Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 16-Nov-2022 | Report No: PIDA34827

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Tanzania	P178156	Tanzania First Inclusive and Resilient Growth Development Policy Financing (P178156)	
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
EASTERN AND SOUTHERN AFRICA	20-Dec-2022	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Ministry of Finance and Planning	Ministry of Finance and Planning		

Proposed Development Objective(s)

The objective of the proposed development policy operation series is to support Tanzania's inclusive and resilient recovery and growth by supporting reforms to improve the environment for private sector growth and jobs creation, strengthen public sector efficiency and transparency, build resilience.

Financing (in US$, Millions)

SUMMARY

Total Financing	500.00

DETAILS

Total World Bank Group Financing	500.00
World Bank Lending	500.00

Decision

The review did authorize the team to appraise and negotiate

B. Introduction and Context

Country Context

To reverse the downward trend in private sector activity, and promote an inclusive and resilient economic recovery,

Tanzania needs to overcome persistent challenges faced by its private sector. The challenges faced by the Tanzanian private sector, including costly practices in obtaining business licenses and permits, low access to finance, lagging regulatory environment for FDI attraction, low penetration of ICT services, and inefficient public sector transactions curbed domestic private investments and FDI inflows long before the Covid-19 pandemic and the Ukraine war. Since 2015, the number of new businesses registering in Tanzania dropped by a third, reflecting the real and perceived challenges of conducting business in the country. Similarly, FDI inflows decreased from 3.2 percent of GDP in 2015 to only 1.6 percent in 2021, lower than regional peers. With the pandemic and the war in Ukraine, these trends were aggravated: While total private investments grew by 12.3 percent each year between 2010 and 2015, and by 7.5 percent annually between 2015 and 2020, it slowed further to an estimated 4.5 percent per year by 2022.

The proposed DPO will support the Tanzanian Government's reform program aimed at boosting private sector activity, and public sector efficiency and transparency under an adequate macroeconomic policy framework. As the country's space to absorb external shocks narrows, Tanzania is advised to balance between proactive counter-cyclical monetary/fiscal policies and structural reforms. The authorities' emphasis on promoting a private sector driven recovery, improving public sector efficiency and accountability, focusing on domestic revenue mobilization, and maintaining prudence in concessional and non-concessional composition of loans reflect such an appropriate balance. This is also confirmed by the projections for key macroeconomic indicators, including a relatively low inflation rate (which shows that demand is not overstimulated in the presence of supply shocks), a controlled absorption of external shocks through the fiscal budget, and the country's stable and sustainable fiscal balances. Therefore, the macroeconomic framework of Tanzania is assessed to be adequate for the proposed operation.

Relationship to CPF

The three pillars of this DPO support directly the CPF Focus Areas 1, 2, and 3. The World Bank CPF for Tanzania identified three major focus areas and objectives. These were: Focus Area 1 (Enhance productivity and accelerate equitable and sustainable growth) , Focus Area 2 (Boost Human Capital and Social Inclusion Using a Lifecycle Approach), and Focus Area 3 (Modernize and improvise the efficiency of public institutions). These areas have been captured by the three pillars of this DPO (Pillar 1: Improving the environment for private sector-driven recovery and growth, Pillar 2. Strengthening the management of SOEs and fiscal risks and improving fiscal transparency, and Pillar 3: Boosting economic resilience). The correspondence between the CPF and DPO objectives is further elaborated by the following table.

Table 5. Correspondence between World Bank's CPF (2018) and the DPO Prior Actions

CPF Focus Areas and Objectives	Corresponding DPO Actions
1.1. Strengthen the business environment for job creation, notably in manufacturing, agri-business, and tourism	**PA#1:** Amendment of the Investment Bill to create business conditions for more domestic and foreign investments
1.2. Put credit within reach, improving access to credit particularly for MSMEs and women	**PA#2.** Amendments to the Banking and Financial Institutions Act of 2006 to enhance financial sector stability and resilience, maintain investor confidence, and ensure continued access to credit by private sector and households.
2.3. Improve the quality of healthcare and education **2.5. Promote social inclusion**	**PA#6.** Introducing universal health insurance coverage.
3.1. Strengthen public accountability and financial efficiency in delivering services	**PA#5.** Expediting arrears clearance adopting a new Arrears Management Strategy

C. Proposed Development Objective(s)

The objective of the proposed development policy operation series is to support Tanzania's inclusive and resilient recovery and growth. This will be achieved by supporting reforms to improve the environment for private sector growth and jobs creation, strengthen public sector efficiency and transparency, and boost economic resilince. Pillar 1 (Improving the environment for private sector-driven recovery and growth) supports critical business climate measures aimed at job-creating private-sector-driven growth by addressing longstanding constraints on private investment, including excessive bureaucracy, predatory taxation, limited access to finance and other inputs, and low uptake of digital solutions due to their high costs and limited access. Pillar 2 (Strengthening the management of SOEs and fiscal risks and improving fiscal transparency) support fiscal reforms to strengthen the risk monitoring of SOEs and to enhance the efficiency and transparency of fiscal operations by improving the management of arrears. Broadly, these will, in turn, bolster the resilience of Tanzania's economy to shocks and boost inclusive growth through better and more efficient provision of public services. Pillar 3 (Boosting economic resilience) focuses on (i) deepening inclusiveness (through expanding health insurance coverage), which will help protect especially the low income Tanzanian against future climate and shocks, as this group tends to be more vulnerable to weather shocks and have less access to other social safety nets, (ii) strengthening the monitoring of climate risks in the financial system and public investment projects, and (iii) building preparedness for future climate shocks by creating a farmer registry, which will facilitate timely and better targeted interventions to mitigate the adverse weather and market shocks.

Key Results

The reform actions in this DPO are expected to boost private sector activity, investments, and public efficiency and accountability, and economic resilience. Specifically, the Pillar 1 (private sector) and Pillar 2 (public sector) reforms will likely increase private investments, including FDI, increase the resilience of the financial sector, reduce Vat refunds and public expenditure arrears, and strengthen the monitoring of fiscal risks from SOEs. In comparison, Pillar 3 (resilience) will increase the sharer of population with health insurance, lead to better accounting for climate change driven risks in the financial sector and in public investment projects, and boost capacity to counteract climate shocks by registering farmers in a centralized registry.

D. Project Description

The proposed program supports Tanzania's institutional and policy reforms aimed at boosting the country's inclusive and resilient recovery by: (i) Improving the business environment for a more dynamic private sector, (ii) Strengthening public sector transparency and fiscal risk management, and (iii) Boosting economic resilience. As the first operation in a programmatic series of two, the proposed DPO for USD 500 million IDA credit from the Scale Up Window (SUW) aims to support the Tanzanian Government's reforms targeting, in the short-term, the facilitation of a private-sector led economic recovery from the compounding effects of Covid-19 pandemic and the global economic fallout from the war in Ukraine. By reducing obstacles to private investments and businesses, and improving the sustainability and credibility of public policies through greater transparency and fiscal risk management in the public sector, these reforms are also designed to provide a medium-term relief trajectory for the country's structural challenges, which have been aggravated by overlapping external shocks. Finally, following the Bank's "GRID Approach", the reforms supported by the DPO aim to raise the bar for the resilience of Tanzanian economy by reinforcing the inclusiveness of economic processes and enhancing preparedness for future shocks, especially climate-driven factors which have disproportionate effects for low income Tanzanians.

The proposed DPO will support the Tanzanian Government's reform program targeting to reduce, or remove altogether, these constraints. Pillar 1 of this program will support critical business environment measures aimed at supporting employment-intensive private-sector-driven growth by addressing longstanding constraints on private investment, including excessive bureaucracy and overlapping mandates of regulatory agencies, resulting in high costs of compliance for businesses, excessive taxation, limited access to finance and other inputs (e.g. food and agrochemicals) and facilitate enhanced stability in the financial sector and better access to credit by means of improved supervision of risks associated with climate change and of Tier II and Tier III Micro Finance Institutions (MFIs) who serve the majority of MSMEs in Tanzania. Pillar 2 will support measures aimed at streamlining public sector transactions (arrears management), enhancing transparency (public spending and fiscal risks). Pillar 3 will bolster the resilience of Tanzanian economy by increasing health insurance coverage, which is particularly important for low income Tanzanians in rural areas, whose livelihoods are more fragile against volatile weather events, and improve public ability to extend support when and where needed by creating a comprehensive farmer registry, and mandating a more explicit identification of climate risks in financial sector and public investment management system, which is a prerequisite for optimizing adaptation.

These reform efforts reflect the new Tanzanian administration's drive to accelerate structural reforms to continue the recovery and improve longer term inclusiveness and resilience. The election of Tanzania's new administration, including the country's first female president, in March 2021 has strengthened the country's resolve for reform, opening a path for renewed engagement with DPOs after a gap of several years. The new administration's policy objectives remain guided by the Tanzania Development Vision 2025 and supported by five-year development plans, however, the reform momentum has picked up. The administration's priorities are: (i) altering its COVID-19 policies to more actively manage the pandemic; (ii) proactively engaging with multilateral and bilateral partners, both in the region and worldwide; and (iii) reaffirming the private sector as the engine of economic growth by addressing major constraints on private investment. These priorities have recently been reinforced with the onset of the war in Ukraine, and the subsequent economic fallout, which is expected to affect the Tanzanian economy moderately through elevated costs of imported fuel, food and fertilizers. Within this context, Tanzanian authorities have requested from the World Bank financial assistance to support Tanzania's inclusive and resilient recovery from the adverse impact of the overlapping shocks. In parallel, the authorities have also requested a new IMF Extended Credit Facility (ECF) for US$1.046.4 billion, which was approved in July 2022.

E. Implementation

Institutional and Implementation Arrangements

Monitoring and evaluation of the reform program will be undertaken jointly by the MoFP and World Bank teams. These two teams will meet regularly to monitor progress in implementing the agreed policy and institutional reforms supported by the operation, and to assess progress made towards achieving the expected results. Result indicators have been specifically selected to reflect available data sources in Tanzania, and build on lessons learned from earlier policy based lending operations that recommend the use of simple and manageable results frameworks using available secondary sources of data.

F. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

The proposed prior actions have the potential to support inclusive growth as the reforms will create opportunities for the poor to move out of poverty. The potential elimination of the minimum investment requirement for FDI registration ($500 thousand) through the investment act, will likely affect the composition of FDI inflow towards smaller investments. These are typically more labor intensive and small in upfront capital needs and also feature higher backward/forward linkages with the host economy. Thus, by allowing more of the smaller type FDI, the authorities will likely boost employment opportunities. The investment act also reduces the eligibility of investment incentives from TIC for Tanzanian firms, enabling the smaller firms to also benefit. The PA on Micro-Finance Institutions (MFIs) would lead to more systematic reporting of financial health data (capital adequacy, NPLs etc) to the Bank of Tanzania which will help improve the MFI sector's health in the medium term. These will probably have a J-shaped effect on access to credit for poor

Tanzanians. Initially, more transparency may force the MFIs to become more timid on lending, but as the NPLs drop and the lenders' financial health improves, it will lead to a more healthy and stronger expansion of credit to micro and small entrepreneurs.

The health insurance act will provide access to affordable health care for many low-income Tanzanians. Sudden health expenses are a common phenomenon in Tanzania and these can lead to severe household distress, loss of savings and increasing debt levels, setting back a household's income earning ability for years. According to the latest NPS survey, 8 percent of households experienced a chronic or severe illness or accident in the year before the survey. The reform will enable households to insure against such risks. The Act will contain specific measures to enable the poor to obtain health insurance through (i) risk sharing and cross-subsidizing mechanisms embedded in the universal health insurance mechanism, and (ii) reductions or exemptions in contributions. None if the other reforms are expected to lead to increases in poverty. For example, improving financial performance of SOEs through better oversight will not lead to substantial lay-offs of workers. At the same time, ensuring the compliance of banks with the disclosure of climate related financial risk is not expected have negative impacts on households' access to credit. This is because a potential decrease in credits due to enhanced risk screening is likely to be offset by more explicit consideration of climate driven systemic risks, which reduce NPLs at the margin, and help alleviate the risk aversion of credit institutions in non-climate related areas.

Environmental, Forests, and Other Natural Resource Aspects

PA#7, which aims to facilitate effective management and supervision of climate related financial risk and is likely to have important climate adaptation implications. The proposed action could have the potential to open the space to maximize climate action impacts much more broadly through the economy as opposed to sectoral focus. It could also nudge along options and investment opportunities to be implemented with long-term benefits as well as shorter-term benefits in climate-sensitive (e.g., agriculture, livestock) and non-climate sensitive (e.g., mining) sectors. Effective actions here could improve efficiency in the use of resources which would complement the creation of fiscal space to finance reduction in climate vulnerability of the Tanzanian people and economy to climate shocks. Finally, this could support private sector participation at scale in terms of climate action.

PA #8, which aims to incorporate climate risks into the Public Investment Management System, is a major step towards the country's transition towards a more resilient future in light of climate risks. Requiring public investment decisions to consider climate risks and low-carbon alternatives in project selection and evaluation would (a) help to reduce inefficiencies, manage the risks climate change poses to Tanzania, and (b) enhance actions that can help avoid carbon lock-in in key public investments. Also, a key outcome of COP26 of the United Nations Framework Convention on Climate Change (UNFCCC) held in Glasgow, United Kingdom in 2021 is the renewed focus on nature-based solutions & forestry as key and cost-effective approaches to address climate change mitigation and adaptation. Tanzania has a significant forest estate but which faces key degradation pressures. Tanzania is also a biodiversity hotspot with impressive of protected areas that serve as the base for tourism and provide key climate co-benefits. This PA could support URT in promoting nature-smart and climate-informed investments and would contribute to effective climate action at local, national and global levels with significant co-benefits in terms of jobs, gender and key environmental services. Other prior actions in this DPO are not assessed to have significant direct effects on climate or environment related conditions in the country.

G. Risks and Mitigation

The overall risk rating of the proposed DPO is moderate. All risk categories are rated moderate with the exception of "sector strategies and policies" and "Institutional capacity for implementation and sustainability", which are rated substantial. Even though publicly stated, there is a risk that the level of commitment to the business environment, public investment management and arrears management reforms may change overtime. . To help mitigate the risks on the investment and business environment reforms, the Bank is in dialogue with the Government to draw up an action plan to implement the key recommendations from the Joint Government-World Bank Private Sector Assessment conducted in 2021. The Government has placed renewed emphasis on the importance of private sector in deriving the inclusive growth by increasing high-level dialogue meetings to facilitate opportunities to exchange views and taking actions resolve private sector concerns. The implementation and sustainability of the program supported by the DPO series may also face risk in terms of the ownership of the reform agenda and the capacity to implement the program. Challenges include: (i) insufficient technical capacity; and (ii) possible implementation delays due to delays in decision-making and weak institutional capacity and coordination. To mitigate these risks, several parallel technical assistance programs have been designed to increase capacity in select areas, such as for investment attraction and retention, financial sector stability, and debt management (DeMPA), by the Bank and other development partners. In addition, the multi-donor funded PFMRP VI will continue to provide support to PFM reforms.

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APPROVAL

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