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Tanzania Financial Sector Adjustment Programme Project Completion Report

African Development Fund

AFRICAN DEVELOPMENT FUND

TANZANIA

FINANCIAL SECTOR ADJUSTMENT PROGRAMME

PROJECT COMPLETION REPORT

COUNTRY DEPARTMENT	**OCDE**
EAST REGION	**AUGUST 2000**

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ACCRONYMS AND ABBREVIATIONS

ADF	:	African Development Fund
BOT	:	Bank of Tanzania
CRDB	:	Cooperatives and Rural Development Bank
DANIDA	:	Danish International Development Agency
ERP	:	Economic Recovery Programme
FIDP	:	Financial Institutions Development Project
FSAL	:	Financial Sector Adjustment Loan
FSAC	:	Financial Sector Adjustment Credit
FSAP	:	Financial Sector Adjustment Programme
GDP	:	Gross Domestic Product
GOT	:	Government of Tanzania
IFEM	:	Inter-Bank Foreign Exchange Market
IRTAL	:	Industrial Rehabilitation and Trade Adjustment Loan
LART	:	Loans & Advances Recovery Trust
MOF	:	Ministry of Finance
NBC	:	National Bank of Commerce
OGL	:	Open General Licence
PCR	:	Project Completion Report
PBZ	:	Peoples Bank of Zanzibar
PFP	:	Policy Framework Paper
SPA-JEM	:	Special Program of Assistance-Joint Evaluation Mission
UA	:	Unit of Account
TIB	:	Tanzania Investment Bank

BASIC PROGRAMME DATA

A THE BORROWER

1.	COUNTRY	:	Tanzania
2.	NAME OF PROGRAMME	:	Financial Sector Adjustment Loan
3	LOAN NUMBER	:	F/TAN/FSAP/92/30
4.	BORROWER AND BENEFICIARY	:	Government of Tanzania
5.	EXECUTING AGENCY	:	Bank of Tanzania
6.	LOAN ADMINISTRATION	:	Bank of Tanzania

B. THE LOAN

1.	DATE OF REQUEST FOR FINANCING	:	1991
2	LOAN AMOUNT	:	UA 27.63 million
3.	SOURCE	:	ADF
4.	LOAN INTEREST RATE	:	Nil –service charge-0.75%
5.	REPAYMENT PERIOD	:	50 years including grace period
6.	GRACE PERIOD	:	10 years
7.	LOAN NEGOTIATION DATE	:	23/04/92
8.	LOAN APPROVAL DATE	:	25/05/92
9.	LOAN SIGNATURE DATE	:	01/12/92
10.	DATE OF LOAN EFFECTIVENESS	:	16/06/93

C PROGRAMME DATA

1.	TOTAL FINANCING REQUIREMENTS	:	US $ 261 million
2.	FINANCING PLAN	:	ADF: UA 27.63 million IDA: SDR 150.20 million (US$ 200 Million) ODA: GBP 10.00 million Switz.: Swiss Franc. 10 million

		APPRAISAL	ACTUAL
3.	DEADLINE FOR FIRST DISBURSEMENT:	31/12/94	N/A
4.	EFFECTIVE DATE OF DISBURSEMENT:	N/A	23/07/93
5.	PROGRAMME COMPLETION DATE:	Sept, 1993	June, 1997
6.	DATE OF LAST DISBURSEMENT:	Aug, 1993	June, 1997

D. PERFORMANCE INDICATORS

1. TIME OVERRUNS

Slippage on Loan Effectiveness:	7 months
Number of Extensions of Last Disbursement:	3
Slippage on First Disbursement:	12 months
Slippage of Completion Date:	4 years

2. PROGRAMME IMPLEMENTATION

Institutional Performance	:	Unsatisfactory
Submission of Quarterly Reports	:	Unsatisfactory
Submission of Annual Audit Reports:		Improved later

3. DISBURSEMENT

Total Amount Disbursed	:	UA 27.46 million
Amount Cancelled	:	UA 0.174 million
Date of First Disbursement & Amount	:	23/07/93-UA9.21 million
Date of Second Disbursement & Amount	:	29/11/96 -UA 9.19 million
Date of third Disbursement & Amount	:.	04/06/97-UA 9.05 million

4.

MISSIONS	Duration	No. of Staff
Identification	N/a	N/a
Preparation	N/a	N/a
Appraisal	10 days (March, 1992)	3

Supervision	10 days (August, 1994)	1
Mid-Term Review	10 days (July, 1996)	2
Project Completion	10 days (Nov. 1998)	2

EXECUTIVE SUMMARY

1. This Project Completion Report (PCR) has reviewed the completion of implementation of the Financial Sector Adjustment Programme, which was supported by the ADF loan F/TAN/FSAP/92/30. The loan was approved on 25 May, 1992 and signed on 01 November, 1992. It became effective on 16 June, 1993. The loan was parallel financed with the World Bank's Financial Sector Adjustment Credit (FSAC), and was planned to be disbursed in three tranches. The first tranche was released on 23 July, 1993 and the last tranche on 04 June, 1997. The loan was closed on 30 June, 1997, and the Borrower's PCR submitted to the Bank in February, 1998. This PCR is based on the Staff Appraisal Report, information and documentation from the project file, the Borrower's own PCR, and additional information and insights obtained from the field.

2. The financial sector reform was introduced in 1991, and formed a major component of Tanzania's economic and financial programme supported by the IMF and other donors. The reforms were necessitated by the deterioration in the performance of the state controlled financial sector. The problems in the financial sector stemmed largely from excessive government interference in the management of financial institutions, which was manifested in directed credit policies and regulated interest rates. Credits were directed to inefficient parastatal enterprises, cooperative unions, and to Government itself. The effect of these policies was to crowd out private economic agents and impair the loan portfolio. A weak macro-economic environment characterized by large budgetary deficits, high inflation and an overvalued exchange rate reinforced the banking sector problems. By the time the financial sector reform was ushered in, most banks were burdened by non-performing assets, and their capital eroded. It was against this background that the Financial Sector Adjustment Programme (FSAP) was designed.

3. The objective of the FSAP was to develop a sound market-oriented and autonomous financial system that would be efficient in the mobilization and allocation of financial resources to support economic growth. The FSAL was intended to support the programme through the provision of quick disbursing balance of payment assistance to meet part of the estimated external financing requirements over the 1991/92-1993/94 period.

4. The implementation of the programme took nearly four years as against the planned period of eighteen months. The delays necessitated three extensions of the closing date of the loan. The slippage was caused by delay in the fulfillment of the conditions for the second and third tranche. The delay in fulfilling some of the conditions was mainly due to the Borrower's inability to provide the required documentation. The conditions were fairly straightforward, except for the condition relating to the liberalization of insurance as it required legislative changes, which took time to implement. The PCR has identified a number of shortcomings in implementation, among which were, weak reporting by the Borrower, and weak supervision by the Bank.

5. The programme has gone some way in achieving its objective. Its most significant achievement was creating the enabling policy, legal and regulatory framework for a sound and competitive financial sector. These reforms have enabled the entry of private banks into the financial sector, while strengthening bank supervision. There are, currently, seventeen private banks, in operation. Where the programme's success was limited was in bank restructuring. Bank restructuring proved more difficult than changes in banking laws and regulations, as it required substantial capacity building, and also involved staff retrenchment.

The PCR has concluded that despite these difficulties, the programme has laid the foundation for a modern and competitive financial sector. The Bank's contribution was beneficial to the country in terms of leveraging the reforms and providing the resources needed to sustain the reform process. The Bank still has a role to play in promoting the long-term development of the financial sector in Tanzania.

6. The PCR has drawn a number of key lessons that should inform the design of future policy based operations in Tanzania.They include the following:-

(a) The implementation of adjustment operations require close supervision and follow-up especially where there are many conditions and the programme is relatively complex as was the case with the FSAL. It is, therefore, important that future adjustment operations are supervised more frequently, and where practicable, joint missions with the Bretton Woods Institutions fielded. This also has the advantage of strengthening policy dialogue with the Government.

(b) The time frame for implementation of some policy actions was short, and the expectation of the programme's results, rather ambitious. The lesson here is that results of structural reforms, especially in countries in transition from a socialist to a market-oriented economic system, take time to be realized, and cannot be rushed through conditionalities. The short-term nature of quick disbursing loans, to address balance of payment constraints, needs to be reconciled with the longer-term effort required to lock-in Government's commitment to reform and ensure ownership.

(c) Where an adjustment programme is being co-financed or parallel financed lags in disbursement between donors should be minimized to the extent possible. This can only be realized through improved coordination at both the appraisal and implementation stage.

(d) Reporting by the Borrower was weak, which, in the absence of regular bank supervision missions, made it difficult for the Bank to follow-up closely the progress in the fulfillment of the loan conditions. The ultimate solution to this problem lies in strengthening the in-country capacity to coordinate and manage Bank programmes, and in improving coordination between the Ministry of Finance and the sectors implementing the respective reforms.

(e) Compliance with the reporting requirements was unsatisfactory and yet no action was taken by the Bank to enforce compliance. In future, the Bank needs to be stricter and systematic in enforcing the general conditions.

1. INTRODUCTION

1.1 The Government of Tanzania (GOT) embarked on major economic reforms in 1986 following the launching of the Economic Recovery Programme (ERP), which was supported by the international donor community. The ERP was aimed at restoring economic growth and price stability through the pursuit of market-oriented policies, improved macro-economic management and institutional reforms. The first phase of the reforms lasted until 1989, and at that point, it had become evident that the financial sector was in a state of crisis, and needed a major overhaul if economic recovery was to be sustained.

1.2 Recognizing the poor performance of the financial sector, the Government set up in 1988 a Presidential Commission of Enquiry (PCE) into the Monetary and Banking system to analyse the functioning, constraints and weaknesses of the banking system and develop a blueprint for sector reforms. The Commission completed its report in 1990 which formed the basis for the financial sector reforms.

1.3 In order to implement the financial sector reforms, the Government requested the World Bank, the ADB and other donors for financial and technical assistance. Thus, in November, 1991 the World Bank approved its Financial Sector Adjustment Credit (FSAC) of US Dollar 200 million. The FSAC was supplemented by contributions from two bilateral sources namely, the United Kingdom with British sterling Pounds 10 million and the Swiss Government with CHF 10 million. The ADF's Financial Sector Adjustment Loan (FSAL) of UA 27.63 million, was approved in July, 1992. Prior to the FSAL, the Bank had extended loans for two sector adjustment operations namely; the Multi-Sector Rehabilitation Loan (Transport and Agriculture) and the Industrial Rehabilitation and Trade Adjustment Loan (IRTAL), which were approved in 1987 and 1990 respectively.

1.4 The implementation of the FSAL took nearly four years, and the loan was closed on 30 June, 1997 after release of the third tranche. There remained a balance of UA 0.174 million which was cancelled on 18 March, 1998 upon the Government's request. The Borrower's Project Completion Report (PCR) was submitted to the Bank in February, 1998 which fielded a PCR preparation mission in November, 1998. The preparation of this PCR is based on the Staff Appraisal Report (SAR), information and documentation from the project file, the Borrower's own PCR and additional information obtained from the field. The PCR has taken long to finalize as some of the data was not provided until early 2000.

2. **ORIGIN OF THE PROGRAMME**

2.1 After the Arusha declaration of 1967 the state nationalized all the existing financial institutions, and by 1986 when the ERP was launched, Tanzania's financial system was among the most repressed in Sub-Sahara Africa. Government-owned financial institutions monopolized all segments of the financial sector ranging from commercial banking, housing finance, development finance and insurance. The National Bank of Commerce (NBC) was by far the largest banking institution, accounting for almost ninety percent of the assets in the banking system. The other major state-owned financial institutions comprised the Co-operatives and Rural Development Bank (CRDB), the Tanzania Investment Bank (TIB), the Peoples Bank of Zanzibar (PBZ), and the Tanzania Housing Bank. The structure of the financial sector, was, thus, highly segmented and narrow. Capital and money markets were not yet developed, with the market for Government securities limited to the National Insurance Corporation and the National Provident Fund.

2.2 Direct government interference in the operational policies and management of financial institutions was pervasive. Credits were directed to the Government and inefficient parastatals on highly preferential terms. The effect of directed credit policies was to crowd-out private economic agents, and severely impair the quality of the loan portfolio in the banking system as most parastatal borrowers were insolvent and largely dependent on government subsidies. Banks operated as quasi-fiscal agents of Government, with unlimited access to the re-discounting window of the Central Bank. The regulatory framework and prudential bank supervision were non-existent, which exarcebated the weaknesses in the banking system. The problems in the financial sector were in the early 1980s reinforced by the deteriorating macroeconomic environment characterized by large fiscal deficits, high inflation and an overvalued exchange rate. Real interest rates were negative, which hindered savings mobilization and undermined efficiency in resource allocation.

2.3 Inappropriate macro-economic policies, including trade restrictions, price controls and regulated interest rates had led to a sharp decline in economic growth from the late 1970s to the mid-1980s. Faced with an economic crisis, Tanzania adopted market-oriented reforms with the aim of improving performance of the real sector by strengthening the incentives regime. The reform process involved price and trade liberalization, exchange rate adjustment, and structural reforms in the agriculture and industrial sectors. Tight fiscal and monetary policies were also adopted to reduce the budget deficits and restrain credit growth. The economy responded positively to the initial reforms, with real annual GDP growth rate averaging 4.1 percent over the 1986-1990 period compared to 0.4 percent during the economic crisis period. Inflation which had reached 30 percent in 1985 was brought down to 20 percent. However, as the initial phase of the reforms was coming to an end the performance of the financial sector deteriorated, and most banks became insolvent. The Government recognized that unless the financial sector was restructured, Tanzania's long-term economic growth would be severely undermined.

2.4 It was against this background that the financial sector reform programme was initiated. The financial sector reforms constituted an important component of the overall economic and financial programme supported by the IMF under the Enhanced Structural Adjustment Facility programme for the 1991/92-1993/94 period.

<u>Programme Identification, Preparation, Appraisal and Approval</u>

2.5 In 1991, the Bank was requested by the Government to support the programme in collaboration with the World Bank. The programme was subsequently included in the Lending Programme for financing under ADF VI. There was no preparation mission undertaken for this programme, and from identification the Bank proceeded straight to appraisal. A three man appraisal mission was fielded in February, 1992. The FSAL was negotiated in April, 1992 and approved by the ADF Board on 25 May, 1992.

3. **PROGRAMME DESIGN**

3.1 Sector Goal

The overall sector goal was to promote higher economic growth under conditions of price stability.

3.2 Programme Objectives

The objective of the programme, supported by the World Bank, the ADF and other donors was to develop a market-oriented and autonomous financial system that would be efficient in the mobilization and allocation of financial resources to foster long-term economic growth.

3.3 Programme Components

The following were the components of the programme:-

(i) Consolidation of the Macro-economic Framework : A stable market-oriented macro-economic framework was recognized as necessary for the success of financial sector restructuring. The GOT, was in this regard, required to implement prudent monetary and fiscal policies, as spelt out in the Policy Framework Paper for the 1991/92-1993/94 period. The policy measures under this component included the imposition of credit restrictions to loss-making agricultural marketing boards and parastatals; the elimination of subsidies; the adoption of a flexible interest rate regime; and the introduction of indirect monetary policy instruments.[1]

(ii) Strengthening the financial infrastructure This component involved four key elements; the enactment of appropriate legislation to enable private participation in the financial sector; the strengthening of bank supervision; the introduction and enforcement of modern and transparent prudential banking rules and guidelines; and the creation of an institutional mechanism for recovery and disposal of non-performing banking assets.

(iii) Bank Restructuring: The existing banks were to undergo financial, operational and managerial restructuring within the framework of a liberalized financial system. This entailed among other actions, the cleaning-up of the balance sheets, the transfer of non-performing loans to the Loans and Advances Realization Trust (LART), the recapitalization of the insolvent banks, branch closures and staff rationalization.

(iv) Restructuring of the major bank clients: This component was intended to support the restructuring of the major clients of the banking system comprising commercial parastatals, cooperatives and agricultural marketing boards.

(v) Deepening of the Financial Sector : Under this component initial steps to develop money and capital markets were to be taken.

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[1] To avoid disruptions in the marketing of major export crops resulting from credit restrictions, it was agreed under the programme, to provide for interim financing of agriculture cooperatives in the budgets for 1991/92 and 1992/93.

The retrospective MPDE and the FSAL Policy Matrix are shown in Annexes I and II respectively.

3.4 Loan Description

The FSAL was intended to support the programme through the provision of quick disbursing balance of payment assistance to meet part of the estimated external financing gap over the 1991/92-1993/94 period. It was designed as a three tranche operation.

3.5 Evaluation of Programme Design

3.5.1 The programme was broad in scope, but with clearly defined objectives and components. Moreover, the linkages between financial sector reform and other key reforms in the economy were built-into the programme design. The linkage between financial sector restructuring, macro-economic stabilization and parastatal reforms was especially important so as to; (i) ensure a stable macro-economic environment within which financial institutions could operate and; (ii) create a strong client base for banks. The pre-reform conditions were such that the various components of the programmes needed to be implemented simultaneously. Overall, the programme was well conceived and designed given the prevailing situation in the financial sector. Where the programme design can be faulted is that performance indicators to measure the outcome of bank restructuring were not specified in both the FSAL and the FSAC.

3.5.2 There were, clearly, risks associated with the implementation of a programme of such complexity. These were identified at the design stage. One major risk was the limited technical and institutional capacity available in the country to effectively implement the financial sector reforms, particularly bank restructuring. To address the institutional development requirements of the programme, the IDA FSAC included a technical assistance component. A number of bilateral donors also agreed to provide technical assistance. Another risk was the uncertainty over the budgetary cost of financial sector restructuring. At the time of designing the programme the full extent of the non-recoverable loans in the banking system had not been ascertained because of the poor accounting systems.

4. PROGRAMME IMPLEMENTATION

Fulfillment of Loan Conditions

4.1 First Tranche Release : The conditions for first tranche release were as follows; (i) the opening of a Special Account for the FSAL ; (ii) an undertaking to pursue on a timely basis the implementation of measures contained in the PFP ; (iii) submission of a progress report on NBC's restructuring; (iv) submission to the Fund of a copy of the guidelines on capital adequacy ; and (v) submission to the Fund for review a statement indicating the amount of non-performing assets transferred from NBC and CRDB to LART, and the extent of loan loss provisioning for each institution. The aforementioned tranche release conditions were fully met in May, 1993.

4.2 Second Tranche Release : The conditions for second tranche release were ; (i) submission of satisfactory evidence that the Borrower had utilized the first tranche of the loan for the defined purpose; (ii) submission of satisfactory evidence of budgetary allocation for payment of interest on bonds issued by LART; (iii) submission to the Fund of the progress reports on the restructuring of CRDB, TIB and PBZ and; (iv) submission of a report on the status of negotiations and processing of applications for entry of new private local and foreign banks. At mid-term review in July, 1996 the Borrower had not yet submitted some of the documents required for the fulfillment of the second tranche release conditions. Two conditions remained outstanding namely ; (i) the submission of satisfactory evidence that the Borrower had utilized the first tranche of the loan for the defined purpose ; and (ii) evidence of budgetary allocation for payment of interest on the LART bonds. The above loan conditions were fulfilled only in August, 1996 due to delays in the submission of the required documentation.

4.3 Third Tranche Release The third tranche release conditions required the Borrower to submit; (i) evidence that it had utilized the second tranche for the defined purpose and achieved reasonable additional progress in the implementation of the policy matrix ; (ii) reports on financial deepening studies ; (iii) evidence of implementation of the Restructuring Action Plan for NBC, CRDB, TIB and PBZ ; and (iv) evidence of the legal framework and regulations put in place to introduce competition in the insurance business. Conditions ii) and iii) were fulfilled in August, 1996 and the rest of the conditions were satisfied in May, 1997 leading to the release of the third tranche in June, 1997.

Implementation

4.4 The Staff Appraisal Report (SAR) had projected that the FSAL would be fully disbursed over a period of 24 months from entry into force of the Loan Agreement. The first tranche was expected to be released in August, 1992, while the second tranche was planned to be disbursed in November, 1992 after the mid-term review mission. It was envisaged that the third tranche would be released in July/August 1993. However, as noted above, delays in the fulfillment of the tranche release conditions were encountered, resulting in a slippage of almost four years. The condition that took the longest time to fulfil was that relating to the liberalization of the insurance industry. The fulfillment of that condition required legislative changes, which took longer than envisaged to implement. It is also pertinent to note that in 1993/94, after the release of the first tranche, the IMF's ESAF programme became derailed because of the sharp deterioration in fiscal performance and the problem of cash cover arrears on donor funded imports. Most donors suspended their balance of payment assistance to Tanzania during that period.

4.5 The closing date of the loan stipulated in the Loan Agreement was 31 December, 1994, but owing to the delays in tranche release the loan closing dates had to be extended three times. The last extension was from 31 December, 1996 to 30 June, 1997.

4.6 The FSAC was closed much earlier than the FSAL. One of the reasons for this lag was that, unlike the FSAL, the FSAC was a two tranche operation. Moreover, some of the conditions were not identical. The FSAC, for instance, did not have, as a tranche release condition, the establishment of a legal framework to support the liberalization of the insurance industry. In fact, most of the conditions for the FSAC had to be fulfilled prior to Board presentation. The World Bank had from the outset planned a series of follow-up interventions to support the long-term development of the financial sector. The sequel to the FSAC was the Financial Institutions Development Project (FDIP), which was approved in 1995 to assist the Government with bank restructuring and in establishing the institutional and regulatory framework for a liberalized insurance industry and for capital market development. Hence, the the FSAL period overlapped with the implementation phase of the FDIP.

Financing Sources and Disbursements

4.7 The total financing package for the programme amounted to UA 189.22 million in form of quick disbursing balance of payment support. The sources of financing were as follows : IDA UA 150 million (79 percent), ADF-27.63 million (15 percent) UK ODA –UA 8.40 million (4 percent)-Switzerland-UA 3.19 million (2 percent). The contributions of the two bilaterals were administered as trust funds under the IDA FSAC. The first tranche of the FSAC was already disbursed when the FSAL was presented to the Board for approval. The last tranche of the FSAC was disbursed in 1994 after which IDA declared its loan closed.

4.8 The ADF Loan was disbursed in three tranches of equal amounts of UA 9.21 million. The actual dates of disbursement were May, 1993, November, 1996 and June, 1997 respectively. The SAR stipulated that the proceeds of the loan would be channelled through the OGL system that was in place at the time. With further liberalization of the foreign exchange regime, an Inter-bank Foreign Exchange Market (IFEM) was introduced, which necessitated changes in the modalities of administering donor balance of payment support. The adoption of the IFEM entailed a change in procedures, which the Bank subsequently approved. The documents required, under the new system of import support administration, consisted of Import Declaration Forms, Clean Reports of Pre-shipment Inspection Findings and Tax Assessment Notices. And in line with the recommendation of the SPA Joint Evaluation Mission (SPA JEM), all withdrawal applications forwarded to donors were required to be audited by the Tanzania Audit Corporation on a quarterly basis, and the audit reports circulated to all donors. This arrangement was introduced with the view to ensuring transparency in the utilization and accounting of donor balance of payment support, in light of the serious problem of cash cover arrears on donor commodity and import support that had emerged in 1992/93 because of weak controls.

4.9 The utilization of the proceeds of the first tranche was slow, and when the OGL system was phased out in 1994 the equivalent of US $ 7,220,508 remained unutilized in the Special Account. This balance was subsequently channelled through the IFEM with the approval of the Bank. The main reason cited by the Borrower for the slow rate of utilization of the disbursed funds was the liquidity constraints in the economy that had made it difficult for most importers to raise the 100 % cash cover required to open the letters of credit.

Procurement

4.10 The SAR and the Loan Agreement stipulated that public sector imports in excess of UA 1.38 million would be procured through International Competitive Bidding. Public contracts below this threshold were to be procured through International Shopping whereas private imports were to be procured in accordance with established commercial practices acceptable to the Fund. The Borrower complied with the stipulated modes of procurement, and all imports originated from eligible sources. All the imports financed by the Bank were below the UA 1.38 million threshold for International Competitive Bidding, and hence the modes of procurement used were International Shopping and the existing commercial practices in the case of private sector imports. The details of the imports financed under the FSAL are on the project file.

Reporting

4.11 The Borrower failed to submit quarterly progress reports on a regular basis as required by the General Conditions in the Loan Agreement. Neither were audit reports submitted regularly. The Borrower started complying with the audit requirement only after the Bank had expresssed serious concern about the violation of the General Conditions. Two audit reports by the Tanzania Audit Corporation were submitted on 23 September, 1996 and 14 November, 1997 respectively. The audit reports contained no adverse findings and certified that ; (i) the proceeds of the tranches of the FSAL were duly received and recorded in the relevant books of accounts of the BOT ; (ii) the counterpart funds generated through the sale of these proceeds were transferred to the Government's Account on a timely basis ; (iii) no imports were double financed across donors ; and (iv) the Bank's procurement rules and the negative list had been complied with.

5. OPERATING PERFORMANCE AND RESULTS

5.1 The evaluation of the programme's performance and results is provided below :-

Macro-economic Environment

5.2 There was a major slippage in macro-economic performance during the early years of the financial sector reform programme. Revenue collection fell from 16.8 percent of GDP in 1991/92 to 12.8 percent percent in 1992/93. In 1992/93 the overall budget deficit (before grants) deteriorated to 11 percent of GDP from 2.1 percent in 1991/92. The cause of the deterioration in the fiscal situation was weak tax administration, rampant tax evasion, and excessive import tax exemptions. The large fiscal deficits were financed through borrowings from the banking system and, consequently, broad money supply accelerated to 39 percent at the end of 1993. Inflation which had declined in the initial years of the ERP to around 22 percent rose to 30 percent. Because of the slippage in macro-economic performance the growth momentum of the early years of the reform period could not be sustained. Real GDP growth rate during the 1992/93-1993/94 period declined to an average of 3.7 percent from 4.7 percent in 1991/92. Annex III shows the trend in the key macro-economic indicators over the life period of the FSAL.

5.3 The agreed policy actions in the area of monetary and exchange rate reform were, nonetheless, implemented. In July, 1993 the lending rate ceiling of 31 percent was removed as a step towards full interest rate liberalization. Other actions taken included; (i) the introduction of the treasury bill auction to improve liquidity management and ; (ii) foreign exchange market liberalization.

5.4 Fiscal performance improved, from the first half of 1995/96, following the adoption of the cash budgeting system, the strengthening of tax administration and the introduction of new revenue measures. At the FSAL mid-term review, the Government had just completed a six months shadow programme with the IMF, which was followed by the approval, in November, 1996, of a new three year arrangement under the ESAF programme. Since then sound macro-economic management has been sustained.

Changes in the Financial Infrastructure

5.5 The changes in the legal and regulatory framework were implemented through the enactment of the new Banking and Financial Institutions Act (No 12 of 1991). Pursuant to the Act, various prudential and policy guidelines as well as bank licencing regulations were issued by the BOT. In addition, the Act establishing the LART was passed with the aim of providing a mechanism for the expeditious recovery and disposal of non-performing assets. Subsequent legislations included amendments to the BOT Act in 1995 and the new Insurance Act which was enacted in 1996 to open up the insurance industry to competition.

5.6 The passage of the new Banking and Financial Institutions Act of 1991 has enabled private participation in the banking industry, which hitherto, was state controlled. There are, currently, seventeen private commercial banks and nineteen non-bank financial institutions in operation including a few international banks. The changes in banking legislation have similarly enhanced the BOT's supervisory and regulatory role. The BOT's supervision unit was in 1992 upgraded to a directorate and the supervisory capacity has been gradually strengthened through staff training, external technical assistance, and computerization. [2]

Bank Restructuring

5.7 The banks that were earmarked for restructuring under the programme were NBC, CRDB, TIB and PBZ. As already noted, these banks had large non-performing loans on their balance sheets, and were grossly undercapitalized. Hence the first step in the restructuring process was to promptly restore their solvency by transferring the non-performing assets to the Loans and Advances Recovery Trust. It was envisaged that the banks would then be re-capitalized to provide them a solid base from which to proceed with operational restructuring, and compete effectively in a liberalized financial market. Private participation in the equity of these banks was also to be promoted. The outcome of restructuring of each of the four banks is assessed below :

5.8 NBC Several transactions were made as part of NBC's loan portfolio restructuring. Firstly, Tsh 18.8 billion worth of non-performing assets were in 1992 transferred to LART in exchange for bonds. Secondly, Tsh 113 billion of loan losses were written-off and offset by special government bonds. Thirdly, NBC was recapitalized to the tune of Tsh 54.6 billionby way of fresh equity (Tsh 43.6 billion in treasury bills and Tsh 11.0 billion in cash). On the operations side, the loss making branches were closed and excess staff retrenched. Furthermore, the NBC Board of Directors was reconstituted in August, 1994 and a professional management team appointed to stem the losses and turn around the bank. The rationalization of NBC resulted in the closure of 42 branches and 14 regional offices, and by 30 June, 1996 its staffing had been reduced by 3,767.

5.9 However, despite its restructuring, NBC continued incurring losses and to hinder effective competition in the banking sector because of its weak operational policies and market dominance. Consequently, further restructuring measures were adopted in 1995 which required NBC to break-even on a cash basis during the January-June, 1996 period and improve its loan portfolio by ceasing lending to the remaining non-performing borrowers

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[2] The technical assistance was provided under IDA's FSAC and FDIP

while reducing the ceiling on outstanding loans.[3] At the FSAL mid-term review in July, 1996 NBC had broken-even by raising fees and reducing costs drastically. Although loan recovery improved, the quality of NBC's new loans continued to be poor, necessitating the imposition of further prudential lending restrictions by BOT. It is worthwhile noting that after the FSAL was closed in June, 1997, a privatization strategy for NBC was developed. Pursuant to that strategy, NBC was in August, 1997 split into three banking entities; NBC Holding Company, NBC (1997) Ltd and the National Micro-finance Bank as a prelude to its privatization.

5.10 CRDB: After completion of the audit and loan portfolio review Tsh 5 billion worth of CRDB's non-performing loans were in 1992 transferred to LART. In addition, Tsh 40 billion of non-performing loans were written off and partly offset by the issuance of treasury bills. The Government also injected Tsh 2.3 billion into CRDB as equity. This capital injection, however, proved inadequate, and CRDB's capitalization remained short of the capital adequacy requirements resulting in the suspension of its lending operations by BOT for a period of time. In line with the recommendations of the Advisory Team, CRDB was reorganized through branch closures, change of management, and sizeable staff cuts to reduce operating costs. With the amendment of its Act, CRDB was in July, 1996 privatized marking the completion of the bank's restructuring. It was transformed into a full commercial bank under the name CRDB (1996) Ltd. The Bank's shares are owned by individual shareholders 41 percent, Danish International Development Agency (DANIDA) 29 percent, Cooperatives 16 percent and parastatals 14 percent.[4] CRDB's restructuring, though difficult has been successful, and the Bank is well poised to compete effectively in a liberalized banking industry.

5.11 TIB: Prior to the financial sector reforms, TIB was the main source of term financing for industrial parastatals, but over the years its loan portfolio deteriorated largely due to the inability of its clients to repay foreign exchange loans in the wake of the devaluation of the local currency during the ERP era and import liberalization. In 1993 a restructuring plan for TIB was developed by an Advisory Team and endorsed by the World Bank. The plan involved two steps namely; the recapitalization of TIB and the reoganization of the bank from a single product term lending institution to a fee-based financial services institution that would eventually be privatized. As part of TIB's restructuring, the long-term loans (mostly lines of credits from international financial institutions) were converted to equity. In addition, some of TIB's deliquent parastatal borrowers were transferred to the PSRC for liquidation. The TIB Act was then amended in 1994 to enable the Bank to undertake merchant banking functions. While TIB has been substantially restructured, it remains grossly under-capitalized and its operations restricted to debt recovery and the management of special donor funds.

5.12 PBZ: PBZ's non performing assets were transferred to LART in 1992 and the Bank recapitalized to the tune of Tsh 12 billion. In the event, the initial restructuring plan for this bank proved difficult to implement, in part, due to lack of commitment to a major reorganization of the bank by the Zanzibari authorities, which continued operating as a quasi central bank. At the FSAL mid-term review a new restructuring plan was adopted which involved; the strengthening of internal controls ; the development of a strategic business

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[3] The new restructuring measures were part of the Memorandum of Understanding signed between the Government and NBC

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plan ; recruitment of a private management team ; and the introduction of new products. Partial implementation of the plan had started, including the secondment of BOT staff to PBZ to strengthen its internal controls

Policy Linkages with the Restructuring of Banking Clients

5.13 It was envisaged that the financial sector reform would be complemented by parastatal reform. The parastatal reform programme was launched in 1992 following the establishment of the Parastatal Sector Reform Commission to oversee the process. The parastal reform progress was slow initially, partly because of the time required to put in place the privatization procedures, but when the FSAL was coming to an end the reforms had gathered momentum. As at June, 1997 about 250 out of about 400 state enterprises were divested through outtright sale, leases, management/employee buyouts, performance contracts, liquidation etc. The focus initially was on the small to medium-sized commercial enterprises, but at the time of the FSAL's closure emphasis had shifted towards major infrastructure parastatals. The parastatal enterprises that remained under government control were subjected to a hard budget constraint to ease the fiscal burden, and lending to such enterprises was strictly on the basis of their creditworthiness. Similarly, agricultural marketing boards, which were a cause of distress in the banking sector, have been dismantled. Parastatal reform has, thus, helped shape a more conducive environment for a sound banking system.

Preparation for the Development of Capital and Money Markets

5.14 Under this component, various studies were conducted with the aim of defining strategies for capital market development. Based on this analytical work the policy framework for capital market development was put in place. This was followed by the enactment of legislation in 1994 establishing the Capital and Securities Market Authority, and paving the way for opening of the Dar Es Salaam Stock Exchange.

Overall Assessment

5.15 The FSAL's most significant achievement was to establish an appropriate policy, legal and regulatory framework for a market-oriented and independent financial system. The policy and legislative changes have enabled private participation in the financial sector, while promoting the central bank's supervisory role. However, during the FSAL implementation period progress in the restructuring of the existing state-owned banks was slow, and the results limited. Perhaps not surprising, changes in banking legislation and regulations were easier to implement than bank restructuring, which required capacity building and involved staff retrenchment. The difficulty in bank restructuring was compounded by the fact that the quality of the loan portfolio in the banking industry turned out to be worse than the initial portfolio reviews had revealed. Furthermore, the incentives to promote change at the level of bank management , and the drive to improve financial performance, were lacking. The, results of the FSAL, during the implementation period, were, therefore, mixed. In its assessment of the programme, the World Bank also concluded that bank restructuring had achieved only limited success, citing the failure of the reforms to foster competition in the banking industry. However, the passage of time has brought about significant improvements in the financial sector, with the commercial banking system now entirely in the hands of the private sector following the privatization of NBC. Undoutedly, this is the result of the foundation that was laid through the changes in policy and banking laws under the programme and consolidated through the World Bank's FDIP.

6. INSTITUTIONAL PERFORMANCE

6.1 Performance of the Borrower

6.1.1 Although the programme was complex, the Borrower demonstrated a strong commitment to financial sector reform. By the time the FSAL was approved the Government had already issued new prudential regulations, and enacted new banking licencing laws to allow private participation in the banking industry. The initial portfolio reviews to assess the extent of non-performing assets in the banking system for transfer to LART had also been conducted. In addition, advisory teams to develop restructuring plans for the existing banks was already set up. These up-front actions made it possible for the Borrower to fulfill the conditions for first tranche release relatively quickly. The Borrower's performance in terms of the fulfillment of the conditions for the second and third tranche release was, however, less than satisfactory. If the Borrower had been more proactive by reporting regularly to the Bank on the status of implementation of the outstanding actions, the delays in fulfilling some of the conditions could have been minimized as they were fairly straight forward.

6.1.2 Similarly, the Borrower's compliance with the general conditions stipulated in the Loan Agreement was weak. Quarterly progress reports were never regularly submitted to the Bank. Compliance with the general conditions improved only after the Bank's mid-review mission of July, 1996.

6.2 Programme Monitoring by the Borrower

The responsibility for administering the loan was entrusted to BOT while an Inter-Governmental Group of officials comprising of the then Principal Secretaries was entrusted the responsibility of monitoring all aspects of the financial sector reforms as part of the broad economic reform programme. The monitoring of the FSAL by the Borrower proved weak as demonstrated by the irregular submission of quarterly progress reports to the ADF and delays in providing the documentation required to enable the Bank verify the fulfillment of the loan conditions. This weakness can be partly attributed to changes in staffing over the period of the loan and weak coordination between the MOF, and the BOT. It is pertinent to note that the weaknesses in loan monitoring and reporting were also highlighted in the PCRs of the previous sector adjustment operations namely ; the Sector Rehabilitation Loan and the Industrial Rehabilitation and Trade Adjustment Loan.

6.3 Performance of the Bank And Other Co-financiers

Performance of the Bank

6.3.1 Although the ADF was not involved in the design of the programme, it coordinated closely with the World Bank at the appraisal stage, and during the early years of the FSAL. Coordination took the form of exchange of documentation and information which was supplemented by the Consultative Group Meetings. Unfortunately, coordination with the World Bank during the remaining period of the FSAL, which overlapped with the World Bank's FIDP, weakened somewhat.

6.3.2 At the initial stage of the FSAL, the ADF did monitor the fulfillment of the conditions for loan effectiveness closely. The Bank’s Nairobi Regional Office, which was in existence then, certainly, helped to facilitate the follow-up of the loan. Bank performance, as measured by the frequency of supervision missions was however, unsatisfactory. Only two supervision missions were fielded by the Bank, and these were combined with other Bank missions such as the country portfolio review of 1994. Clearly, had supervision missions been more regular, the delays in fulfillment of some of the conditions would have been mitigated. The mid-term review mission of July 1996 proved very useful in resolving the outstanding issues, which facilitated the release of the second tranche.

6.3.3 The Bank was also not vigilant enough in enforcing compliance with the general conditions of the loan, particularly the reporting and audit requirement. The loan closing date was extended three times to accommodate the delays in the fulfillment of the tranche release conditions. The Bank's patience and flexibility paid-off as the outstanding conditions were eventually fulfilled and the loan was fully disbursed.

6.3.4 In their PCR, the Borrower expressed appreciation for the support provided by the Bank. The Borrower, on the other hand, felt that the Bank had been slow in responding to queries, but pointed out that Bank procedures were not well understood by the executing agency. The importance of providing training to implementing agency staff on Bank Group disbursement procedures was highlighted.

Performance of other Co-financiers

6.3.5 The World Bank, being the lead donor for the programme, was instrumental in the design and preparation of the FSAP. The institution worked closely with the GOT and the IMF in the design of the programme and putting together a financing package. The World Bank managed the funds of the two bilateral donors that participated in the programme. A portion of the FSAC (US $ 3.7 million) was allocated for technical assistance in the areas of bank supervision and restructuring to complement the assistance provided by other donors, such as USAID, Switzerland, DANIDA. The World Bank’s performance was, therefore, satisfactory.

7. ECONOMIC IMPACT OF THE PROGRAMME

7.1 It is rather early to fully assess the economic impact of the programme. The economic impact of the programme would depend to a large extent on the outcome of NBC's restructuring and privatization in terms of its impact on market interest rates and credit allocation to the real sector. Until recently, NBC remained dominant in the market (including the treasury bills market) and, because of limited competition, lending interest rates continued to be high. NBC had also not resumed normal lending operations because of the restrictions imposed by the central bank for prudential reasons. But, this notwithstanding, the programme has had some positive impact. Firstly, the quality of banking services has, generally, improved even though the activities of the new banks have been largely confined to trade financing, catering mainly for corporate clients in Dar Es Salaam and few other urban centres.. Secondly, the private sector’s share in total domestic lending has shown an increasing trend reflecting the impact of parastatal restructuring, privatization and the elimination of directed credit policies. Annex IV shows that the private sector share in commercial banks'domestic lending rose from 22 percent in 1991 to 76 percent in 1996. Thirdly, new financial and savings instruments (e.g foreign exchange deposits) have been introduced in the market implying that some financial deepening, albeit limited, has occurred. Fourthly, the role of the Central Bank in the promotion of price stability has been enhanced, which has helped reduce money supply and inflation. The rate of inflation fell from 24.8 percent in 1991/92 to 15 percent in 1996/97 and has continued to decline (see Annex III).

7.2 It is expected that the splitting and its privatization of NBC, will enhance the competitiveness of the financial sector, and improve efficiency in financial intermediation. The reduction in lending rates resulting from increased competition, combined with price stability, would in turn stimulate increased private sector investment and promote rapid growth.

7.3 The cost of restructuring the financial sector has been high. As at 30 June, 1996, Tsh 236 billion worth of securities were issued in exchange for non-performing loans and to finance the recapitalizing of banks. [5] The actual cost incurred by the Government on interest payments on LART bonds over the 1991/92-1993/94 period was Tsh 3.5 billion. This is in addition to cash injection for the recapitalization of NBC and CRDB. The cost of bank restructuring would, however, be outweighed by the longer-term benefits from the programme. The benefits are expected to be in form of the savings on the subsidies that would have otherwise been provided to loss-making banks, and the incremental fiscal revenues from the earnings of profitable financial institutions and higher economic growth.

8. THE SOCIAL IMPACT

8.1 The programme's social impact can be assessed in two ways. Firstly, in terms of the number of employees laid off as a result of bank restructuring weighed against the employment creation potential of a restructured financial sector, and secondly, in terms of the impact of the reforms on job creation in the economy in general, and the reallocation of the budgetary savings to the social sector.

8.2 The total number of employees of public owned banks made redundant by bank restructuring, is roughly estimated at 4,000, the majority of whom served with NBC. The retrenched employees were fully compensated, hence the social cost of financial sector adjustment was minimized.[6] In the long-run, however, greater employment opportunities in the economy are likely to be generated as the financial sector reforms begin to have a sustained impact on the real sector. The financial sector reforms are also likely to generate other social benefits as the budgetary savings realized are increasingly allocated to the social sector.

9. SUSTAINABILITY OF THE PROGRAMME

9.1 The financial sector reforms in Tanzania have proved to be sustainable, which is demonstrated by the Government's decision to split and privatize NBC immediately after the FSAL was closed. The Government has also committed itself to completing the restructuring of PBZ and injecting new capital in TIB, partly through private sector participation.

[5] The bonds carry interest rates of 11 percent and the redemption dates range from 2011 to 2015

[6] The GOT injected Tsh 2 billion in NBC by way of equity to cover the retrenchment cost.

Additionally, bank supervision is being further strengthened, and there are efforts to deepen the capital market by introducing a secondary market for Treasury Bills.

9.2 The fact that Tanzania has been able to sustain the financial sector reform process is a demonstration of its strong commitment to the overall reform programme. However, in order to ensure that the financial sector plays a dynamic role in the economy, the reform will need deepening. The following are some of the issues that in the next phase of the reforms will need to be dealt with:-

(i) The liberalization of the financial sector and, in particular, the restructuring of Government owned banks has created a gap in agricultural credit delivery to the detriment of small-holder farmers. CRDB which used to specialize in short and term agricultural financing has been transformed into a full commercial bank and the volume of its agriculture lending has declined. The new banks are risk averse, and unwilling to finance small holder agriculture. The Government will, therefore, need to aggressively promote rural financial and micro-credit institutions in order to stimulate higher and broad-based economic growth.

(ii) The outdated legal system in the country is an impediment to speedy loan recoveries and needs overhauling if banks are to be encouraged to increase lending to the real sector.

(iii) The cheque clearing system in the country is not well developed and inhibits bank transactions especially in rural areas where most transactions are in still in form of cash. Improving the national payment system is, thus, necessary to strengthen financial intermediation.

10. **CONCLUSION AND LESSONS LEARNT**

10.1 Conclusion

10.1.1 The programme's objective was to promote the development of a sound, market-oriented and independent financial system that would be efficient in the mobilization and allocation of resources and foster long-term growth under stable prices. This objective was to be achieved through changes in the policy, legislative and regulatory framework, bank restructuring, parastatal reforms and financial deepening through the development of money and capital markets.

10.1.2 This PCR has concluded that the programme has gone some way in achieving its objectives. The programme's most significant achievement was to establish the policy, legal, and regulatory framework required for a competitive and sound financial sector. The reforms have enabled private participation in the financial sector which, hirtheto, was entirely in the hands of the public sector. The ability of the BOT to conduct monetary policy has also been strengthened, and interest rates fully liberalized to improve efficiency in financial intermediation. Most of the commercial parastatals have been restructured, or privatized, and agricultural marketing bodies dismantled, thereby creating a more conducive business environment for banks.

10.1.3 Even though the results of bank restructuring during the programme period were limited, the programme has, nonetheless, laid the foundation for a modern, competitive and efficient banking sector. In fact, after closure of the loan the National Bank of Commerce was split into two banking entities; NBC (1997) Ltd and the National Micro-finance Bank. NBC (1997) Ltd, has been privatized and the commercial banking system is now dominated by the private sector. The FSAL was beneficial in terms of leveraging the reforms, and providing the external resource needed to sustain the reform process up to this point. Moreover, the FSAL has built-on the achievements of the Bank's earlier policy-based operations, which had contributed to the revival of growth in the Tanzanian economy in the late 1980s. Nonetheless, the Bank still has an important role to play in the long-term development of the financial sector in Tanzania

10.1.4 The PCR has identified a number of shortcomings in programme implementation, of which the major ones were weak reporting by the Borrower and weak supervision by the Bank.

10.2 Lessons Learnt

The review of completion of the implementation of the FSAP in Tanzania has brought out a number of valuable lessons for both the Bank and the Government that would be useful in improving the performance of future Bank Group policy-based operations. The key lessons are enumerated below :-

(a) The implementation of adjustment operations require close supervision and follow-up especially where there are many conditions, and the programme is relatively complex as was the case with the FSAL. It is, therefore, important that future adjustment operations are supervised more frequently, and where practicable, joint missions with the Bretton Woods Institutions fielded. This, also, has the advantage of strengthening policy dialogue with the Government.

(b) The time frame for implementing of some of the policy actions was short, and the expectation of the programme's results, rather ambitious. The lesson here is that the results of structural policy and institutional reforms in countries that are in transition to market-oriented economic systems, take time to be realized, and cannot be rushed through conditionalities. The short-term nature of quick disbursing loans, to address balance of payment constraints, needs to be reconciled with the longer time frame required to lock-in Government's commitment to reform, and ensure ownership.

(c) Where an adjustment programme is being co-financed or parallel financed the lags in disbursement between donors should be minimized to the extent possible. This can only be realized through improved coordination at both the appraisal and implementation stage.

(d) Reporting by the Borrower was weak, which, in the absence of regular bank supervision missions, made it difficult for the Bank to follow-up closely the progress in the fulfillment of the loan conditions. The ultimate solution to this problem lies in strengthening the in-country capacity to manage Bank programmes, and improving coordination between the MOF and the sectors implementing the respective reforms.

(e) Compliance with the reporting requirements was unsatisfactory and yet no action was taken by the Bank to enforce compliance. In future, the Bank needs to be stricter and systematic in its enforcement of the general conditions.

Narrative summary (NS)	Verifiable Indicators (OVI)	Means of verification (MOV)	Important Assumptions
Goal: 1. Achieve higher economic growth with stable prices	1.1 Real GDP growth of 4.5 percent and single digit inflation.	1.1 Economic surveys, national accounts and BOT economic reports.	**(Goal to Supergoal)**
Project Objectives: 1. Develop a market-oriented, and competitive financial system efficient in the mobilization and allocation of resources	1.1 Number of private banks in the financial sector 1.2 Interest rates positive and competitively determined 1.3 Range of savings and other financial instruments. 1.4 Improvement in the profitability of state banks, and reduction in ratio of non-performing loans to total banking assests 1.5 Reduction in the market share of NBC	1.1 Economic surveys, FSAL progress reports and BOT reports. 1.2 Ditto 1.3 BOT reports 1.4 Published accounts of commercial banks, and BOT reports. 1.5 BOT reports.	**(Project Object. To Goal)** 1.1 Overall economic reform programme remains on track 1.2 Macro-economic stability sustained and complementary reforms implemented. 1.3 A greater proportion of loanable funds directed to productive sectors.
<u>Outputs</u> 1. The enabling policy, legal and regulatory framework for a competitive financial sector created.	1.1 New banking laws enacted and prudential regulations issued	1.1 The new Banking and Financial Institutions Act, the LART Act and capital adequacy and prudential regulations.	**<u>(Output to Project Obj.)</u>** 1.1 Adequate budgetary allocation, to meet the recapitalization requirements of state owned banks, made.
2. Balance sheets of existing state owned banks (NBC, CRDB, TIB & PBZ) restructured to restore their solvency.	2.1 Transfer of non-performing assets to LART, loan loss write-offs and recapitalization of banks.	2.1 LART reports and financial statements of restructured banks.	
3. The legal framework to allow competition in the insurance industry put in place.	3.1 Enactment of new insurance laws and adoption of regulations allowing competition in insurance.	3.1 Economic Reports and FSAL progress reports.	
4.Existing state owned banks restructured in accordance with agreed action plans.	4.1 Reduction in staffing, branch network ationalization, and adoption of strategic business plans focusing on profitability.	4.1. FSAL quarterly progress reports; supervision mission reports; BOT reports and commercial bank financial reports.	

Narrative summary (NS)	Verifiable Indicators (OVI)	Means of verification (MOV)	Important Assumptions
5.Clients of the banking system, comprising parastatals and agricultural marketing boards, restructured or privatized.	5.1 Number of parastatals restructured and/or privatized. Subsidies to loss-making enterprises eliminated.	5.1 PSRC annual reports and FSAL quarterly progress reports.	
6. BOT's supervisory capacity strengthened.	6.1 The supervision unit in BOT upgraded to a department and modern supervision procedures and systems adopted.	6.1 BOT reports	
7. Clients of the banking system comprising parastatals and agricultural marketing boards restructured/privatized.	7.1 Parastatals restructured and/or privatized. Subsidies to loss-making enterprises eliminated.	7.1 PSRC annual reports and FSAL quarterly progress reports;	
Activities: 1.1 Preparation of new banking and insurance legislation and prudential guidelines.	Technical Assistance IDA: US$ 3.6 million Quick Disbursing Adjustment Support IDA: UA 150 million Bilaterals: ODA: GBP: UA 8.40 million: Swiss: UA 3.19 million; ADF UA 27.63 million	FSAL quarterly progress reports.	<u>Activities to Output</u> 1.1 Timely provision of technical assistance.
1.2 Audit and portfolio reviews of state banks to determine the quality of the loan portfolio and the non-performing assets for transfer to LART.		FSAL quarterly progress reports.	
1.3 Preparation of Action Plans for the restructuring of NBC, CRDB, TIB and PBZ.		FSAL quarterly progress reports.	

TANZANIA – Financial Sector Adjustment Loan (FSAL) – Policy Matrix

Policy Area & Objective	Required Actions and Time Frame	Actions Taken and Results
MACROECONOMIC FRAMEWORK		
Maintain GDP growth rates at about 4-5 percent to bring down inflation from 20 to 7 percent and reduce the external account deficit to 20 % of GDP.	Implement the 1992/94 PFP program to consolidate macroeconomic reform, and in particular maintain monetary and fiscal discipline, institute taxation and tariff reforms and fully liberalize the foreign exchange regime. Budget deficit to be further reduced to 6 percent of GDP by 1993/94.	There was slippage on fiscal targets in 1992/93 and the first half of 1993/94 due to revenue shortfalls caused by tax rate cuts and weak administration. The budget deficit fell from 2.1% in 1991/92 to 11% in 1992/93, and remained high. Fiscal discipline was restored from 1995/96 with introduction of the cash budgeting.
ENABLING ENVIRONMENT FOR FINANCIALSECTOR DEVELOPMENT		
i) Make the financial sector more competitive and autonomous to improve efficiency in financial intermediation.	Pass new Banking Act to liberalize the financial sector and allow entry of private banks.	The new Banking and Financial Institutions Act was passed in 1991, and then bank licencing guidelines issued. Seventeen private banks are in operation.
ii) Improve financial resource mobilization and allocation.	Establish the legal framework to promote competition in the insurance business.	The new Insurance Act enacted by Parliament in 1996.
iii) Strengthen monetary management.	Maintain flexible interest rates and eliminate the practice of directed credits at preferential rates	The maximum ceiling of 30 percent on lending rates was removed in 1993, and interest rates fully liberalized. Directed and subsidized credits to parastatals and cooperatives have ceased.
	Introduce treasury bill auction as a tool for indirect monetary management.	BOT Treasury bill operations introduced in 1993. 1995 Act has reinforced the central bank's autonomy in monetary management

Policy Area & Objective	Required Actions and Time Frame	Actions Taken and Results
STRENGTHENING THE FINANCIAL INFRASTRUCTURE		
i) Create an enabling regulatory environment for a competitive and autonomous financial sector.	Issue prudential regulations to ensure a sound financial system.	Prudential regulations issued in 1991, and are bieng enforced by BOT
ii) Develop an effective supervisory and regulatory capacity at the BOT to oversee the development of a dynamic banking industry.	Strengthen bank supervision through training, provision of equipment and technical assistance.	The Bank supervision unit was upgraded to a department, staff trained and equipment supplied. BOT has developed capacity in off-site and on-site supervision.
RESTRUCTURING OF FINANCIAL INSTITUTIONS		
i) Under take financial restructuring of financial institutions.	Transfer non-performing assets to LART for recovery, make provision for loan losses and recapitalize the banks.	Transfer of non-performing assets to LART completed in 1992 following portfolio review. NBC, CRDB and PBZ recapitalized through the issuance of LART bonds. CRDB was privatized in 1996. TIB awaits recapitalization.
ii) Under take an organizational and operational restructuring of the existing banks.	Reorganize the banks on the basis of the approved restructuring action plans involving branch network rationalization, staff retrenchment and business reorientation.	Banks have been restructured except PBZ.

Policy Area & Objective	Required Actions and Time Frame	Actions Taken and Results
STRENGTHENING OF MAJOR BANKING CLIENTS		
i) Liberalize agriculture marketing, which until recently, took up as much as 60 percent to bank lending and was in perpetual arrears.	Restructure marketing boards, and ensure that cooperative unions operate along commercial lines.	Marketing boards have been restructured and their role is largely regulatory. Cooperatives are now autonomous, and unviable ones have been liquated.
ii) Restructure the industrial and commercial parastatal enterprises so that they operate profitably and become creditworthy to banks.	Prepare modalities for the restructuring and privatization of parastatal enterprises. Subject enterprises to a hard budget constraint.	Modalities for the restructuring and privatization of parastatals are in place and reforms are underway. About half of the parastatals have been privatized. Public utilities have been commercialized and hard budget constraint is being enforced.
CAPITAL MARKETS DEVELOPMENT		
Develop capital markets to mobilize long-term finance to stimulate private sector investments.	Conduct studies to plan for capital market developments.	Studies and other preparatory work for capital and money development undertaken. The Capital Markets and Securities Authority Act was enacted in 1994.

ANNEX III

TANZANIA : KEY MACROECONOMIC INDICATORS : 1991/92-1996/97

	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97
GDP growth rate	4.7	3.9	3.5	3.8	4.5	4.7
Gross domestic Investment/GDP	31.3	31.3	29.4	26.6	27.7	28.0
Domestic Savings/GDP	6.9	7.2	6.2	13.2	17.3	18.2
National Savings/GDP	2.2	2.5	1.7	9.9	13.9	15.7
Government Rev/GDP	16.8	12.8	14.8	14.5	15.0	15.8
Government Rev. Incl.grants/GDP	20.0	17.3	19.2	16.9	17.4	18.9
Government Expenditure/GDP	18.9	23.8	22.7	21.4	19.9	18.1
Overall Budget Deficit (-)/GDP						
(checks issued, before grants)	-2.1	-11.0	-7.9	-6.9	-4.9	-2.3
(checks issued, after grants)	1.1	-6.4	-3.2	-4.5	-2.4	0.9
Exports real growth (goods and nonfactor services)	9.9	9.8	38.5	29.2	3.8	8.6
Exports (goods and nonfactor services)/GDP	21.3	25.8	24.2	26.3	23.4	23.9
Imports real growth (goods and nonfactor services)	8.0	8.1	25.7	1.1	0.2	4.7
Imports (goods and nonfactor services)/GDP	47.2	55.9	63.6	52.3	43.8	42.8
Debt service (US$ million)	361.5	538.3	528.6	480.4	491.9	461.7
Debt service ratio	7.9	18.3	22.2	35.2	34.7	30.0
Current account, excl. Grants (US$ millions)	-1067.7	-1114.7	-1075.8	-861.7	-674.9	-626.9
Current account/GDP (excl. Grants)	-31.7	-35.5	-30.5	-20.6	-13.1	-10.3
-Current account (US$ million) (including official transfers)	-259.0	-356.1	-442.3	-336.7	-283.0	-268.5
Current account/GDP (inc. Transport)	-6.6	-9.8	-12.5	-8.0	-5.5	-4.5
BOP overall balance (US$ million)	-179.9	-491.7	-185.7	-222.8	-169.3	-121.0
Memorandum items						
GDP (US$ million)	3996.5	3606.0	5327.1	4191.8	5157	5544.9
GDP per capita growth rate	1.7	0.8	0.6	0.9	1.6	1.8
Exports (goods and non-factor services)(US$ million)	851.3	929.2	1046.6	1365.9	1418.3	1540.2
Inflation (CPI) (average)	24.8	23.8	30.2	34.0	25.7	15.0
Gross Official reserves (weeks of imports)	16.2	10.4	10.0	8.8	8.1	9.9

ANNEX IV

Selected Banking & Monetary Statistics

End of Period	1991	1992	1993	1994	1995	1996	1997
Private and Public Shares in Commercial BankLending (in %)							
Public	74.1	59.9	46.8	29.3	37.3	23.6	57.4
Private	25.9	40.1	53.2	70.7	62.7	76.4	42.6
Distribution of Commercial BankLending by Borrowing Sectors (in %)							
Public Administration	0.3	0.4	0.4	0.3	7.5	4.2	0.6
Agricultural Production	9.6	8.4	6.6	8.4	8.1	5.3	6.4
Mining and Manuf.	21.0	20.5	38.7	25.0	21.2	30.5	33.2
Marketing of Agric Produce	36.6	26.5	25.2	25.1	19.7	11.3	14.9
Trade	13.6	28.7	5.2	29.2	20.0	17.9	17.9
Others	18.9	15.5	23.9	12.0	23.5	30.8	27.0
Interest Structure, Lending Deposit Ratios & Growth in Money Supply							
Savings Deposit rates	26.0	26.0	24.0	25.0	22.0	16.7	10.3
Short-term (31-91 days) deposit rates	16.0	16.0	17.0	17.5	23.0	17.5	14.8
Short-Term Lending Rate	25.5	24.5	26.5	33.5	36.6	37.0	25.6
Medium/LongTerm Lending Rate	26.0	30.0	30.0	31.5	35.5	33.5	28.5
Lending to Deposit Ratios	154.3	109.0	102.2	88.5	48.8	25.5	23.0
Money Supply (M2) growth	36.5	38.5	28.8	32.5	26.2	12.1	11.0
Money Supply (M3) growth	34.9	42.7	39.3	35.5	32.2	8.7	13.3

Source: Bank of Tanzania, Quarterly Economic Bulletins for June, 1996 and 1997

ANNEX V

LIST OF REFERENCES

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