations.

From Tanzanian context, the Government budget was in poor shape in the early 1990s. At the time, the efficiency of collecting internal revenue was very low and relations with development partners were not good. The government had no confidence in donors and likewise on the part of donors. However, the Government made significant and difficult decisions to implement major economic and structural reforms pertaining to the revenue, expenditure, structures and responsibilities of the State as well as its institutions. Furthermore, based on the recommendations of an independent expert group (The Helleiner Report), the Government succeeded in restoring good relations with development partners as well as putting in place an effective dialogue framework. During the ten years beginning in 1996, the Government implemented a number of reform proposals in the fields of revenue, expenditure, and structures under special agreements with the International Monetary Fund (IMF) which are anticipated to have improved government budget, increased revenue collection, provision of social services and economic growth.

Despite the previous efforts that were undertaken, there hardly has been a dedicated and robust study exploring the dynamics and extent of budget sustainability from the Tanzanian context. While there are different definitions of budget sustainability, Slack and Bird (2004) define fiscal sustainability as the ability of a government. It should be noted that the Government budget is a vital tool for the implementation of Government policy objectives. Also, the budget is a tool for assessing and evaluating Government performance in delivering different socio-economic services to the citizens. Over the past decade, budget analysis has indicated that the implementation of the Government budget was not satisfactory and some of the budget objectives were not achieved. Based on these findings, this study undertakes an analysis of budget sustainability so as to address challenges that impede the achievement of Government budget objectives.

1.2. Objectives of study

The overall objective is to undertake an analysis of budget sustainability in Tanzania.

Specifically, the study seeks to:

i. Analyse the extent and dynamics of Government revenues and expenditure for the last 10 years
ii. Examine the impact of global shocks (for example COVID-19 and Russia – Ukraine war) on Government revenues and expenditure
iii. Track the participation of the private sector in financing development projects
iv. Identify challenges that impede the implementation of the Government budget

v. Come out with specific and workable recommendations to address the challenges identified.

1.3. Scope and Approach of the Study

The scope of this assignment is to undertake an assessment and analysis of the Government budget and its implementation and come out with key challenges and best workable recommendations for addressing the challenges identified. The study mainly focuses on a period of the last ten years up to the financial year 2020/2021. We believe that such periodization will provide most updated theoretical and practical understanding related to the two instruments in line with recent the implementation of Global and Regional Development agendas.

2. METHODOLOGY

2.1. Data

The study largely relies on the secondary time series data on both the government revenues, borrowings and expenditures for the past 10 financial years' period. Regarding budgetary statistics, the study assesses both the estimated and actual budgetary values to also shed some light on the magnitude of variations between the two. To address the third objective of the study, data on government borrowings by sources is collected and analysed. This allows us to estimate the proportion of government borrowing that comes from domestic private sector to provide insight on their extent of participation.

In addition to the existing secondary data, the research team undertook a few consultations with key stakeholders in fiscal sustainability with the aim of getting clarity on some critical aspects of the practicability of sustainable budgeting, including getting qualitative answers on key mechanism influencing the current state of affairs in the country.

As the approach to the study, extensive review of literature and reports is conducted. The focus is to document conceptual issues of budget sustainability, the applicability in practice, challenges and recommendations for addressing the identified challenges. The review also generates some secondary data useful for analysis in the study. Thus, both quantitative and qualitative data generated are used to achieve the stated specific objectives.

2.2. Empirical Strategies

The study is designed to shed light on the extent and dynamics of budget sustainability in the country. To this end, both qualitative and quantitative analytical methods are used. Qualitatively, the study assesses budgetary trends of the key components (i.e. revenues, borrowings and expenditure) using relevant charts, graphs and tables. This allows us to underscore the pattern of budget deficit over time (whether expanding or narrowing) as well as dynamics of key indicators of budget sustainability.

Quantitatively, we estimate and assess various indicators of budget sustainability as recommended in the literature. When we look at the literature that examines budget deficits or, in a broader sense, fiscal sustainability, we see that sustainability is examined with a number of sustainability approaches such as the accounting approach, the intertemporal budget constraint approach and the Bohn approach (see for example Ergen and Güzhan, 2022; Telatar et al, 2004; and Kia, 2008).

This study empirically estimates the sustainability of the Tanzanian budget for the period from 2010/11 to year 2021/22 by taking the model in the studies of Hakkio and Rush (1991) and thereafter adopted in Ergen and Güzhan (2022). The basic model to be analysed is determined as in Equation:

$$lnR_t = \alpha + lnG_t + \varepsilon_t$$

Where $lnR_t$and lnG_t are natural logarithm of public revenues and expenditures (including interest payments), respectively. This model allows us to estimate the cointegration between the two variables as the basis of building a case for or against budgetary sustainability in the country. To investigate the cointegration relationship between lnR and lnG variables, the stationarity of the series of two variables is first examined since the variables must be stationary at the same order; the long-term equilibrium relationship between the two series by ensuring the same degree of stationarity of the series was analysed using the cointegration test.

3. LITERATURE REVIEW

3.1. Budget Sustainability

A sustainable budget can be recognized as having the primary characteristics of enabling the Government to meet basic expenditure without compromising the basic indicators of macroeconomic stability. The Government budget is constantly flexible based on economic, political and social needs hence the need to update and evaluate it regularly to ensure that it is sustainable in the short term and long term.

3.2. Mechanisms for Preparing Government Budget

Preparation of Government budget commences with preparation of a Guideline for Budget Plan that provides preliminary budget directives and estimations for three subsequent years. The Guideline involves a committee comprising several ministries (Interministerial Committee) under the supervision of Ministry of Finance. However, the reality indicates that there is a misleading perception that the responsibility of assessing sources of funds rests with Ministry of Finance alone and that it is not a responsibility of the Ministry of Finance and any other Departments and Regions. It is important that this perception be changed to recover discipline in preparing realistic and implementable budget. Moreover, as recommended in the Helleiner Report[1], there is a need for taking immediate measures to strengthen the authority of the Ministry of Finance and Planning to enable it to prepare a realistic budget; to make realistic income estimations; to devise a strong financial control to Accounting Officers and to strengthen supervision of Government Expenditure.

Generally, experience shows that there is much insistence on subsequent annual financial budget because of challenges in attaining right information about estimations of annual income and demands for the two previous years and unforeseen changes of statistics and different indicators. Together with this Guideline, the government also prepares Annual Development Plan that identifies priorities to be considered in the subsequent financial year. Once this information is endorsed by the government and later passed by Parliament, it is passed on to the Ministry, Private Departments, Agents, Regional Secretariats, Local Government

[1] The Hellainer Report of a Group of Independent Advisors; June 1995.

Authorities, Public Institutions and Organizations as an important tool to guide them in preparing budget in their respective areas. Some of the things to consider are envisaged sources of income, limitation to expenditure budget and strategic priorities.

A major challenge that emerges all the time is presence large numbers of priorities and high implementation costs relative to actual income from all internal and external sources. Moreover, experience shows that negotiation during the budgeting process provides more opportunity to discuss expenditure than strategies to increase income. Normally, allocation of financial resources considers several things such as compulsory requirements (such as salary, and settling of government debt), needs with special sources of income, continuing projects, ring-fenced expenditure and money for running office. However, allocation of financial resources should consider realistic availability of income in order to have implementable and sustainable budget.

3.3. Review of Budget Implementation

Government implements budget with the aim of implementing policies, strategies and goals of improving economy, reducing poverty and other issues as outlined in the National Development Vision, the Directive Development Programme and the Five-Year Development Plans. The trend of the recent years' implementation of Government budget shows results below target, a situation that has caused ordinary expenditure, especially development expenditure, to fail to achieve objectives in planned time, thereby weakening service delivery, causing accumulation of internal debt and increasing project costs. For instance, during the ten financial years (2007/08 - 2016/17)[2] expenditure from budget has produced less than expected results at the rate of 12per cent while ordinary expenditure has fallen below projections at the rate of 4per cent and development expenditure has fallen below projection at the rate of 23.7per cent. The Breakdown of development budget expenditure indicates that, although the government has had agreements with donors to contribute to development budget, some donors have failed to fully implement the agreements, thereby affecting implementation of development projects.

[2] Budget estimate figures are based on Government Speeches on Revenue and Expenditure Estimates for relevant years.

3.5. Private Sector Involvement- Context

Traditionally, financing of public projects including mega infrastructure projects has been using public fund given the typical nature of the public goods (OECD, 2014)[3]. This has been a Global practice. Given ever increase in public deficits, increased public debt to GDP ratios, and in some cases inability of the Governments to deliver efficient investment and misallocation of resources contributed by political interference has led to reduced commitment of public sector resources on financing such projects. Private sector has become a focus in financing such investments through various arrangements including those under the PPP such as "project finance" approach.

In theory but also in practice, financing of public projects using private sources of fund has been in a number of forms including through private sector engagement in providing loans and purchasing bonds, through investing in public utility infrastructure and projects in general, which in most cases prove to have financial return to the private investors. In such arrangements, government could provide concession agreement to private entity to construct public infrastructure at some agreed arrangement that will ensure the entity observe some financial gains. Also, the use of Public Private Partnership (PPP) where the government and private entity enter a concession agreement for the private sector to construct infrastructure on behalf of the government (URT, 2016) is another common approach[4]. OECDP (2014) suggests that PPP can take at least two forms, differentiated by the public sector role in financing the project. The first form is "institutional PPP" where public sector becomes the equity partner. The second form is "contractual PPP" where public sector plays planning and regulatory role. Given the dynamism of the private sector and public projects, application of either of the two PPP form is context specific and can further be broken down into various types of PPP.

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[3] https://www.oecd.org/daf/fin/private-pensions/Private-financing-and-government-support-to-promote-LTI-in-infrastructure.pdf

[4] Build, Operate, and Transfer (BOT); Build, Own, Operate, and Transfer (BOOT); and Build, Operate and Own (BOO) are commonly used types of concessions.

4. DATA ANALYSIS AND FINDINGS

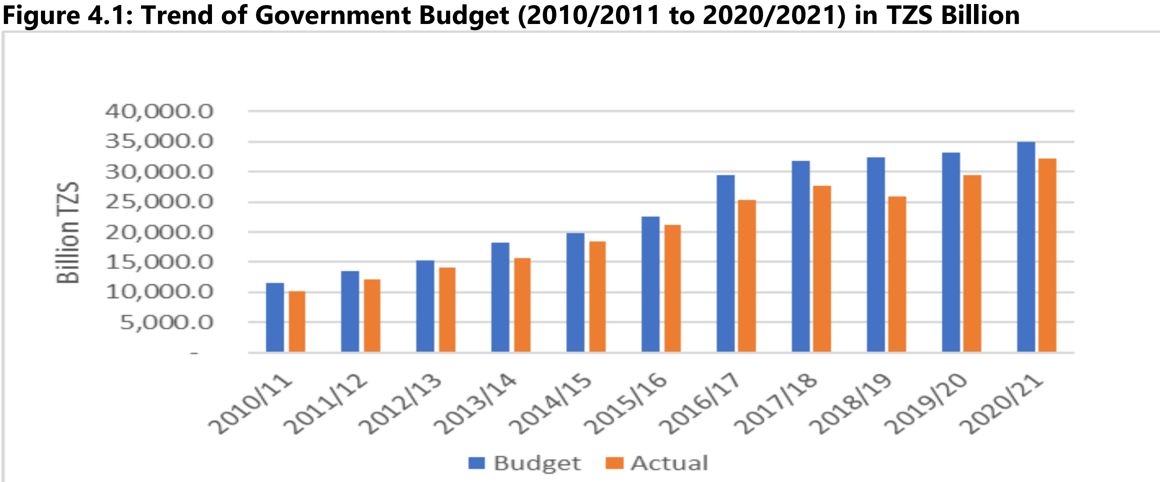
4.1. Analysis of Government Revenues and Government Expenditure

4.1.1. Government Revenues

Tanzania has over the past five years continued to register robust economic growth coupled with a stable macroeconomic environment that it has been enjoying since the turn of the century. GDP figures based on rebased national accounts estimates (using 2015 as the base year instead of 2007) indicate that the annual GDP in mainland Tanzania has been growing at an average rate of 6.9 percent from 2014 to 2019. Even though this growth trend is one of the highest among developing economies, it remains below the national target growth rate of about 8–10 percent per annum. Growth has been mainly from mining and metals (17.7 percent); construction (14.3 percent); creative and entertainment industry (11.2 percent); transportation and storage (8.7 percent) and agriculture (26.6 percent).

Similarly, from 2010/11 to 2020/2021 the government budget has increased from TZS 11,609.6 billion to TZS 34,879.9 billion and has grown by an average of 26 per cent per annum. Internal revenue collection has increased from TZS 5,736.27 billion in 2010/2011 to TZS 20,594.74 billion in 2020/2021(Figure 4.2). Growth in domestic revenue collections has averaged 22.1 per cent year-on-year. Thus, the pace of domestic revenue collection growth has been below the pace of budget growth by approximately 4 per cent per year. Meanwhile, budgetary dependence on foreign aid has decreased from an average of 37.7 per cent in 2007/08 to an average of 9.0 per cent in 2016/17. Despite the increase in domestic revenue, the collections were unable to meet expenditure demand due to high demand as well as decreased aid funds and cheap loans from Development Partners.

Figure 4.1: Trend of Government Budget (2010/2011 to 2020/2021) in TZS Billion

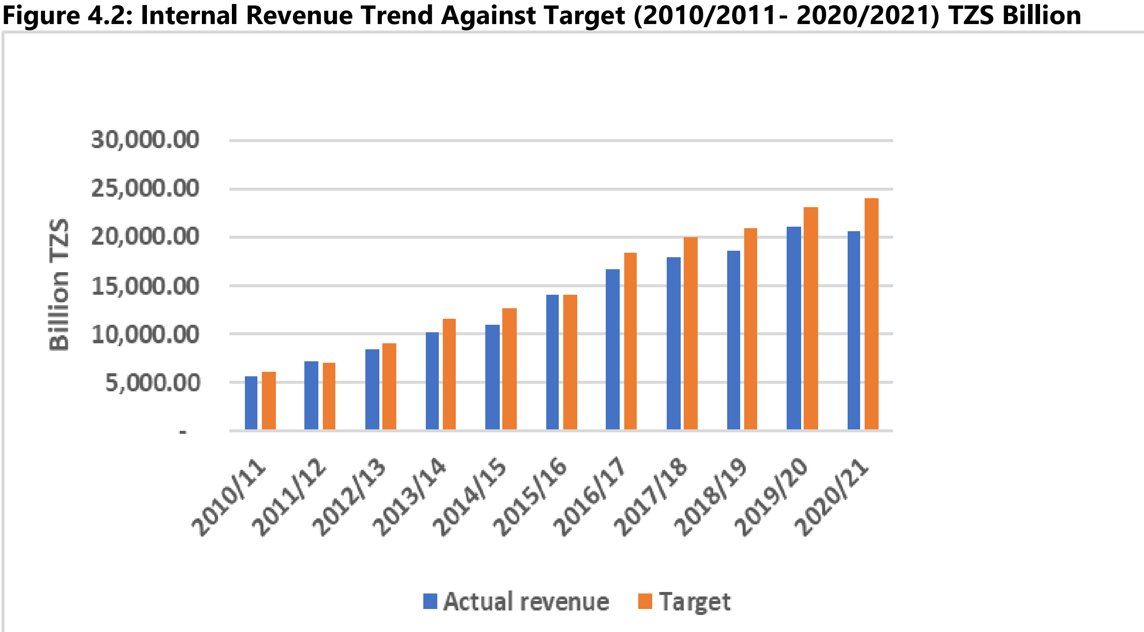


Source: Ministry of Finance and Planning

Internal revenue comprising taxes, non-tax revenues and council revenues are the main and reliable source of funds to finance the Government budget. This source alone covers an average of 60 per cent of the total annual budget. The remaining amount is financed with domestic and foreign commercial loans as well as grants and cheap loans from Development Partners. Due to the size and uncertainty of internal revenue, the Government has been making various efforts to strengthen this source including updating tax policies, strengthening tax administration, improving payment systems especially the use of electronic systems, controlling tax evasion loopholes, abolishing tax exemptions, and improving the business and investment climate.

Overall, efforts to consolidate domestic revenues have achieved increased collections over the past decade. Despite this increase, there is still scope for increasing revenue because the ratio of gross domestic product to GDP was 15.6 per compared to an average of 16.5per cent for sub-Saharan Africa. In addition, there are other sources of income that are not efficient enough and if used (exploited) properly can increase revenue significantly. Some of those sources are resource harvesting licenses (minerals, gas, and forestry), royalties, hunting and tourism, and various collections of the Council. On the other hand, government expenditure has been moving faster than the increase in revenue. This has resulted in a significant portion of government spending, especially funds for development activities depending on donors and loans.

Figure 4.2: Internal Revenue Trend Against Target (2010/2011- 2020/2021) TZS Billion



Source: Ministry of Finance and Planning

However, comparing with targets set, domestic revenue collections have fallen below targets at an average rate of 5.6 per cent over the past decade. While tax revenues have been down at an average rate of 4.4 per cent during the same period, non-tax revenue has had down yields by an average of 12.2 per cent. Council revenue have been below targets by an average of 24.9 per cent. The internal revenue collection is generally below the capacity (potential). While the average gross domestic product for sub-Saharan Africa's low-income countries is 16.9 per cent of GDP, Tanzania's average gross domestic product is 14 per cent of GDP. The size of the informal sector as well as the agricultural sector which contributes approximately 30 per cent to the GDP is one of the reasons for the decline as these sectors do not have a significant direct contribution to taxation.

4.1.2. Tax exemptions

The Government has been granting tax exemptions for the purpose of strengthening social services and attracting investments that will help increase employment opportunities in the country as well as government revenue. The whole concept of exemptions is that the Government is depriving itself of its due revenue today so that tomorrow it can collect more and more reliable revenue from the investments that will be made in the exempt sectors or see that the exempt social service sectors are improved and provide quality services to the community and at an affordable cost.

Despite the correctness of this assumption, there is an opinion that many of the exemptions granted have not yielded the expected success and many have been counterproductive. Furthermore, there are other suggestions that lowering tax rates or providing tax exemptions is not the only attraction to attract investment as emphasized by the private sector, but a key attraction is a conducive environment such as peace and political stability, better infrastructure, geographical position, low business operating costs (such as electricity), and predictable economic policies. Moreover, it is important to note that tax collections are what enable the construction of basic infrastructure for private sector investment. In 2013, the Government assessed tax exemptions through the Tanzania PER Tax Exemptions Study, 2013). The assessment report found that, of the 160 provisions of the Act that listed exemptions in various areas, approximately 50 per cent needed to be amended or repealed. Fifty-six per cent of the legislative provisions that needed to be repealed or amended were about Value Added Tax. Following this analysis, the Government took steps to enact the new Value Added Tax (VAT) Act that came into force in July 2015.

4.1.3. Government Expenditure

The government's expenditure budget is an important component in the slippage of fiscal policies that focus on public resource allocation and sustainable economic growth. Public expenditure policies are aimed at strengthening the control and management of public finances through the implementation of the Budget Act No. 11 of 2015. To have a sustainable and reliable budget, expenditure must be commensurate with revenue from all relevant sources, both internal and external. The Government has established a payment system that monitor and control government expenditure to ensure that expenditures are carried out as authorised by the Parliament in the Annual Appropriation Act for the purpose of giving the Minister the power to disburse funds to the General Fund and transfer them to the relevant budgetary provisions as passed by Parliament.

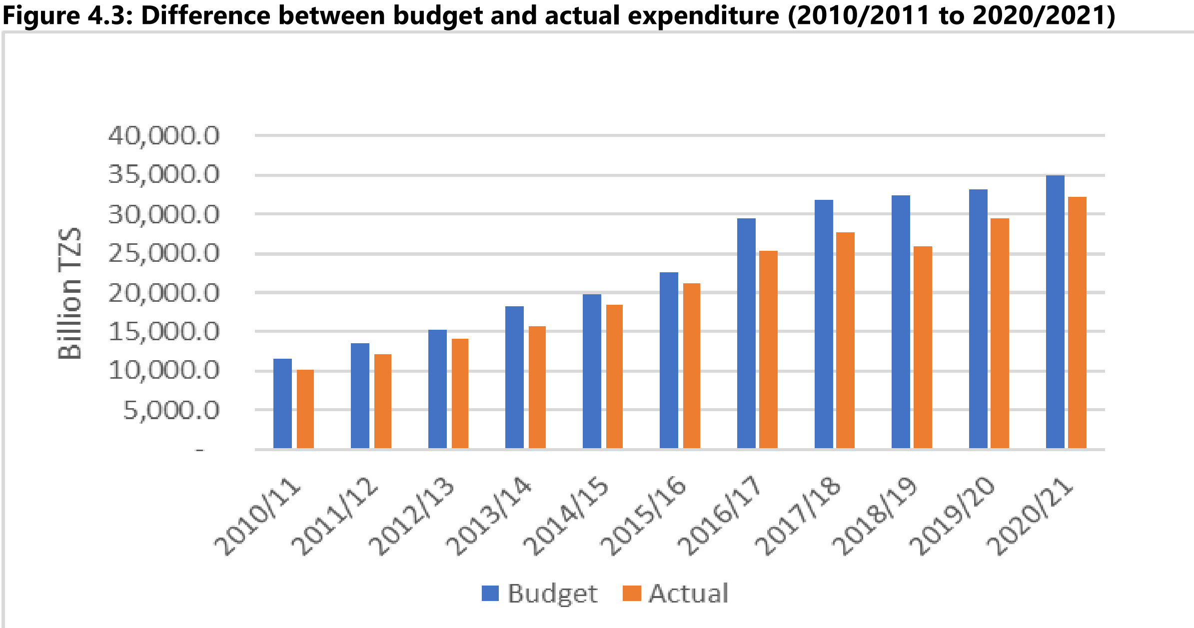
Government expenditure is divided into two areas namely:

a. Development expenditure budget, which covers various development projects.
b. The recurrent expenditure budget, which includes funds allocated to finance:
    i. Salaries for workers, annual salary increases, and promotions.
    ii. Treasury General Fund Services: Estimates of costs for National Debt (Capital and Interest), social fund contributions, backbones and pensioners' benefits.
    iii. Emergency Fund: Regulation 22 of the Budget Act 2015 provides for allocating one per cent of the Government's budget for the relevant financial year for the fund.
    iv. Protected Expenditure: Estimates of expenditure to finance the conduct of key government activities. Such expenditures include food allowance for soldiers, costs for conducting exams for primary and secondary schools, allowances and salaries for staff working in embassies, grants to political parties, Government contributions regionally and internationally, caveat costs to Government offices, dues of retired officials, practical training allowance, hospital pharmaceutical services, special medical allowances, prisoners' meals, and State allowance.
    v. Non-recurring expenditure: Estimates relevant to activities such as General Elections, Local Government Elections, population and housing census, etc.; and
    vi. Administrative Costs: Number of staff and officials, number of legislative sessions, caveat costs and fuel requirements as well as the cost of performing basic functions for Ministries, Autonomous Departments, and Institutions as specified in the structure.

During this 10-year period government expenditure has increased from 11.6 trillion Tanzanian Shillings in 2010/2011 to 34.9 trillion Tanzanian shillings in 2020/2021, equivalent to an average of 23 percent of the country's gross domestic product. During the same period, the recurrent expenditure budget has increased from 7.45 trillion shillings to 22.34 trillion shillings and the development budget has increased from 3.82 trillion shillings to 12.77 trillion shillings. Also, the pace of development budget growth is slow compared to the pace of recurrent expenditure budget growth. Its interpretation is that the Government is not investing enough in development projects due to either, budget shortfalls or increases in inevitable needs such as salaries, government debt payments and other protected expenditures.

Trends in budget implementation over the past 10 years indicate that actual expenditure did not meet the budget estimate target by an average of 12% (Figure 4.3). Moreover, actual expenditure averages 22 percent of GDP. The difference in budget and actual expenditure has been increasing further from the years 2010/2011 to 2020/2021 compared to actual expenditure. Looking at the trends in the implementation of the budget for this period, the availability of revenue has been inconsistent with the requirements for the implementation of the expenditure budget for the relevant year. The flow of revenue to the General Fund of the State does not correspond to the flow of cash requirements to implement the budget for the relevant period. The continued failure to achieve the target of expenditure estimates affects the sustainable management and implementation system of the budget, especially in the implementation of development projects. Despite the presence of the Budget Act No. 11 of 2015 which prohibits expenditure outside the budget, there have been new projects that are being implemented that were not approved in the budget for the relevant year (off budget expenditure) or the approved budget was less than the actual requirements.

Figure 4.3: Difference between budget and actual expenditure (2010/2011 to 2020/2021)

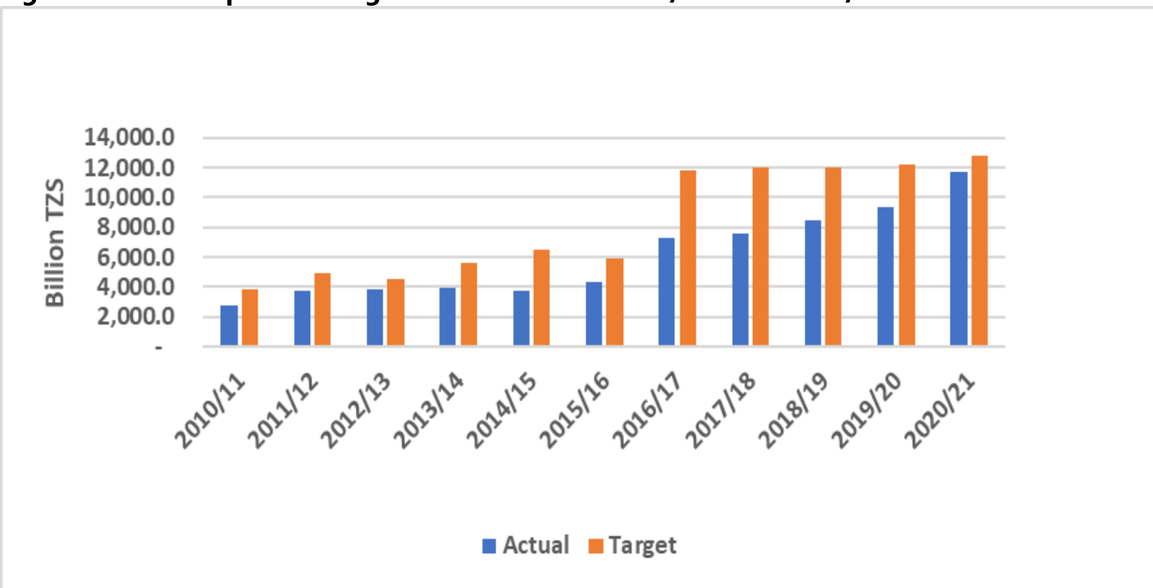


Source: Ministry of Finance and Planning

Over the same period, the cost of paying interest on domestic debt has increased from 3 percent to 5 percent of total expenditure, and funds deployed to implement development projects have been increasing. The government has started implementing major projects in domestic currency from 2 per cent in 2007/2008 to 6 per cent of GDP. Meanwhile, budgetary dependence on foreign funds has decreased from 5 percent to 2 percent of GDP.

The trend of development budget expenditure for the past ten Government financial years shows that the actual budget for the implementation of development projects was below the target set for the relevant period throughout the review period (2010/2011 – 2020/2021). Figure 4.4 shows the trend of the actual development budget and targeted development budget on the implementation of different projects.

Figure 4.4: Development Budget Trend between 2010/2011 to 2020/2021



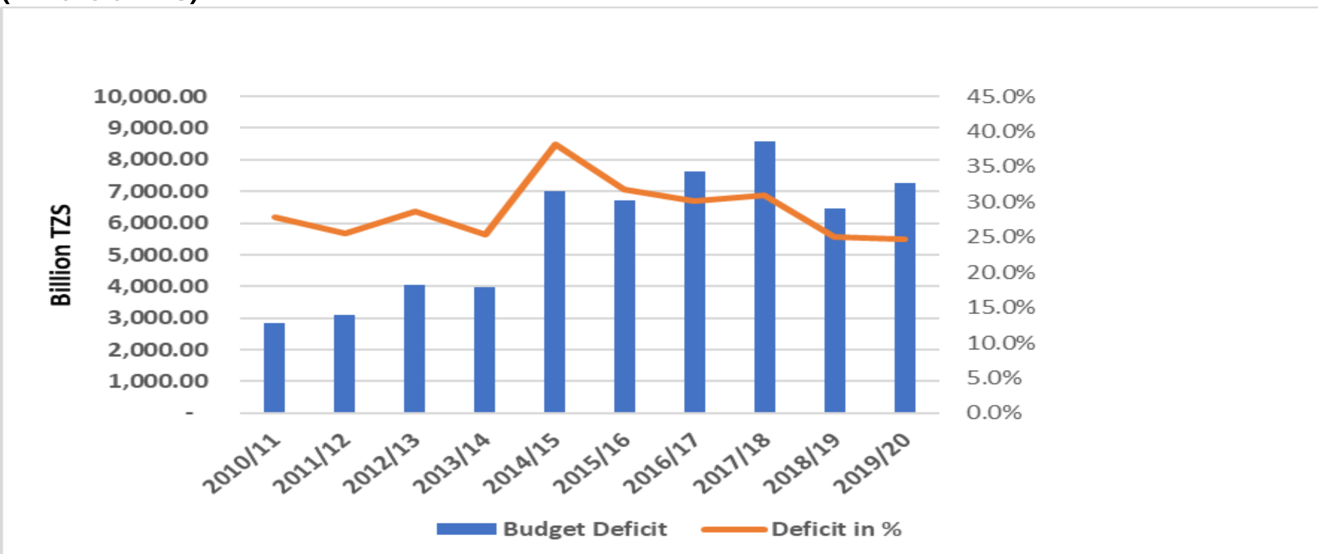
Source: Ministry of Finance and Planning

Furthermore, reviews on development budget trends using domestic or foreign funds shows that the implementation of development projects, especially flagship projects, will be difficult with the development budget of local funds. Model projects are usually large-scale projects that make a significant economic and social impact and benefit many citizens. To implement these projects more effectively, it is advisable that the Government through the Ministry of Finance and Planning set up a dedicated committee (dedicated team) that will oversee the projects from identification to completion. Similarly, the magnitude of these projects constitutes incompleteness during the scheduled period due to insufficient funds to carry out the projects.

4.1.4. Budget Deficit

The Government budget deficit during the years 2010/2011 to 2019/2020 has averaged of 28.8%. The trend shows that; Government budget deficit has decreased from 27.9 percent in 2010/2011 to 24.7 percent in 2019/2020. However, looking at actual amount of money, which is deficit, the amount is large and shows that implementation of development projects faces challenges due to lack of sufficient funds. After realising that the importance of the implementation of these projects and the resources needed are greater than the Government's capacity, the private sector in the Second Development Plan has been tasked with implementing the priority programmes.

Figure 4.5. The Trend of Government Budget Deficit between 2010/2011 to 2019/2020 (Billions of TZS)



Years	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Budget Deficit	2,844.47	3,110.16	4,064.58	3,964.94	7,017.49	6,699.72	7,635.17	8,584.68	6,475.46	7,265.89
Deficit in %	27.9%	25.5%	28.7%	25.3%	38.1%	31.7%	30.2%	31.0%	25.1%	24.7%

Source: Ministry of Finance and Planning, various reports

4.2. Impact of Global Shocks on Government Revenues and Government Expenditure

The section was aimed at analysing the impact of global shocks such as COVID -19 on Government revenues and Government expenditure. Given challenges in accessing monthly data on Government revenues and Government expenditure during the critical times of COVID-19 pandemic, i.e., 2019/2020 and 2020/2021 it became difficult to undertake rigorous analysis to see the impact and come out with relevant and substantive workable solutions to absorb such shocks. Therefore, to undertake this analysis needs accessible reliable data and time.

4.3. Participation of Private Sector in Financing Development Projects

In Tanzania, a common practice has been to relay on budgetary appropriation (development budget) to finance the so called "public projects". Nonetheless, the role of private sector in financing public projects is well recognized and can be clearly traced in the national policy and guidance documents including the National Five Year Development Plans (FYDP), National PPP Policy (2009), National PPP Act (2010), PPP Regulations (2011) and PPP Operational Guidelines (2010), the Public Investment Management Operational Manual (PIM-OM)[5] and the Budget Act, 2014. All these documents underscore the importance of including the private sector as an innovative way to finance public projects beyond the reliance of public sector and Official Development Allocations.

In implementing the FYDP I, around TZS. 8.9 trillion were required annually, out of which 67 percent was expected to come from the private sector and development partners (FYDPII). Attainment of financing targets for FYDP I proved some challenges as: there was no clear strategy to solicit fund; the efforts for PPP arrangements have not been successful; Dar es Salaam Stock Exchange (DSE) has been unreliable and insignificant source of investment capital since the market remains in infancy stages. For the FYDP II, it is estimated that 40 percent of annual budget will go to investment projects through Development Budget. A total of TZS 107 trillion is required as the implementation fund, which needs to be mobilized from both public and private sector sources as well as development partners during the FYDP II period. The Government is planning to contribute a total of TZS 59 trillion, translating to an average of TZS 11.8 trillion per annum over the Plan period. A need to increase private sector participation on some key resource-intensive infrastructure, productive and social services related proposed projects is emphasized in the FYDP II. Overall, the private sector is expected to contribute TZS 48 trillion, at TZS 9.8 trillion per annum with an increasing trend overtime. This is shown in Table 4.1 and figure 4.6 below[6].

Table 4.1: Expected Contribution of Private Sector in Financing Public Projects

SOURCE	2016/17	2017/18	2018/19	2019/20	2020/21	TOTAL

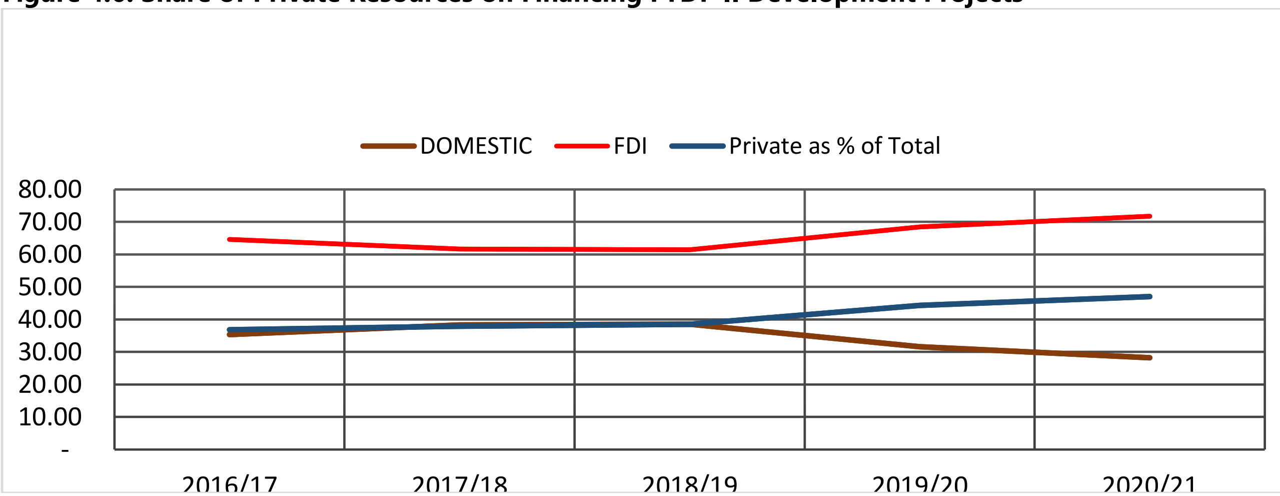
[5] This Public Investment Management Operational Manual (PIM-OM) provides guidance on methods and procedures involved in selecting, financing, implementation and evaluation of public investment projects in Tanzania including those executed by the private sector on behalf of the government.

[6] Of recent, both tax revenues and gross fixed capital formation (GFCF) by private sector have demonstrated potential to be dependable sources of development finance.

Domestic as (%) of Private Resources	35.36	38.32	38.56	31.58	28.23	33.63
FDI as (%) of Private Resources	64.64	61.68	61.44	68.42	71.77	66.37
Private Resources	6,893,449	7,437,934	7,910,217	10,331,249	11,973,182	44,546,031
Total Resources	18,709,290	19,614,887	20,555,790	23,319,300	25,453,577	107,652,844
Private as % of Total	36.85	37.92	38.48	44.30	47.04	41.38

Source: Author's construction using data obtained in FYDP II

Figure 4.6: Share of Private Resources on Financing FYDP II Development Projects



Source: Authors' construction using data obtained in FYDP II

In the case of PPP operations in Tanzania, a number of projects have been initiated under the arrangement. These include: Kinyerezi III Power Plant project; Dar es Salaam Bus Rapid Transit (BRT) Project-Phase 2; Power generation Project in Somanga Fingu Mkuranga; and the three pharmaceutical PPP Projects in which the feasibility studies have been finalized and the projects are under procurement stage. In terms of legal framework, the PPP Act and its regulations have been promulgated to create a clear understanding of the private sector in investing in public projects. Further, a Finance Unit (FU) has been created within MoFP with a role to assess, manage, and monitor fiscal risk, assess the affordability of projects, and appraise value for money from PPPs[7].

While various efforts have been undertaken to ensure private sector participation

[7] Tanzania – Assessment of the Public Finance Management systems of the Central Government applying the PEFA 2016 Framework).

in financing public projects as is highlighted above, there are still concerns as the engagement is very minimal. The potential of the private sector in terms of financing public projects is yet to be fully utilized. The current financing gap on public projects with existing reasonable capacity of the private sector to finance the same calls for attention. And a logical concern what should be done to private sector participation in public investment.

5. CHALLENGES WHICH IMPEDE IMPLEMENTATION OF GOVERNMENT BUDGET

5.1 Government Revenue

i. Cost and Environment of Taxation: There are views and perceptions of various stakeholders that the tax environment in the country is unfriendly due to three main reasons: First, these taxes and charges are excessive; Second, the tax rates (tax rates) and the charges are high; and third, there is a bureaucracy resulting from the demand for many procedures and measures that need to be done before paying the relevant taxes, thus wasting a lot of time pursuing paying the same kind of tax. For example, a hotel owner is required to pay at least nine taxes and charges to a different jurisdiction (hotel license, bar operating license, business license from local government, Food and Nutrition authority license, environmental council license, OSHA, Hotel Levy, SDL, VAT, and Social Security Funds), Etc.

ii. Analysis conducted in the Blueprint for Regulatory Reforms to Improve the Business Environment shows that there is a lot of inconvenience and time wasted on paying taxes/charges. There are taxes and charges of different types and rates levied by different jurisdictions for the same type of business. In addition, some of these authorities perform compatible functions (duplication and multiplicity) such as TBS and TFDA, EWURA and TCRA; TBS regulates quality standards in its entirety, but those other authorities regulate the same thing (quality) in the regulating sector only. This situation increases the cost of doing business differently for the same type of business.

iii. Large Informal business sector, where majority does not pay taxes as their records are not captured

iv. Tax evasion in mining sector

5.2. Government Expenditure

The following are some of the challenges affecting the preparation, implementation and monitoring of government expenditure:

i. Presence of unreliable budget year estimates and medium-term projections (MTEF projections): In recent years there has been an increase in the expenditure budget inconsistent with real revenue from various domestic and foreign sources and thus the implementation of the MTEF has deteriorated. Annual estimates tend not to be widely trusted and thus an annual budget is usually prepared from the first stage rather than developing it in the previous Central Plan.

ii. Expenditure for financing national debt payments and salaries accounts for approximately three-quarters of total recurrent expenditure and gross domestic revenue has led to the government retaining a very small amount (less than 25%) for other recurrent and development expenditures. In addition, protected expenditure takes up a significant portion of the budget, thereby reducing the ability of officials to direct plans and budgets to priority areas and ultimately undermining their participation in budget preparation. This situation is not sustainable because it significantly affects the demand for priorities in service delivery, government operations and development projects.

iii. The absence of a reliable revenue stream has affected the implementation of the expenditure budget.

iv. Although the national debt is stable by all international criteria's, the payment of the national debt is a huge burden on the Government budget.

6. CONCLUSION AND RECOMMENDATIONS

6.1. Conclusion

Budget trends in recent years show indications that the current trend may not be sustainable. For example, as noted earlier, revenue from all sources does not meet targets, and the same goes for consumption. In addition, during the past five years' government expenditure on salaries and government debt consumed an average of 75 percent of total gross domestic. It is correct that government debt is stable in all criteria's for measuring international debt resilience but based on the available figures, it is evident that expenditure on debt payments from a short-term perspective is a significant burden on the Government's budget and measures are needed to reduce that burden. Therefore, this area needs to be looked at in detail to have a more effective strategy to ensure that the share of the remaining internal revenues after providing government debt expenditure and salaries increases to provide opportunities for these revenues to finance other activities, especially the development budget.

6.2. Recommendations

6.2.1. Government Revenue

Increasing the tax base: In increasing the tax base (in the sense of new sources of revenue), there are two main areas of focus namely institutionalizing the informal sector and improving the investment climate to find new sources of revenue from such investments.

Strengthening the management of existing sources and endorsing other policy and administrative measures.

> **Informal sector**: This is a large group and thus has the potential to increase government revenue significantly if incorporated into the formal system. There are formalization measures that have begun, such as the valuation of buildings, and the assessment of plots through the MKURABITA project. However, there is a need to accelerate formalization, including innovative, friendly, participatory and strategic approaches. The government should focus on strategies to improve the business environment, including measuring and issuing residential/plot title deeds, valuing buildings - especially in urban areas, and allocating specific business areas in each Council.
>
> The Government should speed up the assessment and issuance of title

deeds for residences/plots, and farms and value buildings – especially in cities, and allocate specific business areas.

Local governments should be encouraged to identify and register all persons in their areas with unformalised properties and businesses so that they can be involved in the formalisation programme.

6.2.2. Government Expenditure

i. Have a strategy to improve planning and budget for the year by having a realistic and reliable budget and finally having a planning and budget process based on the medium-term expenditure framework (improving the integration of the medium-term expenditure framework into the annual budget process).
ii. MTEF is required to set priorities and estimates of its costs over three-year periods for regular and development activities (whether funded by the Government or Donors) based on the performance indicators set out in the strategic plans of all Government Ministries, Departments and Agencies.
iii. Restore budgetary discipline by fully implementing the Budget Act No.11 of 2015 and its regulations.
iv. The Ministry should take into account the legal powers it has in controlling Accounting officers in violation of existing procedures, laws and guidelines regarding the use of public funds.
v. The government should take concrete steps to control the pace of expenditure growth so that it is in line with the reality of revenue generation.

6.2.3. Private sector involvement in financing Public Projects

i. Improve the Business Environment through undertaking necessary reforms: The business environment needs to be reliable, secure and predictable for the private sector to profitably operate, sustain and flourish. Clear and Stable regulations, efficient procurement procedures, certainty in timing are fundamental conditions that attract private sector investors are essential for effective participation of the private sector.
ii. Improve the Technical Capacity of the Public Sector Officials about PPP Management: It is essential for public sector personnel to have a good understanding of the PPP arrangements and their applicability under different project types. Without that capacity it becomes difficult to convince the potential private sector actors to invest in public projects. Also, aspect of stakeholder's management is vital for successful PPP implementation.

iii. Enhance the Capacity and Utilize Domestic Development Finance Institutions: One of the solutions is to start using domestic Development Finance Institutions (DFIs) i.e. TIB and TADB to leverage government revenues and to facilitate access to other sources of finance. The viability of establishing other DFIs particularly for Construction and SMEs sectors should be explored (FYDP III).
iv. Improve the Legal Framework of PPP Arrangements: The finances from the private sector are lower than the expectation partly because of the challenges related to weakness in the PPP legal framework, unsolved land issues and inadequate understanding and operationalization of PPP concepts.
v. Forge a clear consensus and vision between the Government and private sector: In some countries, the public and private sectors forged consensuses around policies as well as the strategic direction of the economy and the attendant transformation path, which helped to build mutual trust and solid effective platforms for engagement (FYDP III).
vi. Establish mechanism to reduce investment risk faced by private sector: Allocation of project risks equitably among all parties involved in the transaction. Here risks are assigned to the contractual counterparts best able to control and manage them hence the willingness and appetite of the investor has to be considered. These include have in place appropriate types and level of guarantees required.

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REPOA HQs

157 Migombani/REPOA streets, Regent Estate, P.O. Box 33223,
Dar es Salaam, Tanzania.
Tel: +255 (22) 270 0083 Cell: +255 (0)784 555 655
Website: https://www.repoa.or.tz
Email: repoa@repoa.or.tz

Branch Office

2nd Floor Kilimo Kwanza Building
41105 Makole East, Kisasa,
Dodoma, Tanzania