PROGRAM INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

May 18, 2015
Report No.: AB7718

Operation Name	Tanzania First Business Environment for Jobs DPO
Region	AFRICA
Country	Tanzania
Sector	General industry and trade (50%); Other industry (30%); General finance (20%)
Operation ID	P150009
Lending Instrument	Development Policy Lending
Borrower(s)	MINISTRY OF FINANCE
Implementing Agency	MINISTRY OF FINANCE
Date PID Prepared	April 1, 2015
Estimated Date of Appraisal	April 27, 2015
Estimated Date of Board Approval	August 25, 2015
Corporate Review Decision	Following corporate review, the decision was taken to proceed with the appraisal of the operation.

I. Country and Sector Background

Bolstering private sector performance and improving job creation is central to the goal of achieving shared prosperity and eradicating extreme poverty in Tanzania. Helping Tanzanians obtain a secure a decent earning is the most direct and sustainable way to improve the lives of the 12 million people (28 percent of the population) currently living below the poverty line.[1]

Over the past decade, the private sector has only played a limited role in employment creation and as an engine of growth for the general economy. Economic studies have shown that growth in the 2000s has been mainly driven by consumption and current government spending and that private investment and growth has been largely concentrated in the extractive, communication, and transport sectors. These sectors will not be able to provide opportunities to a workforce that must accommodate the entry of 800,000 young people into the labor market every year and which is expected to double in size from 20 million today to over 40 million by 2030.

A strategy to support employment creation by the private sector has to be anchored on eliminating barriers to growth for small/informal businesses and on fostering investments in labor-intensive sectors. Allowing household enterprises and small firms to move out of the informal sector to more structured forms of businesses is one route to create jobs with higher productivity. In parallel, the expansion of labor-intensive industries based on Tanzania's comparative advantages, such as light manufacturing, agribusiness and tourism, is an imperative for Tanzania to create job opportunities going forward.

[1] 2011/12 Household Budget Survey (HBS). For more details, see forthcoming World Bank's Poverty Assessment.

Reducing the cost of "doing business" in Tanzania is critical to stimulate local entrepreneurship and attract foreign investors. The complicated and opaque regulatory framework, partly the legacy of a highly-regulated planned economy, generates unnecessary costs and has proven especially difficult to improve over time. Tanzania remains at the bottom of the Doing Business ranking (131 out of 189 countries); the Global Competitiveness Index ranking (125 out of 148 countries); and the Transparency International Corruption Perceptions Index (119 of 175 countries). The poor quality of the business environment is detrimental to all businesses, but international experience has shown to be more damaging to smaller ones which make up the vast majority of firms in Tanzania[2] and that lack the experience and resources to navigate through a complex business environment and deal with (or circumvent) administrative and regulatory procedures.

Private firms, including medium size ones and those operating in the formal sector will benefit from a simplified access to the basic factors of production (land, labor, and financial capital). While Tanzania is blessed with abundant factor endowments—notably vast land and a fast-growing population—several barriers and bottlenecks prevent the well-functioning of these markets and the optimal allocation of factors of production. The process for acquiring land is complicated and the procedures costly. The labor market suffers from relatively high regulations and underdeveloped cooperation between the private and public sectors, notably in the provision of training programs. Finally, access to (formal) finance—identified by Tanzanian firms as their most significant obstacle in the latest World Bank's Enterprise Survey (2013)—is low and unequal due to constraints on the demand and supply sides of the market, hampering the reallocation of savings to their most productive uses.

Beyond addressing these crosscutting issues, a competitive and job creation strategy will have to address industry-specific constraints, which have kept promising sectors, such as agribusiness and tourism from reaching their full potential. Both sectors have expanded relatively fast in recent years, building on the country's advantages and sustained global demand, but their expansion has been hampered in large part by outdated regulatory frameworks and cumbersome taxation systems.

II. Operation Objectives

The DPO revolves around three policy areas defined as "pillars": **Pillar 1 -** Making the Regulatory Environment (for business registration, licensing, trade and taxation) More "Business Friendly"; **Pillar 2 -** Improving the Functioning of Factor Markets (Labor, Land, and Capital); and **Pillar 3 -** Establishing an Enabling Environment for Competitive, Job-Creating Industries (in particular for Agribusiness and Tourism). The **PDO** of the DPO series is to increase the job creation potential of the Tanzanian private sector by reducing the overall cost of doing business and by creating an enabling environment for selected labor-intensive industries.

[2] It is estimated that approximately 3.1 million MSMEs operate in Tanzania, employing more than 5.2 million people, and contributing to about 27% of GDP.[2] Only 4% of these businesses are formally registered.

III. Rationale for Bank Involvement

This reform agenda is well aligned with the Government's Five Year Development Plan (FYDP) and the Big Results Now (BRN) initiative, and fully congruent with the current Country Assistance Strategy (CAS) and the Africa Regional Strategy. Promoting private sector development by improving the business environment is one of the objectives of the Government's National Growth and Poverty Reduction Strategy (MKUKUTA II) and FYDP. The recent BRN initiative provides a further focus, by having identified a series of concrete actions needed to upgrade the business environment for both the short and longer terms. The CAS Progress Report (July 2014) identifies a more vibrant private sector as one of the key sources of job creation and economic growth.

IV. Tentative financing

Source:		($m.)
BORROWER/RECIPIENT		0
International Development Association (IDA)		80
Borrower/Recipient		
IBRD		
Others (JICA)		TBC
	Total	TBC

V. Institutional and Implementation Arrangements

The implementation of the DPO series will be monitored by the Government and the World Bank as well as JICA. The implementation of the series has been conducted through periodic missions involving relevant GoT offices, which allow the team to obtain updated data on a regular basis. As part of an overall framework, supervision and preparation of the operations in the series take place in collaboration with other donors and in consistency with the MKUKUTA review mechanism.

VI. Risks and Risk Mitigation

The overall risk of this operation is considered to be moderate. The main risk to this operation lies in the potential lack of drive from the relevant authorities to tackle the main legal and regulatory obstacles to private sector growth, particularly in light of the upcoming elections.

Political and Governance risks. Elections will be held in November 2015, and in the past these have put pressure on the Government to increase spending to meet election promises.[3] In addition, as the election year approaches and political contestation increases, the Cabinet will be increasingly drawn to address more politically motivated issues that may delay policy decisions related to the program. There is also a potential governance risk as shown in the recent case of IPTL, the inquiry into which has still has not been fully completed. A key mitigation measure is

[3] Prior to the 2010 elections, Government spending led to major arrears in the 2011/12 budget.

the high level Government leadership commitment and the focus on BRN which should target specific areas of spending.

Macroeconomic and Fiscal risks. Among the exogenous external risks, the economy remains exposed to variations in prices on the international market, notably of food, fuel, and gold. On the domestic front, the most important risks arise from fiscal policy, including: (i) shortfalls in revenue collection while facing increased public spending, particularly from the BRN initiative and possibly from the elections; (ii) financial distress in the energy sector; (iii) contingent liabilities from Public Authorities and Other Bodies (PA&OBs); and (iv) level of debt with increased non-concessional borrowing. To mitigate against fiscal risks, the Bank will continue the macro-fiscal dialogue through the IMF program and PER process which offer the platform to monitor recent fiscal development and inform policymakers, and conduct debt sustainability diagnostics such as DSA and debt management technical assistance activities. In addition, the Bank has strategically processed a series of operations to address fiscal risk, including a Power and Gas Sector DPO and a Pension Reform DPO.

Sector Strategies and Policies Risks. Many agencies are financed through the revenues they collect from charging specific sector taxes or levies to the privates (e.g., business licenses, skills levies, certification fees, etc.). Therefore, the streamlining process and the reforms proposed under this operation are likely to be unpopular and may encounter opposition or even lead to reform reversal. Communication and stakeholders' engagement will be important mitigation measures to explain why the reforms are needed and the problems which will arise if nothing is done. The team may also discuss with the Government alternative financing sources or mechanisms for the agencies that collaborate in the reform process.

Technical Design. The DPO series has been designed to strengthen Tanzania's private sector and foster productive job creation in the country by improving the overall business environment and establishing enabling conditions that help build competitive job-creating industries. The main risk to this is that the relevant authorities may lack the drive to tackle the main legal and regulatory obstacles to private sector growth. To mitigate this risk the team will engage with the full range of stakeholders – i.e. the Ministry of Finance, the President Office Planning Commission, the Ministry of Industry and Trade, the Ministry of Labor and Employment, the Bank of Tanzania and other relevant stakeholders.

Institutional Capacity for Implementation and Sustainability Risks. Numerous implementation challenges exist in relation to the reform process, including:

i) **Institutional capacity**: some of the agencies involved in the DPO lack either the necessary resources or capacity to successfully and timely implement the proposed reforms. The World Bank can provide assistance with capacity building through the Investment Climate Advisory Services Program implemented by the Trade and Competitiveness GP. The Advisory program will complement the DPO by providing technical assistance through ad hoc analytical work, training, and technical consultancies.

ii) **Coordination:** the proposed reforms involve a large number of Government agencies, sometimes with conflicting interests in their operations (ex. TBS and TFDA). This raises an important coordination issue that needs to be addressed. A key mitigation measure will be to identify within the Government a key champion for the reform program, coordinating and synchronizing the other players, to ensure timely implementation.

iii) **Sustainability:** some of the proposed reforms risk being reversed after the end of the DPO series unless proper monitoring mechanisms are in place. In particular, the positive impact of the business-license streamlining process might be cancelled if new redundant licenses are approved. To mitigate this risk the programmatic nature of the DPO series will facilitate the sequencing and close monitoring of the reforms, thus ensuring their sustainability.

Fiduciary Risks. The overall PFM system in Tanzania remains adequate for DPOs and fiduciary risks directly related to this operation are low. However, capacity constraints in PIM and PFM continue to pose a risk in the country's PFM system. The ongoing PFMRP IV program, the PER dialogue process, the budget support dialogue, as well as the former PRSC series are important channels of dialogue and technical support to ensure that further deterioration of the PFM system does not happen. The open government partnership DPO which is currently being designed also facilitates dialogue and actions on improving public investment management, cash management, procurement and transparency in the PFM system.

Environmental and Social Risks. The specific policies supported by this programmatic operation are not expected to have negative effects on Tanzania's environment, forests, water resources, habitats or other natural resources. Tanzania has in place adequate environmental controls and legislation under the mandate of National Environmental Management Council (NEMC), providing support to line-ministries including the MoF in incorporating environmental guidelines.

Stakeholder Risks. The operation and the series require a high level of political commitment and coordination among different government agencies and stakeholders involved in the implementation of the various components. Transparency, participation, and good communication among all stakeholders are key to mitigate such risks at the national level.

VII. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

Overall, the proposed operation is expected to have positive impacts on poverty reduction in the country through its contribution to job creation and shared prosperity. The set of reforms supported by this operation and the series aim to improve investment climate in Tanzania, which will facilitate development of a competitive domestic private sector and ultimately lead to job creation—the main channel to reduce income poverty. The operation's industry focus on two labor-intensive industries, namely agribusiness and tourism, as well as its support for effective functioning of labor market and skill development, is particularly catered to this objective.

The weak private sector performance really "hits home" in an entrepreneurial economy such as Tanzania's where the vast majority of nonfarm businesses are household enterprises. They consist of self-employed people operating informal businesses as well as family members working in those businesses. Unlike large industrial firms, which have experience navigating the business environment and the resources to deal with (or circumvent) administrative and regulatory procedures, small entrepreneurs are highly sensitive to the financial cost of overcoming these obstacles. Indeed, overly burdensome procedures or regulation can make or break a small firms' business, and also deter them from entering the formal market, where they will generally have better access to capital and other factor inputs.

Some policy actions supported by this operation have specific pro-poor implications. First, streamlining business registration and licensing processes will reduce cost of doing business, particularly among micro and small enterprises. Second, several studies, including the recent study commissioned by Prime Minister Office – Regional Administration and Local Government and Ministry of Finance, show that the tax burden of agricultural cess which is proposed for reduction here, while assessed on traders of agricultural produce, is passed on to poor farmers by reducing farm-gate prices due to market power traders have. Third, greater transparency in resource allocation for rural roads development will ultimately enable the poor households in the rural sector to improve their accessibility to markets. Firm-level data in Tanzania show that micro and small enterprises face more difficulty in accessing credit. The policy actions supported by this operation and series to enhance access to finance in the country, including improved credit information system, will benefit such micro and small enterprises more than large enterprises.

Several policy actions will also have positive impacts to promote gender equity. Firm-level data also show that women entrepreneurs are disproportionately concentrated among microenterprises as opposed to medium and large enterprises. Reducing cost of doing business, including more streamlined procedures for registering businesses and access to credit, will provide a more conducive environment for female entrepreneurs to formally start their businesses. Also, streamlining land administration will lead to empowerment of women, who still suffer from application of customary law, particularly with reference to property, inheritance, and land rights in the rural areas.

Environment Aspects

The specific policies supported by this programmatic operation are not expected to have negative effects on Tanzania's environment, forests, water resources, habitats or other natural resources. The risk of unanticipated adverse effects to the environment and natural resources is low.

The existing regulatory and institutional framework in Tanzania encourages sound environmental management of investments financed through the Government budget. The Environmental Management Act of 2004 (EMA) and associated regulations require due diligence in managing environmental impacts emanating from government operations and investments. The EMA gives a mandate to the National Environmental Management Council (NEMC), under the Vice President's Office (VPO), to oversee enforcement, compliance, review and monitoring of, and compliance with, environmental impact assessments; conduct research; facilitate public participation in environmental decision-making; raise environmental awareness; and collect and disseminate environmental information. The EMA also requires each sector to establish an environmental section to ensure that sectoral operations are conducted in accordance with the law's provisions, to coordinate aspects related to the environment, and to ensure that environmental considerations are integrated into sectoral planning and project implementation (such as power generation plants).

In implementing 2004 EMA, the 2005 Environmental Impact Assessment and Audit Regulations provide the basis for undertaking Environmental Impact Assessments (EIA) and Environmental Audits for various development projects with significant environmental impacts in the country. According to the Regulations, EIA is mandatory for the following types of transport infrastructure projects under the jurisdiction of local government: construction and expansion/upgrading of roads, harbors, shipyards, fishing harbors, air fields and ports, railways and pipelines. The Regulations also require a Preliminary Environmental Assessment (screening) for rural roads under the jurisdiction of local government. All road development activities that fall under the categories mentioned above must in the first place be registered with the NEMC. Based on the Preliminary Environmental Assessment, the environmental authorities will decide whether a full EIA study is required or not. Most sectoral ministries and departments have environmental units and officers. Their capacity in terms of budget, staffing, and expertise still need to be strengthened. In response to this issue, the development funding for NEMC and for EMA implementation support program in FY2014/15 (both under VPO) has been increased significantly by 50 percent and 300 percent growth respectively from FY2013/14 actual level.

Improving transparency in resource allocation for rural roads development will contribute to better environmental management in implementing the country's rural road policy as well as its operational tool, LGTP Phase II. The Program specifies that all rural road projects (new road construction, upgrading, improvement, rehabilitation, and maintenance if maintenance work requires either opening of new borrow pits or quarries or establishment of labor camps) are subject to NEMC registration and environmental assessments. In implementing the "Removal of Bottlenecks" program under the LGTP Phase II, the Government also has adopted a more specific Environmental and Social Management Plan. In responding to the agenda of capacity building on environmental management, interventions under LGTP Phase II include: providing inputs to the preparation of transport sector environment management tools relevant for local government roads (guidelines, regulations, standards, EMP, etc); liaising with the Ministry of Works' Safety and Environment Unit on environmental training for Council and Regional Secretariat engineers and Council technicians; following-up and monitoring of environmental issues on the local government transport system; conducting training, workshops and seminars on environmental management to stakeholders; and providing equipment for environmental monitoring in the sector.

VIII. Contact point

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