I. Recent Economic Developments and Performance Under the Program

1. **Macroeconomic developments in 2003 continued to evolve broadly in line with the program (Table 2).** Despite a prolonged drought[1], which has adversely affected agricultural production, real GDP is expected to have grown by 5.5 percent in 2003, as other sectors of the economy, notably mining, manufacturing, construction, and tourism continued to grow rapidly. Inflation increased marginally, from 4.5 percent in November 2002 to 4.6 percent in November 2003, as food prices rose by 5.8 percent, while nonfood inflation declined to 1.4 percent, partly reflecting the stability of the exchange rate and of oil prices (Figure 1).

2. **In Fiscal Year (FY) 2002/03 (July-June), the overall fiscal deficit (including grants) was about 1 percentage point of GDP lower than programmed, accompanied by a substantially better-than-projected revenue performance, as well as higher-than-expected expenditure (Tables 3 and 4).** Revenue exceeded projections by 0.3 percent of GDP on account of buoyant value-added tax (VAT) and nontax revenue. Total expenditure exceeded projections by 1.2 percent of GDP, due to a higher-than-projected end-of-year catch-up in recurrent expenditures and the upward revision of development expenditures financed with foreign grants.[2]

3. **In the first quarter of 2003/04, revenue exceeded projections by 0.1 percent of GDP, as tax revenue continued to be strong, partly as a result of the implementation of measures to curtail smuggling of petroleum imports, and expenditures remained below budget.** The latter outcome mainly reflected lower-than-expected payments of interest on external debt. Net domestic financing at end-September was below the program target by about T Sh 40 billion (Appendix I, Table 1).

4. **Further progress was made in the reform of tax administration and expenditure management.** Following approval of the five-year corporate plan by the board of the Tanzania Revenue Authority (TRA) at end-June 2003, organizational and personnel steps were taken toward its implementation.[3] Also, effective July 2003, the government abolished a large number of local government taxes that had been seen as nuisance taxes by the business community. To reduce the abuse of tax exemptions and increase transparency, the government expanded the application of the treasury voucher system for the administration of exemptions from indirect taxes. In the area of expenditure management, recently

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[1] About 2 million people have been experiencing food insecurity.

[2] Foreign-financed development expenditure is based on data from the Ministry of Finance's External Finance Database, obtained directly from donors. While the Accountant General has been encouraging donors to channel projects through the government's Integrated Financial Management System (IFMS), donors have not yet responded to the extent expected.

[3] See paras. 5-6 of the LOI.

introduced codes for priority sector expenditures were utilized to monitor expenditure execution in the first quarter of 2003/04.[4] Furthermore, the Accountant General continued to prepare monthly reports on the payment of utility bills, which demonstrated that spending agencies were meeting their obligations on a timely basis. Moreover, regularly conducted audits suggest that spending agencies are not incurring arrears in other areas.

5. **Through September 2003, the Bank of Tanzania (BoT) tightened liquidity conditions substantially, with a view to meeting the established reserve money targets (Tables 5 and 6).** Reserve money and net domestic assets of the BoT remained below the June and September targets, as the BoT more stringently enforced requirements for the transfer of TRA receipts to the BoT and, in addition, actively engaged in open market operations. As a result, money supply growth at end-September remained below projections by more than 1 percentage point. The liquidity squeeze resulted in some commercial banks being unable to meet reserve requirements and led to temporarily high interest rates on the interbank market. In October 2003, the liquidity situation loosened as a result of the BoT's injection of liquidity and a drawdown of deposits by the government. Through October 2003, credit to the private sector increased (from a low base) by 40 percent, substantially above projections, fueled in part by increased competition in the banking system and the reduction in interest rate spreads.

6. **Through the first quarter of 2003/04, balance of payments developments remained in line with projections (Tables 7–10), as imports, notably petroleum imports, accelerated and export growth was in line with expectations.** International reserves substantially exceeded projections, as scheduled debt-service payments to Japan and Brazil were not made[5] and the BoT sold less foreign exchange than anticipated. The exchange rate against the U.S. dollar depreciated slightly after June 2003 to about T Sh 1070 per dollar. In real effective terms, it depreciated by about 2 percent, which combined with a modest recovery of the terms of trade, improved the environment for exports (Figure 2).

7. **Progress in structural reforms was broadly in line with the program, except that the income tax law was not submitted to parliament by end-October 2003, as envisaged,** as extensive consultations with stakeholders could not be finalized on time. On the positive side, at end-November, the names of individuals, businesses, and nongovernmental organizations (NGOs) that were granted exemptions under the treasury voucher scheme and the amounts received were published on the government's web page.[6] Also, amendments to

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[4] See paras. 8-9 of the LOI.

[5] Debt agreements with Japan and Brazil are yet to be signed. The creditors, through the Paris Club Secretariat, have extended the deadline for bilateral agreements to June 30, 2004.

[6] The authorities indicated that the publication of all statutory and discretionary exemptions (amounting to about 3 percent of GDP) was neither feasible nor served the intended purpose of this measure, which aimed at increasing transparency, and that no discretionary exemptions had been granted outside the treasury voucher scheme.

the Land Act—agreed with stakeholders—that aim at removing impediments to bank lending, were submitted to parliament for first reading in October, with approval expected in February 2004. In addition, a paper on a new, substantially simplified business licensing system has been submitted to the cabinet, and is expected to be approved in early 2004.[7] The authorities have also formulated a private sector development strategy, which they are discussing with stakeholders[8].

8. **Public enterprise reform is continuing to make progress**. The electricity utility, TANESCO, has significantly strengthened its financial performance under the guidance of a private management team, but the use of expensive thermopower-generating facilities in the aftermath of the drought is placing an unsustainable burden on the corporation and resulting in additional budgetary transfers. Also, after the takeover by a concessionaire, the financial and operational management of the water utility, DAWASA, is improving.[9] In the banking sector, following intensive consultations, parliament approved the government's privatization strategy for the National Microfinance Bank (NMB), including offering a maximum share of 49 percent to foreign investors.

II. Report on the Discussions

9. The discussions centered on (i) a review of the financial program for 2003/04; (ii) further steps to promote tax reform; (iii) emerging unanticipated spending needs; and (iv) the future agenda for financial sector reform, against the background of recommendations of the recent Financial Sector Assessment Program (FSAP).

A. Macroeconomic Outlook and Poverty Reduction Strategy

10. **The macroeconomic framework presented in the previous staff report (EBS/03/100) remains appropriate.** The authorities indicated that, with normal rainfall, a substantial recovery is foreseen in agricultural production in 2004, and that, with sustained good performance in other sectors, the projected real growth rate of 6.3 percent in 2004 is achievable. With a return to normal food supplies, the inflation rate is projected to decline to about 4 percent by end-2004.

11. **Tanzania is finalizing the third poverty reduction strategy paper (PRSP) progress report and has started consultations with stakeholders that will lead toward a comprehensive update of the full PRSP.** Mindful of the critical importance of agricultural development to reduce income poverty , the government will carry out a review of crop

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[7] Under the new system every business license is expected to be issued within one day.

[8] See para. 18 of the LOI.

[9] The drought has nonetheless resulted in severe water shortages.

boards, with a view to ending their involvement in procurement and marketing, and limiting their functions to a regulatory role. In addition, with the purpose of enhancing the availability of rural financing, the government is finalizing the implementing regulations for the legal, regulatory, and supervisory framework for microfinance institutions, and strengthening the administrative capacity for implementing the Land Act.

B. Fiscal Policy for 2003/04

12. **Main challenges in the fiscal area remain the structural reforms of tax administration and tax policy, together with a strengthening of expenditure management and of the efficiency of government operations.** In this context, the discussions focused on the next steps toward the full implementation of the TRA's corporate plan, the reform of the exemptions regime, and the new income tax law. The discussions also explored further steps to improve expenditure management and the tracking of poverty-reducing expenditure.

13. **Based on revised fiscal projections for 2003/04**, the overall deficit, after grants, is expected to be higher by 0.9 percent of GDP than that presented in the last staff report, and the projected net domestic financing requirement would be 0.8 percent of GDP, compared with the 0.4 percent previously projected.[10] The larger deficit reflects two factors: first, reflecting additional, unanticipated spending needs (detailed below), expenditure projections have been revised upward by about 1 percent of GDP; and second, based on developments in the first quarter of 2003/04, revenue is projected to be higher by 0.1 percent of GDP and donor support (program grants and loans) by 0.5 percent of GDP. Given Tanzania's low domestic debt burden, the proposed increase in net domestic financing would not adversely affect debt sustainability.[11]

14. **Two items account for more than half of the supplementary budget of TSh 157 billion, to be presented to parliament in February:** (i) the purchase of a government plane to replace the existing aircraft; and (ii) an emergency subsidy to TANESCO (0.4 percent of GDP), which in the aftermath of the drought was forced to rely increasingly on expensive thermopower generating facilities. Additional expenditures are also foreseen for contributions to the pension fund, replenishment of the Strategic Grain Reserve (SGR), the registering of voters, and payments to local governments to compensate for the abolition of a number of local taxes and fees.[12]

[10] The original projection for 2003/04 foresaw 2 percent of GDP in net domestic financing (Country Report No. 03/238).

[11] See analysis of Tanzania's debt sustainability in Country Report No. 03/2 (Chapter IV).

[12] Further details of the supplementary budget request are in the LOI, paras. 26–28.

15. **In justifying the intended replacement of the government plane, the authorities indicated that the current 28-year-old plane is no longer considered safe.** They also explained that, prior to the recent signing of a memorandum of understanding for the purchase of the plane, a comprehensive assessment of alternative options had been carried out, and that transparent procurement procedures had been followed. The staff agreed that the authorities have a legitimate need to ensure safe and efficient means of transportation. Taking into account allocations made in previous budgets, the additional cost for the plane is expected to amount to about US$40 million. In light of Tanzania's comfortable international reserves position, the staff proposed—and the authorities agreed—that the plane be financed through domestic financing. Payments for the purchase of the plane would be accommodated by adjusting the program targets for domestic financing and net international reserves. Priority sector expenditures will not be affected by the purchase of the plane.

16. **Regarding the delays in submitting the new income tax law to parliament, the authorities explained that more time for consultations with stakeholders had been required.**[13] As a result, while they would submit the law to parliament in February for a first reading, approval is expected to take place in April. The staff regretted the further delay in approving the Income Tax Law, but expressed understanding for the need to give parliament adequate time for consideration. The staff and the authorities agreed that the approval of the new income tax law was a critical step toward implementing the medium-term reform program of substantially strengthening tax administration and reining in exemptions and closing loopholes. In particular, the discretionary powers of the Minister of Finance to grant tax exemptions will only be used in emergency situations, and require prior clearance from the cabinet.

17. **Key elements in the implementation of the TRA corporate plan through June 2004 will be the integration of the Income Tax and VAT Departments** (see para. 31 of the LOI). The TRA explained its strategy of starting this integration process in January 2004 with district offices. By June 2004, the TRA plans to also integrate operations in the Large Taxpayer Department (LTD). The TRA will also steadily increase the coverage of the LTD, effective June 2004,[14] and for this purpose, recruit more auditors and other managerial staff. To further streamline administrative efficiency, the VAT threshold will be revised upward by June 2004 to reduce the number of VAT taxpayers and the remaining stamp duty on receipts will be abolished.[15] The authorities furthermore announced that they will undertake a comprehensive review of customs administration in the first half of 2004, with technical assistance from the Fund, in order to design a customs reform strategy.

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[13] Following extensive consultations with the business community, the proposed draft law was revised to introduce some limited investment incentives (para. 30 of the LOI).

[14] The initial increase would be from 100 to 200 taxpayers.

[15] The presumptive tax will be revised to avoid any reduction in the tax base.

18. **The authorities underscored their commitment to a reform of the exemptions regime as an essential element of their strategy.** To this end, and in line with the authorities' previous LOI, all government notices issued prior to 1997 will be revoked, after those that in the view of the Ministry of Finance need to be maintained have been incorporated in the relevant tax laws. As a further step, all tax laws are being comprehensively reviewed, with a view to limiting discretionary powers to grant exemptions.[16]

19. **The staff and the authorities discussed future policy concerning the licensing of operators for export processing zones (EPZs)** (see para. 20 of the LOI). The authorities explained that, in light of the EPZ's purpose as a vehicle for strengthening Tanzania's export performance and the existence of preferential trade agreements other than those for the African Growth and Opportunity Act (AGOA)/Everything But Arms (EBA) initiative markets, it would be appropriate to permit the licensing of all companies for EPZs that are in a position to benefit from preferential trade agreements.[17] The staff concurred with the authorities' view, particularly against the background of their commitment to exercising prudence by licensing only companies that export 100 percent of their output and enforcing strict regulations for EPZs that aimed at preventing leakage of products into the domestic market.

20. **The staff stressed that the front-loading of budget support as a result of the coordination with the Poverty Reduction Budget Support (PRBS) of donors and the improved predictability of disbursements should permit a relaxation of the cash-budgeting system.** It should also allow a more balanced time profile of expenditure. The authorities noted that the cash-budgeting system had been central in attaining the critical goal of sustained low inflation by containing domestic financing in the face of often uncertain timing of donor assistance. They agreed, however, that new procedures for providing donor budget support would permit enhanced flexibility in expenditure execution. To this end, they had begun to expand the process of fully funding high-priority expenditures on a quarterly basis. They also noted that, while the ratio of priority sector expenditures to GDP would increase to 10.8 percent in 2003/04, the share of these expenditures in total expenditures had remained roughly flat, reflecting partly the effect of the supplementary budget.

21. **The authorities emphasized the importance they attached to strengthening expenditure management in light of increased demands on accountability stemming from larger allocations of donor assistance to budget support.** Key measures in this area

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[16] The authorities explained that their earlier intention to completely transfer to parliament the authority to grant exemptions was not practical given the need to be able to respond flexibly to emergencies.

[17] The existing benchmark refers to companies that are exclusively oriented to export to the AGOA/EBA markets.

during 2003/04 are an expenditure-tracking study in the education sector and the preparation of an auditing procedures manual.[18]

22. **The staff also held discussions with the Zanzibari authorities.** These focused on their fiscal policy stance, following recent wage increases and poor revenue collections that had resulted in drastic compression of nonwage expenditures. The Zanzibari authorities noted the fiscal impact of the weakened economy, including sharply lower world prices for cloves and the decline in tourism following terrorism warnings, although tourism receipts had recently shown signs of recovery. The staff urged the authorities to actively address their economic and financial situation, including through the recently established Joint Finance Commission with mainland Tanzania. The Zanzibari authorities are also seeking increased donor involvement.

C. Monetary Policy and Financial Sector Reform

23. **The authorities reiterated their commitment to maintain tight reserve money management, with a view to maintaining inflation below 5 percent.** The BoT agreed that the significant liquidity squeeze experienced at end-September, which had led to a number of bank's being unable to meet reserve requirements, highlighted the need to improve banks' liquidity management, as well as the BoT's liquidity forecasting. To avoid large fluctuations in reserve money at the end of each quarter, the authorities confirmed that transfers of TRA deposits from commercial banks to the BoT would be enforced on a weekly basis. Furthermore, the BoT expected that the introduction of a Lombard facility and the signing of a master repurchase agreement by commercial banks, expected for early 2004, would further strengthen the interbank market and thus help alleviate liquidity shortages.

24. **The revised monetary program foresees a slightly higher than projected money supply growth in 2004, given the continued higher-than-expected demand for credit to the private sector and for deposits.** This higher money growth is justified because the actual velocity for June 2003 turned out lower than projected, indicating that the demand for money and financial deepening are continuing to increase in line with the ongoing development of the financial sector. In view of the higher-than-expected money multiplier, reserve money targets have remained broadly unchanged.

25. **The government has developed a comprehensive financial sector reform agenda based on the recommendations of the FSAP.**[19] The Tanzanian financial sector is sound but substantially underdeveloped by regional standards. Broadening access to financial services, developing financial institutions, strengthening financial markets, and managing the excess liquidity emanating from large-scale donor assistance and other inflows are key components of the financial sector reform agenda. The first step in implementing the FSAP proposals will

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[18]See paras. 32-36 of the LOI

[19] See paras. 39-41 of the LOI.

be the establishment, in March 2004, of an interagency, interministerial Financial Sector Reform Committee, chaired by the Governor of the Bank of Tanzania, to oversee and guide the reform process.

26. **With a view to removing restrictions that have hampered banks' flexibility, the BoT will continue to review the legal framework for lending.** In this context, the government intends to revise and amend the Bank of Tanzania Act (1995) and the Banking and Financial Institutions Act (1991), with Fund technical assistance. Following parliamentary approval of the privatization strategy of the NMB, the authorities expect to bring it to the point of sale by end-2004. The staff queried whether the new strategy, which did not permit majority ownership of the bank by a strategic foreign investor or consortium, would make the bank less attractive to prospective investors. The authorities did not expect the proposed equity shares to present a major impediment, and stressed that parliament had mandated majority local ownership in the NMB's privatization and had encouraged its continued focus on microfinance.

27. **Owing to the BoT's efforts to strengthen banking supervision, indicators of banking soundness have improved significantly over the last two years.** Notwithstanding the robust growth in private sector credit, the share of nonperforming loans has halved over the past two years (to 5.8 percent of banks' portfolio), and the capital adequacy ratio (currently 14.5 percent) has remained significantly above the threshold. The BoT has agreed to implement the recommendations of the safeguards assessment, in particular, to adopt International Accounting Standards and to have an external audit conducted in accordance with International Standards on Auditing.

D. External Outlook

28. **For the current fiscal year, the staff expects the current account deficit (excluding official transfers) to be 12.2 percent of GDP, compared with the 11.7 percent previously envisaged, reflecting higher imports of intermediate and capital goods, and a less robust increase in mining sector exports.** Traditional exports should be slightly higher, reflecting higher-than-projected export volumes. The level of international reserves is expected to exceed slightly the previous target on account of continued and large investment and donor inflows. The authorities continue to be committed to a freely floating regime, intervening only to smooth large exchange rate fluctuations.

29. **Debt negotiations with Brazil, Japan, and other creditors are proceeding,** although progress is uneven. The authorities have placed US$5 million in an escrow account to signal their readiness to settle with non-Paris Club creditors.

30. **Progress in regional integration continues within the framework of the East African Community (EAC) and through continued implementation of the Southern African Development Community (SADC) tariff reduction program.**[20] The presidents of

[20] See paras. 46-47 of the LOI.

Kenya, Uganda, and Tanzania are expected to sign the customs union protocol shortly, establishing a three-band (0, 10, and 25 percent) common external tariff (CET). Tanzania presently has four tariff bands (0, 10, 15, and 25 percent). The authorities informed the staff that the majority of goods now classified at 15 percent would fall under the new 10 percent band. However, they also indicated that the discussions have not yet been concluded. The authorities reiterated their commitment to further reduce the maximum CET from 25 percent to 20 percent within five years, if this were also acceptable to the EAC partner countries. They also expressed their interest in pursuing a code of conduct within the EAC that would help in harmonizing taxation and avoiding harmful competition on investment incentives within the region.

E. Structural Reforms

31. **The authorities are continuing to pursue the structural reform agenda.** To this end, the authorities will continue to undertake a range of measures aimed at (i) improving public enterprise performance, in particular in the energy sector; (ii) fighting corruption, enhancing transparency, and generally improving governance; and, (iii) strengthening the business environment.

32. **Discussions between the authorities and World Bank and Fund staff on the energy sector centered on the need to improve efficiency while limiting the fiscal drain from the growing subsidies for TANESCO.** Since the takeover of TANESCO's management by a private firm, its operational efficiency has improved significantly. TANESCO continues, however, to depend to a large extent on budget support, mainly stemming from capacity and operational charges for the IPTL thermopower plant. This dependency may grow further, owing to the coming onstream of the Songo-Songo plant and the costs associated with a comprehensive debt restructuring. The staff and the authorities agreed that the complex issues associated with the sector required the immediate attention of policymakers from the Ministry of Finance, the Ministry of Energy, and other agencies. In early 2004, the government and the World Bank will hold high-level discussions on the strategy for reform of the electricity sector, following which a short-term action plan will be elaborated that lays out measures in key areas, and could possibly be covered by conditionality in the next review.

33. **The government is continuing its effort to improve governance.** Quarterly updates on the National Anticorruption Strategy and Action Plans (NACSAP) continue to be published. An updated NACSAP for 2003-05 has been drafted, and an assessment report on the human and financial resources required for implementation is being prepared. The Prevention of Corruption Bureau has, however, made limited progress on investigation and prosecution, with most cases in which formal investigations were opened not leading to specific disciplinary actions. Also, anticorruption plans for local governments were not included in the 2003/04 budget, as planned, since they are still being developed. Furthermore, the government is revising the code of conduct for all public servants and putting in place a mechanism to deal with grievances concerning unethical conduct of civil servants.

34. **The authorities confirmed their commitment to further improvements in the business environment, which had already benefited from the ongoing dialogue with the business community through the Investors' Roundtable.** They noted that the recent meeting in Ngorongoro had underscored the importance of addressing the growing shortage of skilled labor, and indicated that government was planning to tackle this issue as a priority.

III. Program Monitoring

35. The program will be monitored through the quantitative and structural performance criteria and benchmarks specified in Tables 1–3 of Appendix I.[21] Submission to parliament of the new Income Tax Law is a prior action, and its final consideration by Parliament in April 2004, is an end-April 2004 performance criterion. Quantitative performance criteria and benchmarks have been set for March and June 2004, respectively, as well as a continuous performance criterion on the accumulation of external payments arrears. Structural benchmarks have been agreed for specific dates through June 2004, and a continuous benchmark on the publicizing on a quarterly basis of the names of recipients of exemptions administered through the treasury voucher system has been established. Program implementation will be assessed during the second review.

IV. Staff Appraisal

36. Tanzania's performance under the program during 2003-04 thus far has continued to be strong, driven by the authorities' high degree of commitment and the continued active support of the donor community. Macroeconomic stability has been sustained, with reasonably high growth and low inflation. In addition, significant progress has been made on structural reforms, including amending the Land Act, demonstrating the government's resolve to improve the environment for private sector activity. Notwithstanding this success, income levels in Tanzania remain very low, and poverty is widespread. Tanzania's continued progress toward the growth and poverty reduction objectives articulated in its PRSP will depend on sustained economic reform efforts, including the implementation of prudent macroeconomic policies, for many years to come. The involvement of the donor community, including the provision of financial support and technical assistance to help address capacity constraints, will be critical to assist the authorities' efforts.

37. Central to the medium-term reform program are efforts to reform the tax system, improve the efficiency and management of fiscal operations and reform the financial sector. The former objective involves broadening the tax base and limiting exemptions, which will facilitate the mobilization of higher revenue and thus strengthen the robustness of

[21] Structural conditionality covers broadly the same areas as those discussed in Box 6 of Country Report No. 03/238.

macroeconomic stability and limit aid dependency. The authorities have made a strong start in implementing the comprehensive reform plan set forth in the recently approved TRA corporate plan. The approval by parliament of the new income tax law, planned for April 2004, the launching of key administrative reforms, as well as strict control of exemptions, are critical first steps toward accomplishing the program's ambitious medium-term objectives. It will be crucial that the authorities rigorously pursue these efforts on a timely basis. In addition, the planned inclusion of fiscal terms of mining agreements exclusively in tax laws will be a critical step to rationalize the tax regime for mining companies. Effective use of technical assistance to help build capacity at the TRA will also be essential.

38. The authorities' efforts to improve accountability and strengthen the effective management of resources are central to their plans to improve absorptive capacity. In this respect, the staff welcomes the authorities' progress in implementing the assessment and action plan aimed at improving the tracking of poverty-reducing expenditure, and their efforts to strengthen auditing and procurement procedures. Of particular importance in this area will be the expenditure-tracking studies that are planned for the current fiscal year. The trend by donors to increasingly channel assistance in the form of program support gives added urgency to the authorities' efforts.

39. The staff notes with concern the rising the fiscal pressures emanating from the growing subsidies for the energy sector and urges the authorities to give high priority to the design and implementation of a comprehensive strategy for the sector. In addition to improving the reliability of the supply of electricity—a critical factor for the business environment—the strategy should aim at establishing the sector's financial sustainability.

40. The staff welcomes the authorities' resolve to address the issue of further reform of the financial sector, as evidenced by their response to the FSAP. In view of the breadth of the reform agenda, establishment of a high-level interministerial, interagency committee to guide the reform agenda is an essential first step. The authorities should also give high priority to the timely completion of the privatization of the NMB, the largest bank in terms of deposits and branch networks, which should facilitate higher access to bank lending in rural areas, and hence enable the financial sector to play a more constructive role in growth and poverty reduction.

41. The staff welcomes the authorities' commitment to closer regional integration in the context of the East African Community. The common external tariff that is being adopted may lead to some liberalization of Tanzania's trade regime. In order to boost efficiency and sustain progress in this area, the staff urges the authorities to pursue with their EAC partners as soon as possible further tariff reductions, particularly for the maximum tariff, and reduce nontariff barriers. The authorities should also pursue efforts to better align EAC tax regimes.

42. The dialogue with the business community has increased the momentum for improving the business environment. Nonetheless, shortcomings in the business environment in Tanzania remain pervasive, and will require the continued engagement of the authorities to attain the level of investment required to sustain and, it is hoped, accelerate the rate of increase in real per capita incomes. The staff fully supports the authorities' strategy for

improving the business environment, including through enhancing the infrastructure. In this area, it will be critical to identify priority projects to improve transport and utilities, which have been persistent concerns of the business community. The staff furthermore urges the authorities to intensify their anticorruption efforts as a crucial element to improve governance and business confidence.

43. Based on the authorities' continued record of good program implementation and their commitments made in the attached letter of intent, as well as the temporary nature of nonobservance of the performance criterion, the staff recommends that the Executive Board grant a waiver for the nonobservance of the structural performance criterion on submission to parliament of the income tax law and complete the first review under the current PRGF arrangement.